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2024

Contracts & Other Obligations • Trade & Commerce

VOLUME 6

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ANNOTATIONS
to the
MONTANA CODE ANNOTATED

Legislative Services Division
Jerry Howe, Executive Director

Code Commissioner & Legal Services Director
Todd M. Everts

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Joe Carroll
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Layout & Distribution
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Published and Distributed by
Montana Legislative Services Division
Capitol Bldg Rm 110 — 1301 E 6th Ave
PO Box 201706
Helena MT 59620-1706
Telephone (406) 444-3064 Fax (406) 444-3036
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CONTENTS

Volume 1

Table of Session Law to Code — 2023
Table of 2022 Ballot Issues to Code
Official Report of the Montana Code Commissioner — 2023
Enabling Act
Constitution of Montana
Title
1. General Laws and Definitions

Volume 2

Titles
2. Government Structure and Administration
3. Judiciary, Courts
4. Reserved
5. Legislative Branch
6. Reserved
7. Local Government
8 and 9. Reserved
10. Military Affairs and Disaster and Emergency Services
11 and 12. Reserved
13. Elections
14. Reserved

Volume 3

Titles
15. Taxation
16. Alcohol, Tobacco, and Marijuana
17. State Finance
18. Public Contracts
19. Public Retirement Systems
20. Education
21. Reserved
22. Libraries, Arts, and Antiquities

Volume 4

Titles
23. Parks, Recreation, Sports, and Gambling
24. Reserved
25. Civil Procedure

Volume 5

Titles
26. Evidence
27. Civil Liability, Remedies, and Limitations

Volume 6

Titles
28. Contracts and Other Obligations
29. Reserved
30. Trade and Commerce

Volume 7

Titles
31. Credit Transactions and Relationships
32. Financial Institutions
33. Insurance and Insurance Companies
34. Reserved
35. Corporations, Partnerships, and Associations
36. Reserved
37. Professions and Occupations
38. Reserved

Volume 8

Titles
39. Labor
40. Family Law
41. Minors
42. Adoption
43. Reserved

Volume 9

Titles
44. Law Enforcement
45. Crimes

Volume 10

Titles
46. Criminal Procedure
47. Access to Legal Services
48. Reserved

Volume 11

Titles
49. Human Rights
50. Health and Safety
51. Reserved
52. Family Services
53. Social Services and Institutions
54-59. Reserved
60. Highways and Transportation
61. Motor Vehicles
62-66. Reserved
67. Aeronautics
68. Reserved
69. Public Utilities and Carriers

Volume 12

Titles
70. Property
71. Mortgages, Pledges, and Liens
72. Estates, Trusts, and Fiduciary Relationships
73 and 74. Reserved
75. Environmental Protection

Volume 13

Titles
76. Land Resources and Use
77. State Lands
78 and 79. Reserved
80. Agriculture
81. Livestock
82. Minerals, Oil, and Gas
83 and 84. Reserved
85. Water Use
86. Reserved
87. Fish and Wildlife
88 and 89. Reserved
90. Planning, Research, and Development
91-99. Reserved

PREFACE TO VOLUME 6
(Annotations — September 2024)

Annotations to this volume include:

Case notes of applicable court decisions through:
- public domain citation 2023 MT 177
- volume 413 Montana Reports page 356
- volume 535 Pacific Reporter (3rd Series) page 1133

Digests of Montana Attorney General's opinions through:
- volume 59 opinion number 1 of the Report and Official Opinions of Attorney General

Amendment notes listed under compiler's comments are intended to explain only amendments made in the year indicated and may not accurately reflect current statutory language because of subsequent amendment.

The annotations are provided as a convenience to the user and are not intended to be an exhaustive compilation of the law under a given statute or in a given area.

TITLE 28
CONTRACTS AND OTHER OBLIGATIONS

CHAPTER 1
OBLIGATIONS IN GENERAL

Part 1
General Provisions

28-1-101. Definitions.

Case Notes

Restaurant Did Not Breach Lease — Prohibition of Music and Cooking Odors Not Reasonable — Anticipatory Breach by Landlord: The plaintiff, a restaurant that leased space from the defendant, initiated a declaratory action after receiving a notice of default of the lease for not abiding by rules that had been added to the lease that required the restaurant to eliminate cooking odors and prohibited music. The District Court found that the plaintiff did not breach the lease and the defendant anticipatorily breached the lease because it violated the implied covenant of good faith and fair dealing and interfered with the plaintiff's right to quiet use and enjoyment of the premises. On appeal, the Supreme Court affirmed, holding that the defendant's rules prohibiting music or cooking odors were not reasonable or fair to the plaintiff restaurant. As such, the defendant's actions interfered with the plaintiff's quiet enjoyment of the premises, the defendant anticipatorily breached the contract, and the plaintiff did not default on the lease. Bridger Del Sol, Inc. v. VincentView, LLC, 2017 MT 293, 389 Mont. 415, 406 P.3d 460.

Oral Notice Held Sufficient When Written Notice Required: The plaintiff argued that the defendant had breached the contract by giving oral notice of cancellation when the contract required written notice. The Supreme Court, while distinguishing this decision from its ruling in Tomsheck v. Doran, 126 M 598, 256 P2d 538 (1953), held that the notice given by the defendant substantially complied with the contract terms and that the plaintiff was not prejudiced by the action. Comphealth, Inc. v. Highland View Outpatient Surgical Center, 240 M 366, 783 P2d 1385, 46 St. Rep. 2198 (1989).

Oral Lease as Contract Establishing Obligations: An oral farm lease under which both parties recognized and fulfilled responsibilities relating to crop sharing, farming methods, and farm subsidy programs for 15 years was a sufficient contract through which each party acquired its respective obligations and breach of which formed a proper basis for award of damages and costs of suit. Albers v. Bar ZF Ranch, Inc., 229 M 396, 747 P2d 1347, 44 St. Rep. 2081 (1987).

Where Payment Alone Does Not Constitute Performance: Performance of a contract is the doing of the things promised to be done, and while the obligation may be for the delivery of money only, in which event performance is called "payment", where the contract calls for the doing of various things (as did the contract in the instant case, payment being one of them), payment alone would not constitute performance. Hardenburgh v. Hardenburgh, 115 M 469, 146 P2d 151 (1944).

"Payment" — Promissory Note: In absence of agreement, either express or implied, providing otherwise, "payment" means the discharge of a debt or obligation in money; hence mere delivery and acceptance of promissory note for amount of an account, whether it be note of debtor or of another, do not operate to discharge debt. Gallaher v. Theilbar Realties, 93 M 421, 18 P2d 1101 (1933).

Tort Liability: Statutory definition of an obligation includes the liability for actionable tortious conduct. Barbarich v. Chicago, Milwaukee, St. Paul & Pac. Ry., 92 M 1, 9 P2d 797 (1932).

Payment by Way of Credits — Pleading: A plea of payment by defendant in an action for money due means payment in money. Therefore, where payment under an agreement to accept something other than money in satisfaction of an obligation is asserted, it must be specially pleaded; when not so pleaded, evidence of payment made by way of credits other than cash is inadmissible. Billings v. Missoula White Pine Sash Co., 88 M 322, 292 P 714 (1930), overruled on another point by Caird Eng'r Works v. Seven-Up Gold Min. Co., 111 M 471, 111 P2d 267 (1941).

Quasi-Contract: Where one has received money which, though not bound to do so by express contract, he in equity and good conscience ought to turn over to him from whom he received it, the law implies a promise on his part to that effect, and the obligation thus created or implied by law is termed a "quasi-contract", as distinguished from a contract as defined in 28-2-101 and

28-2-102. Schaeffer v. Miller, 41 M 417, 109 P 970 (1910), distinguished in Keith v. Kottas, 119 M 98, 172 P2d 306 (1946).

28-1-102. How obligations arise.

Case Notes

Oral Lease as Contract Establishing Obligations: An oral farm lease under which both parties recognized and fulfilled responsibilities relating to crop sharing, farming methods, and farm subsidy programs for 15 years was a sufficient contract through which each party acquired its respective obligations and breach of which formed a proper basis for award of damages and costs of suit. Albers v. Bar ZF Ranch, Inc., 229 M 396, 747 P2d 1347, 44 St. Rep. 2081 (1987).

Lack of Appeal of Federal Agency Decision Not to Affect Contract Rights: Popp had an oral agreement to plant and harvest land owned by Frank and Gountanis. Popp attempted to enroll the land in the federal payment in kind program (PIK) but was informed by the Agricultural Stabilization and Conservation Service (ASCS) that he must have a written lease to be eligible. He never appealed the ASCS decision. Frank later contended that the failure to appeal precluded Popp from collaterally attacking that determination in District Court. The Supreme Court held that Popp's filing of a lawsuit was not a collateral attack on the ASCS decision but rather that the amended complaint showed it was a breach of contract action. The court supported the finding that the PIK program could not be used to destroy Popp's contract rights. Popp v. Gountanis, 221 M 267, 718 P2d 340, 43 St. Rep. 801 (1986).

Proper Quantum for Architect's Services: Under a contract with a landowner who wished to build housing units on the land, an architect prepared plans and specifications that were approved by landowner. Under the contract, the architect was to receive 5% of the construction cost. Following abandonment of the project, he was entitled to a fee based on quantum meruit. The proper recovery was the number of hours of service, 600, times the architect's hourly rate, $30, or $18,000. It was improper for the court to hold that the architect was entitled to only $10,000 based on the value of his services. Kenneth D. Collins Agency v. Hagerott, 211 M 303, 684 P2d 487, 41 St. Rep. 1375 (1984).

Obligation to Third Party Where No Privity Exists: A prime contractor contracted separately with a steel supplier to supply steel and with a subcontractor to erect the steel. Because the supplier was delayed in delivering the steel, the subcontractor suffered financial losses. By entering into the contract with the prime contractor, the supplier placed itself in such a relation with the subcontractor that the law will impose upon the supplier an obligation, sounding in tort, to act in a way so as not to injure the subcontractor. Privity of contract is not required. Hawthorne v. Kober Constr. Co., 196 M 519, 640 P2d 467, 39 St. Rep. 294 (1982), followed in Tynes v. Bankers Life Co., 224 M 350, 730 P2d 1115, 43 St. Rep. 2243 (1986), and in Jim's Excavating Serv., Inc. v. HKM Associates, 265 M 494, 878 P2d 248, 51 St. Rep. 623 (1994), in which it was held that a third-party contractor may successfully recover for purely economic loss against a project engineer or architect when the design professional knew or should have foreseen that the particular plaintiff or an identifiable class of plaintiffs was at risk in relying on the information supplied.

Account Stated — What Constitutes: The basic ingredients of an account stated are an agreement that the items of the account and the balance struck are correct and an express or implied agreement for the payment of the balance. Implied agreement for the payment of the balance may be presumed where there are a course of dealings, an antecedent indebtedness, and retention of a statement of the account for an unreasonable length of time without objection. Johnson v. Tindall, 195 M 165, 635 P2d 266 (1981), followed in Mattson v. Julian, 209 M 48, 678 P2d 654, 41 St. Rep. 544 (1984), and in Able, Inc. v. Kuzara, 241 M 155, 785 P2d 1021, 47 St. Rep. 158 (1990).

Where Contractual Obligation Not Assumed by Defendant, Suit for Breach Wrong Remedy: Where receiver of vendor company assigned contract of sale to another company without assumption by the latter of the vendor's obligation thereunder and assignee sold the property to a third person subject to the rights of the deceased owner's estate, in a suit for breach of contract against the assignee company by the personal representatives of the deceased purchaser, judgment for plaintiff was erroneous in absence of proof that defendant had assumed the obligations of the vendor. Under the facts, the assignee became a trustee for the original vendee by operation of law. Thompson v. Lincoln Nat'l Life Ins. Co., 114 M 521, 138 P2d 951 (1943), followed, with regard to lack of implied assumption of contractual obligations absent assignment of contractual rights, in Davey v. Nessan, 252 M 397, 830 P2d 92, 49 St. Rep. 294 (1992).

28-1-103. What rules govern interpretation of contracts and other obligations.

Case Notes

Application of Banking Standards, Not Livestock Industry Standards, to Loan Transaction Involving Cattle — Bank-Customer Relationship Not Giving Rise to Fiduciary Responsibilities: A bank loaned money to a couple to fund their cattle breeding operation. When the couple failed to make loan payments, the bank brought an action to collect and foreclose, and the couple brought a counterclaim that the bank's actions breached the covenant of good faith and fair dealing and the bank's fiduciary duty toward the couple. After the couple paid the amount owing, they became the plaintiffs and the case proceeded on the breach of covenant and fiduciary duty claim. The District Court granted the bank summary judgment on the claim, and on appeal, plaintiffs asserted that the court improperly applied banking standards to the case rather than livestock industry standards, constituting a breach of good faith. The Supreme Court disagreed. In Montana, the relationship between a bank and its customer is generally described as that of debtor and creditor and does not give rise to fiduciary duties except when special circumstances place a bank into the role of adviser. In this case, the bank acted as a creditor and not an adviser, and did not force the cattle sale but simply sought to enforce the repayment provisions of its contract with plaintiffs, so no special circumstances existed. The bank acted in accordance with the contract provisions and comported with prudent banking policy and reasonable commercial standards. It was appropriate for the District Court to apply commercial banking standards to the analysis of the bank's relationship with plaintiffs and plaintiffs' ability to service their loans. Summary judgment for the bank was proper. McCoy v. First Citizens Bank, 2006 MT 307, 335 M 1, 148 P3d 677 (2006).

Defendant Not Allowed to Characterize Damages: Shilhaneks were injured in a vehicle accident, and defendants were ordered to pay more than $3 million in damages, including punitive damages. Defendants requested that the $750,000 tendered to Shilhaneks to date be allocated toward payment of the punitive award and that Shilhaneks be required to file a corresponding satisfaction of judgment with respect to the punitive damages award, in essence asserting that a defendant has the power to specifically designate payment toward a particular award. Defendants cited 25-9-311 for the rule that a satisfaction of judgment must be provided by the party in whose favor judgment is entered and contended that under 28-1-1106 and 28-1-1225, the power lies with the debtor, not the creditor, when it comes to designating to which particular obligation a payment should be credited. The District Court denied the request, noting that Title 28 applies only to contractual obligations and that Title 25 governs obligations arising from judgments. The District Court did not abuse its discretion, given defendants' failure to provide a legal basis that would allow them to dictate how damages owed are characterized, the fact that defendants owed more than double the available insurance coverage and were obligated to pay the policy limits to satisfy the verdict, and that allocating 22% of the available insurance proceeds to the punitive damage award would have harsh tax consequences on Shilhaneks. Shilhanek v. D-2 Trucking, Inc., 2000 MT 16, 298 M 101, 994 P2d 1105, 57 St. Rep. 89 (2000).

28-1-104. Relief from forfeiture.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

General 3
Equity 4
Payments — Recovery and Tender 6
Real Property 7
Procedure 8

GENERAL

Doctrine of Election of Remedies Inapplicable — Position of Blameless Party After Contractual Breach — Making Whole but No More: The plaintiff brought a suit for damages 6 years after the defendants breached a contract to buy the plaintiff's interests in Dealerspan, LLC, a software company, resulting in the defendants' forfeiture of their interests in Dealerspan. Defendants argued that the doctrine of election of remedies barred damages because the plaintiff elected to pursue forfeiture and thus had rescinded the contract. However, the subject of the contract was the sale of the plaintiff's interests, and the forfeiture of the defendants' interests in Dealerspan did not return the parties to their original positions before executing the contract, so the forfeiture and contractual damages were not inconsistent. Nevertheless, the contract was not designed to place the plaintiff in a better position under the defendants' breach than under the defendants' performance, so the plaintiff could recover only damages covering the difference between the contract purchase price and the value of the forfeited interests, subsequent profits from the business, and profits from selling Dealerspan's physical assets. Bottrell Family Investments Ltd. Partnership v. Diversified Financial, Inc., 2015 MT 185, 379 Mont. 504, 352 P.3d 620.

Notice-Prejudice Rule Applicable in First Party Insurance Coverage: The notice-prejudice rule applies to first party insurance coverage disputes. Under this rule, an insurer may deny coverage based on an insured's failure to comply with a policy notice provision only if the insurer can demonstrate that it was prejudiced by the late notice. Estate of Gleason v. Cent. United Life Ins. Co., 2015 MT 140, 379 Mont. 219, 350 P.3d 349.

Forfeiture on Deed to Purchase Property: Good faith efforts to raise money for installment payments excuse element of grossly negligent, willful, or fraudulent breach of duty. Parrott v. Heller, 171 M 212, 557 P2d 819 (1976).

Repurchase of Stock: Forced sale of shareholder's stock pursuant to repurchase agreement and board of directors' resolution to exercise option to repurchase stock at 50% of book value was not a harsh forfeiture within meaning of this section where the shareholder was allowed, as a fringe benefit, to encourage participation in corporate affairs and to purchase the stock for less than one-half of book value and where he had agreed to the terms of the repurchase agreement whereby the corporation could buy back the stock at 50% of book value in the event of termination of his employment. State ex rel. Howeth v. D. A. Davidson & Co., 163 M 355, 517 P2d 722 (1973), overruled, with regard to elements of collateral estoppel, in Dagel v. Great Falls, 250 M 224, 819 P2d 186, 48 St. Rep. 919 (1991).

Unjust Enrichment: Under this section, when there is a forfeiture the vendee has a cause of action against the vendor for unjust enrichment. Greenup v. U.S., 239 F. Supp. 330 (D.C. Mont. 1965).

Inability to Pay Caused by Strike: Conditional buyers were not entitled to relief from forfeiture of conditional sales contract because of their inability to make payments required by contract due to a widespread strike. Kovacich v. Metals Bank & Trust Co., 139 M 449, 365 P2d 639 (1961).

Willful Breach: This section explicitly points out that if the breach is willful there will be no relief from forfeiture, and no common-law principle can override this exacting statutory provision. Joy v. Little, 138 M 110, 354 P2d 1035 (1960).

Full Compensation Required: Under a lease arrangement the tenant agreed to pay a percentage of the sales over $270,000, in addition to a stipulated monthly rent, and the lease provided for a forfeiture in the event of a breach. The court could give relief against forfeiture under this special statute upon the tenant making full compensation. The forfeiture was claimed on the fact that the tenant did not pay a percentage of the sales of farm implements which were kept in a separate building, although all the sales were made and money received at the leased premises and a controversy arose as to whether such sales should be included in that amount upon which a percentage was paid as rent. Gamble-Skogmo, Inc. v. McNair Realty Co., 98 F. Supp. 440 (D.C. Mont. 1951), affirmed in Moyer v. Comm'r of Internal Revenue, 193 F2d 876 (9th Cir. 1952).

Application of Section — Option: This section was inapplicable where option to purchase did not create an obligation on part of holder of option and option had been terminated at time of commencement of action involving option. N. Min. Corp. v. Cooke Min. Co., 123 F2d 9 (9th Cir. 1941).

Forgetfulness No Excuse: In an action against a corporation to enforce the immediate forfeiture of a contract of purchase for the vendee's failure to make any deferred payment, the corporation is not entitled to any relief on the ground that its officers were so engrossed with other business that they forgot that a payment was due on the contract, especially where time has been made of the essence in the contract. Fratt v. Daniels-Jones Co., 47 M 487, 133 P 700 (1913).

EQUITY

Affirmative Action in Curing Default — Relief From Forfeiture Warranted: After missing a payment when purchasing property from the Ackers, the Quigleys took affirmative steps to cure the default and eventually tendered full compensation for their obligation. These actions showed that the default was not a grossly negligent, willful, or fraudulent breach of duty. In light of other financial factors beyond the Quigleys' control and the fact that forfeiture could have resulted in unjust enrichment for the Ackers, the District Court did not err by applying this section in granting the Quigleys relief from forfeiture. Quigley v. Acker, 1998 MT 72, 288 M 190, 955 P2d

1377, 55 St. Rep. 295 (1998), distinguishing Kovacich v. Metals Bank & Trust Co., 139 M 449, 365 P2d 639 (1961), and Aveco Properties, Inc. v. Nicholson, 229 M 417, 747 P2d 1358 (1987).

Grant of Equitable Relief From Forfeiture — Conditions: Defendant defaulted on a contract to operate a coal mine. The District Court granted summary judgment, finding no genuine issue of material fact regarding defendant's unlawful detainer. Defendant sought equitable relief pursuant to this section. The Supreme Court may, under appropriate circumstances, equitably relieve a party from the harsh effects of a forfeiture. Circumstances warranting equitable relief must not only meet the statutory requirements of tendering full compensation within a reasonable time after service of notice of default and not acting in a grossly negligent, willful, or fraudulent manner, but the party seeking relief must also assert facts that appeal to the conscience of the court of equity. Mere financial inability is not sufficient to appeal to the court's conscience. In this case, defendant's request for equitable relief was deficient because it did not meet statutory and common-law criteria, so the grant of summary judgment was affirmed. Glacier Park Co. v. Mtn., Inc., 285 M 420, 949 P2d 229, 54 St. Rep. 1222 (1997), following Kovacich v. Metals Bank & Trust Co., 139 M 449, 365 P2d 639 (1961), distinguishing Parrott v. Heller, 171 M 212, 557 P2d 819 (1976), and followed in Weter v. Archambault, 2002 MT 336, 313 M 284, 61 P3d 771 (2002).

Appeal to Equity: Under this section a person may be relieved against a forfeiture in any case where he sets forth facts which appeal to the conscience of a court of equity. Blakely v. Kelstrup, 267 M 274, 883 P2d 814, 51 St. Rep. 991 (1994); Greenup v. U.S., 239 F. Supp. 330 (D.C. Mont. 1965); Kovacich v. Metals Bank & Trust Co., 139 M 449, 365 P2d 639 (1961); Estabrook v. Sonstelie, 86 M 435, 284 P 147 (1930).

Forfeiture — Affirmative Defense: Forfeiture is an affirmative defense and must be pleaded in the defendant's answer to a complaint. It will not be considered for the first time on appeal. Massar Cattle Co. v. Reese, 216 M 22, 699 P2d 87, 42 St. Rep. 609 (1985).

Gross Negligence in Failure to Perform — No Relief From Forfeiture: The seller of real property is entitled to cancellation of a contract for deed. The purchasers are not entitled to any equitable relief from forfeiture because they were grossly negligent in failing to perform in accordance with the terms and provisions of the contract. Redinger v. French, 216 M 16, 699 P2d 94, 42 St. Rep. 604 (1985).

Full Compensation to Be Shown: This section cannot be applied where there is nothing to show that one claiming the benefit of it made full compensation. Hares v. Nelson, 195 M 463, 637 P2d 19, 38 St. Rep. 2036 (1981). See also Burgess v. Shiplet, 230 M 387, 750 P2d 460, 45 St. Rep. 293 (1988).

Deposit in Court — Right to Relief: In action to prohibit defendant from canceling an agreement for sale of lands, even though the deposit in court might be legally insufficient as a tender to defendant, plaintiff might be relieved from forfeiture upon a showing of facts sufficient to appeal to the conscience of a court of equity. Blackfeet Tribe of the Blackfeet Indian Reservation v. Klies Livestock Co., 160 F. Supp. 131 (D.C. Mont. 1958).

Free From Blame: Lessors of an oil and gas lease sought to have the lease set aside for failure of lessees to drill more wells. Lessors, however, had refused to allow lessees to enter the land. The court held that one who seeks to enforce a forfeiture must be free from blame even though oil and gas leases are generally construed against the lessee. Fey v. A.A. Oil Co., 129 M 300, 285 P2d 578 (1955).

Mistake: Where a purchaser of realty on deferred payments relied on a supposed breach of a contract of sale by the vendor, based on a fairly debatable point, and mistakenly refused to make further payments, in an action by the vendor to terminate the contract with forfeiture of payments, equity properly relieved purchaser from such forfeiture. Huston v. Vollenweider, 101 M 156, 53 P2d 112 (1935).

Seeker of Equity — to Do Equity: This section is based upon the principle that he who seeks equity must do or offer to do equity; to obtain relief he must, by his allegations and proof, bring himself within its purview. Clifton v. Willson, 47 M 305, 132 P 424 (1913). See Donlan v. Arnold, 48 M 416, 138 P 775 (1914).

Sale of Personalty: One who, after making advance payments on a contract of sale of personalty, refuses to complete the transaction, the seller being ready and willing to fulfill its stipulations, cannot recover them unless he can bring himself within the exception provided by this section by alleging and proving facts and circumstances upon which, in equity and good conscience, he should have relief from the forfeiture and which excuse him from the imputation of gross negligence or willful or fraudulent breach of duty. Clifton v. Willson, 47 M 305, 132 P 424 (1913). See Donlan v. Arnold, 48 M 416, 138 P 775 (1914).

Showing of Entitlement: A party may be relieved from a forfeiture under this section upon a showing that he is equitably entitled to such relief, if his breach of duty was not grossly negligent, willful, or fraudulent. Fratt v. Daniels-Jones Co., 47 M 487, 133 P 700 (1913), distinguished in Roberts v. Morin, 198 M 233, 645 P2d 423, 39 St. Rep. 892 (1982); Cook-Reynolds Co. v. Chipman, 47 M 289, 133 P 694 (1913).

PAYMENTS — RECOVERY AND TENDER

Waiver of Contract Rights — Late Payments Not Considered Breach Based on Prior Acceptance: The uninsured employers' fund (UEF) sought indemnity from an employer that did not have workers' compensation insurance using a monthly payment arrangement that was agreed to by the parties. The UEF accepted four late payments before turning the employer over to collections, at which point the employer sued UEF for breach of contract. The Supreme Court held that UEF waived its right to terminate the contract based on late payment when it accepted late payments without objection. Consequently, it was a breach of contract for the UEF to turn the employer over to collections and the employer was entitled to damages. Elk Mtn. Motor Sports, Inc. v. Dept. of Labor and Industry, 2012 MT 261, 367 Mont. 36, 289 P.3d 165.

Offer of Full Consideration Required: Restitution on the grounds of relief from forfeiture was not appropriate absent an offer of full consideration. Schweigert v. Fowler, 240 M 424, 784 P2d 405, 47 St. Rep. 1 (1990).

Forfeiture to Land in Which No Right Exists — Tender of Full Compensation — Affirmative Defense: Sun Dial purchased land and under an agreement turned possession of the land over to Gold Creek. Gold Creek intended to divide the land into 20-acre parcels for sale as homesites. The planned homesite sale did not materialize, and Sun Dial filed suit to regain possession of the land. A settlement was reached on the day set for trial that required Gold Creek to pay Sun Dial $1.3 million within 1 year of the settlement. Payment was not made, and the court ordered judgment for Sun Dial's immediate possession of the property. The Supreme Court held that this was not a forfeiture. Sun Dial purchased the land and held equitable title. Defendants never had title to the land and therefore cannot forfeit something they never had. In addition, 28-1-104 requires that Gold Creek tender full compensation. The only amount tendered was $50,000, a far cry from $1.3 million. Moreover, a forfeiture is an affirmative defense, which was not affirmatively pleaded by Gold Creek. Sun Dial Land Co., Inc. v. Gold Creek Ranches, Inc., 198 M 247, 645 P2d 936, 39 St. Rep. 908 (1982), followed in Eigeman v. Miller, 229 M 28, 745 P2d 320, 44 St. Rep. 1752 (1987).

Contract for Deed — Payment Offered — Forfeiture Denied: Roberts purchased real property from Morin on a contract for deed. Roberts then sold the property to Iverson on another contract but retained an interest in the original contract until Iverson's obligation to him was satisfied. Iverson failed to make payment to Morin, and Morin sent him a notice of default. No notice was sent to Roberts, but when he learned of the default, he offered to cure. Morin refused the offer, seeking instead to enforce the forfeiture provision of the contract to regain the property, which had greatly increased in value. On appeal, the Supreme Court directed the District Court to deny the forfeiture and allow Roberts to make full payment of the balance due on the Morin contract. Roberts v. Morin, 198 M 233, 645 P2d 423, 39 St. Rep. 892 (1982).

Relief From Forfeiture of Equity Under Contract for Deed: The buyers and sellers entered into a contract for deed under which the buyers made a downpayment and monthly payments and agreed to make a balloon payment at the end of the contract term. The buyers failed to obtain financing of the balloon payment due to no fault of their own and thereby defaulted on the contract but entered into settlement negotiations with the plaintiffs and later tendered payment of amounts due to the plaintiffs, plus the plaintiffs' personal expenses and attorney's fees. Under these circumstances, the antiforfeiture statute would prevent the forfeiture of the defendants' downpayment and monthly payments. The defendants' actions were not intentional, willful, or fraudulent. These facts present a clear case for the application of the antiforfeiture statute. Sharp v. Holthusen, 189 M 469, 616 P2d 374, 37 St. Rep. 1651 (1980), followed in Daugherty Cattle Co. v. Gen. Constr. Co., 254 M 479, 839 P2d 562, 49 St. Rep. 820 (1992), Blakely v. Kelstrup, 267 M 274, 883 P2d 814, 51 St. Rep. 991 (1994), and Club Buffet Bar, Inc. v. Lilienthal, 268 M 164, 885 P2d 526, 51 St. Rep. 1231 (1994).

Competing Policy Considerations Balanced — Oral Real Property Agreement: Section 28-1-104 strikes a balance between the competing policy considerations of encouraging enforcement of agreements though technically deficient (Statutes of Fraud in this case) and the tendency not to favor needless forfeitures. The lower court's balancing in the direction of the former consideration was supported by the evidence. Fraser v. Edmisten, 189 M 443, 616 P2d 360, 37 St. Rep. 1607 (1980).

A purchaser of real property under an oral agreement who voluntarily terminates the contract cannot recover partial payments on the purchase price so long as the seller is willing and able to perform his part of the agreement. Perkins v. Allnut, 47 M 13, 130 P 1 (1913).

Downpayment: Where a $500 downpayment was made on the purchase of land and the balance of $700 was to be paid under the terms of an escrow agreement by a specified date and purchaser failed to pay balance by such date, after which seller sold to another, such first purchaser was entitled to the return of the $500 downpayment. Herman v. Herman, 123 M 39, 207 P2d 1155 (1949).

Tender of Delinquent Payments: Where the vendee of county-owned property was in default in payments on principal and taxes under his contract of purchase dated November 1934, making time of its essence, the county, in 1940, after notice and declaration of forfeiture, brought suit to quiet title. In view of defendant's tender of the full amount of delinquent payments, interest, and taxes at the trial, and of the difficulty for the average person to make loans due to economic conditions, and in the absence of circumstances which would have rendered relief inequitable, the trial court erred in denying relief from forfeiture under this section. Yellowstone County v. Wight, 115 M 411, 145 P2d 516 (1943).

Time of the Essence Clause: A defaulting purchaser of land, under a contract which made time of the essence and under which the vendor exercised his option to declare it ended upon breach, who had made no downpayment and had paid only the first year's interest during his 2 years' possession, was not entitled to recover what he had expended on the premises, under this section. Edwards v. Muri, 73 M 339, 237 P 209 (1925).

When Payments May Be Recovered: Where a purchaser has failed to make payments according to the terms of his contract but has made some partial payments before his breach of the contract, he cannot ordinarily recover the payments made before the breach, nor can he under any circumstances recover them without alleging and proving that the default was not the result of his "grossly negligent, willful, or fraudulent breach of duty". Suburban Homes Co. v. North, 50 M 108, 145 P 2 (1914). See Mont. Williams Double Diamond v. Royal Village, Inc., 186 M 359, 607 P2d 1120 (1980).

REAL PROPERTY

Default Notice in Compliance With Contract for Deed — No Mention of Fees and Costs: A provision in a contract for deed set out additional fees to be paid to the escrow agent in case of default, but when the default notice was sent, there was no mention of the additional fees. Plaintiffs contended that failure to mention the fees rendered the default notice defective. The Supreme Court disagreed. The notice sufficiently complied with the provisions of the contract. Defendants properly followed the default procedure set out in the contract, and excluding the fee information did not render the default notice defective. Danelson v. Robinson, 2003 MT 271, 317 M 462, 77 P3d 1010 (2003).

Enforcement of Acceleration Clause: Defendant purchased real property from the plaintiff for $1.4 million, with $350,000 as a downpayment and the balance payable in nine equal annual payments at 8¼%. The downpayment was made, but the first annual payment was missed. Plaintiff sent two notices of default and notice of an intent to accelerate the entire unpaid balance. The District Court concluded that the acceleration may be tantamount to forfeiture, and courts look with disfavor on forfeitures. On appeal, the court held that the plaintiff was seeking specific performance, not forfeiture. Even if a forfeiture were involved, 28-1-104 could not help because the statute relieves a party from a forfeiture upon "making full compensation to the other party". SAS Partnership v. Schafer, 200 M 478, 653 P2d 834, 39 St. Rep. 1883 (1982), followed in Aveco Properties, Inc. v. Nicholson, 229 M 417, 747 P2d 1358, 44 St. Rep. 2098 (1987).

Showing Required for Relief From Forfeiture of Real Estate Contract: Plaintiff seller sought cancellation of a contract for sale of real property and eviction of defendant buyer upon buyer's default. Upon tender of full payment by defendant, the lower court dismissed the complaint. The Supreme Court reversed, holding that under this section it is only when the defaulting purchaser can make a showing that he is equitably entitled to relief from forfeiture and that his default was not grossly negligent, willful, or fraudulent that the courts will relieve purchaser from forfeiture. Case remanded for further proceedings. Ponderosa Pines Ranch, Inc. v. McBride, 197 M 301, 642 P2d 1050, 39 St. Rep. 577 (1982), followed in Blakely v. Kelstrup, 267 M 274, 883 P2d 814, 51 St. Rep. 991 (1994). See also Stuart v. U.S., 109 F3d 1380 (9th Cir. 1997), for preemption by federal law.

Tax Liens: Any federal tax lien on property that accrues because of the vendee's delinquency attaches to the amount of unjust enrichment if the mortgagee's claim is prior in right. Greenup v. U.S., 239 F. Supp. 330 (D.C. Mont. 1965).

Farm Lease — Hardship Considered: Plaintiffs brought an action to terminate a farm lease for failure to perform according to its terms. The court held that although tenant had not plowed all the acreage required and had plowed some land which plaintiffs had wanted intact, he had substantially complied with the lease. The court relieved the tenant from forfeiture of the lease and restored him to his former estate in order to avoid hardship. Table Mtn. Farms v. Burton, 128 M 434, 278 P2d 213 (1955). See also Smith & Satterfield v. Zepp, Farner & Knowles, 173 M 358, 567 P2d 923 (1977).

Questionable Title to Real Estate: In an action in ejectment by the vendors of a tract of land against the vendee for refusal to complete the contract of purchase, the questions raised by the latter regarding the title offered were fairly debatable but found not meritorious, and as the time for making final payment had expired, the case was one justifying application of the rule for relief against forfeiture under this section. Williams v. Hefner, 89 M 361, 297 P 492 (1931).

Gross Negligence or Willful Breach: Notwithstanding the provision in a contract of sale of ranch land that on default of deferred payments all prior payments should be deemed forfeited as rental, the party in default may obtain relief from forfeiture if not guilty of grossly negligent, willful, or fraudulent breach of duty, on presentation of such grounds therefor as appeal to the conscience of a court of equity. Fontaine v. Lyng, 61 M 590, 202 P 1112 (1921). See also Christensen v. Hunt, 147 M 484, 414 P2d 648 (1966).

Retention of Title by Vendor: Where a vendor retains the legal title to property sold to a purchaser, who defaults in meeting deferred payments, and an action is brought to enforce a forfeiture caused by such default, 71-3-109 and 71-3-1301 are not pertinent. There is no lien, and therefore there is no basis for denying a forfeiture of the contract of sale. Cook-Reynolds Co. v. Chipman, 47 M 289, 133 P 694 (1913).

PROCEDURE

Construction Lien Foreclosure Against Commercial Building Contractor — Finding That Contractor Caused Delays by Not Cooperating in Resolving Conflicting Contractual Requirements — Final Judgment in Favor of Plaintiff Truss Supplier Affirmed. Truss Works v. Oswood Constr. Co., 2022 MT 42, 408 Mont. 27, 504 P.3d 1116.

No Factual Issue of Waiver Under Contractual Consent to Assignment Clause — Summary Judgment Proper: The Nicholsons entered a contract option with J.G.L. Distributing (JGL) that gave JGL 5 years to purchase the Nicholsons' property. The option contained a consent to assignment clause that required JGL to obtain the Nicholsons' written consent before assignment to a third party. JGL subsequently assigned an interest in the property to plaintiff but did not notify the Nicholsons. Plaintiff spent money improving the property but missed a payment. The Nicholsons then notified JGL that the option expired and that they intended to sell the property to someone else. Plaintiff sued JGL and the Nicholsons, JGL counterclaimed against plaintiff and filed cross-claims against the Nicholsons, the Nicholsons counterclaimed against JGL, and all three parties moved for summary judgment. The District Court dismissed plaintiff's claim because plaintiff was not a party to the contract. The court also held that the consent to assignment clause was valid and enforceable, but that even though JGL breached the agreement by not notifying the Nicholsons of the assignment and by missing a payment, the breach was not material and did not serve to terminate JGL's right to exercise the option. The court then concluded that forfeiture would be too harsh a remedy, excused the forfeiture, and granted JGL 20 days to pay the Nicholsons the full purchase price. On appeal, the Supreme Court affirmed. Plaintiff failed to show a genuine issue of material fact that the Nicholsons waived their rights under the consent to assignment clause. The breach of contract by JGL was incidental rather than material, so the District Court's holding that forfeiture would be too harsh was not erroneous. Thus, the District Court correctly applied the antiforfeiture statute when it granted JGL equitable relief under this section because JGL's breach was not grossly negligent, willful, or fraudulent. It was only when the Nicholsons discovered that they could sell the property at a greater profit that they acted to strictly enforce the timely payment provision of the contract, so application of the antiforfeiture statute was appropriate to avoid an unjust result. R.C. Hobbs Enterprises, LLC v. J.G.L. Distrib., Inc., 2004 MT 396, 325 M 277, 104 P3d 503 (2004). See also Erban v. Monforton, 227 M 531, 740 P2d 677 (1987), Norwood v. Serv. Distrib., Inc., 2000 MT 4, 297 M 473, 994 P2d 25 (2000), and VanDyke Constr. Co., Inc. v. Stillwater Min. Co., 2003 MT 279, 317 M 519, 78 P3d 844 (2003).

Appeal Raising Section's Application for First Time: Appellant against whom forfeiture of a contract for deed was granted for failure to make payments could not have Supreme Court review of the application of this section where he did not raise applicability of the section at trial. Hares v. Nelson, 195 M 463, 637 P2d 19, 38 St. Rep. 2036 (1981). See also Massar Cattle Co. v. Reese, 216 M 22, 699 P2d 87, 42 St. Rep. 604 (1985).

Ambiguous Notice: Where vendor brought action to recover possession of realty and the notice of forfeiture was ambiguous and attempted to accelerate payment to an amount almost twice that which could be rightfully demanded and the total amount of the forfeiture was twice the rental value of the property, the vendor's notice did not terminate the vendee's rights under the contract and the District Court should have granted vendee's motion to dismiss under former Rule 41(b), M.R.Civ.P. (now superseded). Shuey v. Hamilton, 142 M 83, 381 P2d 482 (1963).

Judgment of Forfeiture Not Sought: Where, in an action for the cancellation of a land contract for breach of its conditions by the vendee, the vendor does not seek a judgment of forfeiture but waives any claim to damages and prays only for possession after default and notice, giving ample opportunity to repair the default as provided in the contract, the provision of this section that where a party incurs a forfeiture by reason of his failure to comply with the provisions of his contract he may be relieved therefrom upon making full compensation to other party has no application. Huffine v. Lincoln, 87 M 267, 287 P 629 (1930).

Insufficient Statement of Facts: While courts are reluctant to enforce forfeitures and conditions involving them must be strictly interpreted against the party for whose benefit they are created, where a purchaser of farmland, under a contract which made time of its essence and provided that in case of default in the stipulated payments the purchaser should forfeit his right to possession and all payments made as liquidated damages, remained in possession for 10 years without any complaint, and then finding himself unable by reason of conditions beyond his control to meet the final payment notified the vendor of his inability to make payment and of his desire to surrender the land, the contract was declared forfeited. Furthermore, his complaint in his action to be relieved of the forfeiture, asking recovery of the difference between the payments made by him under the contract, with taxes, insurance, cost of improvements made by him, and the value of the rental of the property, was held insufficient to state facts which appeal to the conscience of a court of equity and therefore insufficient to state a cause of action under this section. Estabrook v. Sonstelie, 86 M 435, 284 P 147 (1930).

Improper Complaint: To entitle a defaulting purchaser to relief from forfeiture under the provisions of this section, he must set forth facts which will appeal to the conscience of a court of equity. Hence, a complaint intermingling allegations appropriate to an action for rescission of contract and one for breach of it was properly held insufficient as one for relief from a forfeiture, for failure to allege willingness by plaintiff to do equity even by payment of rent for 7 years of occupancy of farmlands. He on the contrary demanded recovery of the whole amount paid defendant, including taxes paid during that time. Friedrichsen v. Cobb, 84 M 238, 275 P 267 (1929).

Essential Allegations: Where a purchaser of property seeks to avoid forfeiture of an advance payment incurred by reason of his failure to complete his contract, he must, under this section, allege and prove that his default was not the result of his grossly negligent, willful, or fraudulent breach of duty, and failure to do so deprives him of the right to invoke the rule. Ellinghouse v. Hansen Packing Co., 66 M 444, 213 P 1087 (1923).

Law Review Articles

Forfeiture of Payments Under a Land Purchase Contract in Montana, Jacoby, 19 Mont. L. Rev. 50 (1957).

Part 2
Obligations Imposed by Law

28-1-201. General duty of care.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

Case Notes

General 10
Implied Covenant of Good Faith 25
Injury to Person 32
Injury to Property 44

GENERAL

Public Duty Doctrine Inapplicable: The plaintiff sued the city of Columbia Falls for negligence, premises liability, breach of professional duties, and wrongful death after her husband died following a skateboarding accident on a subdivision walking path, the design of which the city had monitored and approved. The District Court applied the public duty doctrine and granted the city summary judgment. On appeal, the Supreme Court reversed. The public duty doctrine does not apply when a governmental defendant has a specific duty to a plaintiff arising from generally applicable principles of law that would support a tort claim, i.e., if a private person would be liable to the plaintiff for the acts that were committed by the government, then the governmental entity would be similarly liable. Because the city was actively involved in the design of the walking path and exercised its statutory and contractual authority to approve it, the city could be held liable for violation of a statutory duty and the voluntary assumption of a duty to act with ordinary care; therefore, the District Court erred in applying the public duty doctrine. Kent v. Columbia Falls, 2015 MT 139, 379 Mont. 190, 350 P.3d 9.

No Evidence to Support Malicious Prosecution or Abuse of Process Claim — District Court Dismissal of Attorney Deceit Claim Improper: In a suit for malicious prosecution, abuse of process, and attorney deceit, the District Court did not err by granting judgment in favor of the defendant on the malicious prosecution claim or by awarding summary judgment to the defendant on the abuse of process claim when the plaintiff failed to prove the elements necessary to establish the claims. The plaintiff failed to prove malicious prosecution when, for purposes of establishing probable cause, all of the parties reasonably believed the facts gave rise to a valid claim. The plaintiff also failed to prove abuse of process despite his allegations that the ulterior purpose of the suit was to coerce him into paying damages. Payment of damages is a legitimate purpose for a civil action, and no facts existed to demonstrate that the defendant acted with an improper ulterior purpose. However, the District Court erred by granting summary judgment to the defendant on the attorney deceit claim when a trier of fact could find that the defendant acted deceitfully with the intent to deceive opposing counsel. Spoja v. White, 2014 MT 9, 373 Mont. 269, 317 P.3d 153, following Plouffe v. Dept. of Public Health and Human Services, 2002 MT 64, 309 Mont. 184, 45 P.3d 10, Hughes v. Lynch, 2007 MT 177, 338 Mont. 214, 164 P.3d 913, and Judd v. Burlington N. & Santa Fe Ry. Co., 2008 MT 181, 343 Mont. 416, 186 P.3d 214.

Causation in Legal Malpractice Claim — Summary Judgment Not Proper — Plaintiffs Not Required to Show Claim Would Have Been Successful: An attorney missed a statute of limitations deadline in a medical malpractice case by failing to file an application with the Montana Medical Legal Panel before filing a complaint in District Court, as required under 27-6-301 and 27-6-701. After the medical malpractice claim was dismissed, the plaintiffs filed a legal malpractice case against the attorney, but the District Court dismissed the legal malpractice case during summary judgment on the grounds that the plaintiffs did not carry the burden of showing that the underlying medical malpractice claim would have been successful. On appeal, the Supreme Court revisited Busta v. Columbus Hosp. Corp., 276 Mont. 342, 916 P.2d 122 (1996), Babcock Place Ltd. Partnership v. Berg, Lilly, Andriolo, & Tollefsen, P.C., 2003 MT 111, 315 Mont. 364, 69 P.3d 1145, and Fisher v. Swift Transp. Co., Inc., 2008 MT 105, 342 Mont. 335, 181 P.3d 601, and determined that it was error for the District Court to require the plaintiffs to prove that the medical malpractice case would have been successful given that there was no independent intervening cause after the plaintiffs' injury. All that was required was a showing that the plaintiffs' injury (not being able to pursue the case) would not have occurred but for the attorney's negligent conduct. Labair v. Carey, 2012 MT 312, 367 Mont. 453, 291 P.3d 1160. On remand in Labair v. Carey, 2016 MT 272, 385 Mont. 233, 383 P.3d 226, the Supreme Court determined that the plaintiffs more probably than not would have recovered a settlement. Thus, the plaintiffs were entitled to judgment as a matter of law on this first element of settlement damages.

Public Duty Doctrine Inapplicable for City Playground Injury: The public duty doctrine did not apply in a negligence claim against a city for the failure to maintain a playground area given the applicability of clear and established rules of premises liability. Based on an analysis of foreseeability, it was reasonable and proper to hold the city to a duty to exercise reasonable care in maintaining its public parks. Gatlin-Johnson v. Miles City, 2012 MT 302, 367 Mont. 414, 291 P.3d 1129, followed in Kent v. Columbia Falls, 2015 MT 139, 379 Mont. 190, 350 P.3d 9.

Proper Venue for Malicious Prosecution Claim Considered County Where Breach of Duty and Damages Occur: Plaintiff filed a malicious prosecution claim in Missoula County, alleging that defendant intentionally and maliciously filed and prosecuted an unsupportable federal cause of action in that county. Defendant moved for a change of venue, but the District Court concluded that Missoula County was a proper venue and denied the motion. On appeal, the Supreme

Court affirmed. Defendant's purported breach of duty occurred upon filing the claim in Missoula County, and plaintiff incurred damages in that county, so the concurrence of breach and damages in Missoula County supported the District Court's conclusion that Missoula County was a proper venue for the malicious prosecution claim. Deist v. Thornton, 2009 MT 21, 349 M 94, 201 P3d 800 (2009). See also Carter v. Nye, 266 M 226, 879 P2d 729 (1994).

No Special Relationship Between City and Residents to Protect Residents in Vicinity of Proposed Building Modification Based on Public Duty Doctrine: The city of Hamilton passed zoning ordinances that included a master plan for providing services and the orderly development of property. When the city approved a casino that bordered a residential zone, neighbors eventually complained about the noise and general nuisances surrounding the casino business. When the city did not respond to the neighbors' satisfaction, the neighbors sued the city on grounds that the ordinances imposed a special duty on the city to protect the residents pursuant to the public duty doctrine expressed in Nelson v. Driscoll, 1999 MT 193, 295 M 363, 983 P2d 972 (1999). The District Court determined that under the doctrine, neither the city nor its officials owed any special duty to the neighbors when passing the master plan or when deciding whether to take action to abate the alleged nuisance, and summary judgment was granted to the city. On appeal, the Supreme Court affirmed. The court noted that the doctrine generally provides that when a municipality owes a duty to the general public, that duty is not owed to any particular individual unless a special relationship exists, under an exception set out in Nelson, thus giving rise to a special duty that is more particular than that owed to the public. A special relationship is established: (1) by a statute intended to protect a specific class of persons, of which the plaintiff is a member, from a particular type of harm; (2) when a government agent undertakes specific action to protect a person or property; (3) by governmental actions that reasonably induce detrimental reliance by a member of the public; and (4) under certain circumstances when the agency has actual custody of the plaintiff or of a third person who harms the plaintiff. In this case, the master plan was clearly adopted for the benefit of the general public and did not create a special relationship between the city and the neighbors, so the city had no special duty to protect the neighbors from any harm that might result from the city's adoption of the plan. Because no genuine issue of material fact existed regarding a special duty required of the city, summary judgment was proper. Prosser v. Kennedy Enterprises, Inc., 2008 MT 87, 342 M 209, 179 P3d 1178 (2008), distinguished in Kent v. Columbia Falls, 2015 MT 139, 379 Mont. 190, 350 P.3d 9.

No Finding of Malicious Prosecution, Abuse of Process, or Tortious Interference in Employment Discrimination Claim — Judgment as Matter of Law Proper: Lynch filed an employment discrimination claim against doctor Hughes for sexual harassment actions that Hughes took in a hospital in which Lynch was employed. The Commission for Human Rights determined that Hughes was not an employer or agent of an employer, so Hughes did not bear an employer's liability for sexual harassment. Hughes' behavior after Lynch filed the claim was determined to constitute illegal retaliation, but because Lynch did not claim retaliation, the claim was dismissed. Hughes then filed an action in District Court alleging malicious prosecution, abuse of process, and tortious interference. The court found that the claims could not be proved and granted Lynch judgment as a matter of law. Hughes appealed, but the Supreme Court examined each claim and affirmed. First, Hughes could not prove that there was a lack of probable cause for Lynch's action or that the proceeding favored Lynch, so the malicious prosecution claim failed. Second, nothing in the record showed that Lynch used abuse of process to coerce Hughes to do some collateral thing that Hughes could not be legally and regularly compelled to do, so the abuse of process claim also failed. Third, there was no evidence to suggest that Lynch's acts were calculated to damage Hughes, and Lynch was entitled to seek redress and damages for the alleged discrimination, so the tortious interference claim failed as well. Thus, the District Court correctly determined that no genuine issue of material fact existed and that Lynch was entitled to judgment as a matter of law. Hughes v. Lynch, 2007 MT 177, 338 M 214, 164 P3d 913 (2007), following Plouffe v. Dept. of Public Health and Human Services, 2002 MT 64, 309 M 184, 45 P3d 10 (2002), and Comm'n on Unauthorized Practice of Law v. O'Neil, 2006 MT 284, 334 M 311, 147 P3d 200 (2006), and followed in Judd v. Burlington N. & Santa Fe Ry. Co., 2008 MT 181, 343 M 416, 186 P3d 214 (2008), with regard to applicability of the probable cause standard for a malicious prosecution claim.

Application of Improper Paint to Water Treatment Center Pipes — Definition of Physical Injury in Context of Commercial General Liability Insurance Contract: Plaintiff entered a contract with the city of Libby for construction of a water treatment plant. Plaintiff then entered a subcontract with defendant to paint the filter tanks and pipes at the plant. Plaintiff was listed as an additional insured on defendant's commercial general liability insurance policy. Defendant used an improper paint, and the city sued plaintiff as the general contractor for repainting costs. The insurer refused to defend or indemnify plaintiff, claiming that policy exclusions precluded coverage for the city's claim. Plaintiff successfully argued in District Court that the exclusions applied only to defendant as the named insured. On appeal, the Supreme Court considered whether the policy language referring to physical injury to tangible property covered the application of improper paint, concluding that the policy applied. Physical injury refers to a physical and material alteration resulting in a detriment. The policy covered property damage, including loss of use, and application of the improper paint physically and materially altered the tanks and pipes, resulting in a detriment to the city. The District Court was affirmed. Swank Enterprises, Inc. v. All Purpose Serv., Ltd., 2007 MT 57, 336 M 197, 154 P3d 52 (2007), following Lindsay Drilling v. USF&G, 208 M 91, 676 P2d 203 (1984).

Summary Judgment on Negligence Claim Affirmed Absent Showing of Breach of Duty of Care: Bonilla claimed that the University of Montana was negligent in providing a chair at a concert that Bonilla attended when the chair broke and Bonilla was injured. Ordinarily, the determination of whether a defendant breached a legal duty is not susceptible to summary judgment unless the evidence is undisputed or susceptible to only one conclusion by reasonable people. However, Bonilla failed to produce any evidence explaining how or why the chair broke and whether it was due to the breach of any duty by the University. Bonilla never reported the incident, so the University had no record of the incident. The only evidence offered to support a negligence claim was Bonilla's own testimony that the chair would not have broken unless there was a problem with it. University officials explained their policy of assuring the safety of their chairs and of selecting chairs for durability and quality. The University met its burden of demonstrating the absence of material fact regarding any breach of a duty of care, while Bonilla did not meet the burden of showing that the University breached a duty of care. Summary judgment for the University was affirmed. Bonilla v. Univ. of Mont., 2005 MT 183, 328 M 41, 116 P3d 823 (2005).

Summary Judgment on Breach of Contract Affirmed — Wrongful Discharge Claim Reversed for Determination of Whether Claimant Was Employee or Independent Contractor: Tvedt brought a claim for breach of contract, wrongful termination, and indemnification of expenses, alleging that defendant group had breached the covenant of good faith and fair dealing, waived the at-will clauses in their employment agreement, and mischaracterized Tvedt as an independent contractor, rather than an employee. Defendant group moved for summary judgment and filed a contingent counterclaim stating that in the event that Tvedt was found to be defendant group's employee, then defendant group's obligation to pay Tvedt the contract value should cease and all payments made to Tvedt should be returned. The District Court determined that Tvedt was not an employee and granted summary judgment to defendant group on all claims, and Tvedt appealed. The Supreme Court affirmed summary judgment on the breach of covenant issue because Tvedt was given adequate notice of termination, defendant group was exercising the specific language of the at-will termination provision of the contract, and Tvedt did not demonstrate that defendant group had waived the right to enforce that provision. However, the court reversed summary judgment on the wrongful discharge claim because the District Court incorrectly applied defendant group's novation argument and because genuine issues of fact remained whether Tvedt was an employee or independent contractor and whether a manager's agreement that recognized Tvedt individually was in effect at the time of termination. Remand was ordered because the District Court never considered whether Tvedt was entitled to relief for wrongful discharge as a matter of law and, if so, whether the claim for indemnification was appropriate. Tvedt v. Farmers Ins. Group of Co., 2004 MT 125, 321 M 263, 91 P3d 1 (2004).

Legal Duty of Sheriff to Protect Domestic Violence Victim — Exception to Public Duty Doctrine Immunity Created Between Sheriff and Victim: Plaintiffs' mother was a domestic violence victim who was killed by her husband. Plaintiffs sued the County Sheriff for negligently failing to take action to protect the victim. A jury found the Sheriff negligent and awarded plaintiffs $358,000. The Sheriff moved for judgment as a matter of law, and the District Court granted the motion and vacated the jury verdict, finding that no special relationship existed between the victim and the Sheriff under the domestic violence statutes that would trigger a legal duty upon the Sheriff to protect the victim. On appeal, the Supreme Court noted an exception to the public duty doctrine's immunity provision in cases when a special relationship between the victim and an officer has been created. The domestic violence statutes created such a special relationship, which gave rise to a special duty by virtue of the victim's status as a member of a protected class. The Sheriff had a statutory duty to protect the victim with a notice of her rights under 46-6-602, and by failing to give the victim the required notice, the jury could conclude that the Sheriff was negligent and, arguably, negligent per se. Although arrest of the husband was discretionary, the

Sheriff also had a mandatory duty under 46-6-603 to seize the husband's weapon, which had been displayed during a prior domestic dispute, but failed to do so. Thus, the jury had sufficient evidence to conclude that the Sheriff's negligence or negligent per se conduct led to the victim's death, and the District Court committed reversible error in granting judgment to the contrary. Massee v. Thompson, 2004 MT 121, 321 M 210, 90 P3d 394 (2004), following Nelson v. Driscoll, 1999 MT 193, 295 M 363, 983 P2d 972 (1999).

Duty of Contractor to Adhere to Building Code — Liability for Radon Damage Properly Submitted to Jury: A contractor built an indoor tennis facility, and the facility developed water leakage and radon damage. The District Court submitted the question of radon mitigation damages to the jury, which the contractor contended was error because neither the construction contract nor building codes required radon mitigation. However, the building code did require installation of a subsurface vapor barrier and proper sized gravel, which the contractor did not install, and breach of the duty to install the barrier and proper gravel resulted in damages, including radon damages. Thus, submission of radon damages to the jury was proper. Glacier Tennis Club at the Summit, LLC v. Treweek Constr. Co., Inc., 2004 MT 70, 320 M 351, 87 P3d 431 (2004).

No Negligence by Architect if Professional Information Not Communicated in Absence of Contract: A tennis club filed a negligence and breach of contract action against a contractor who constructed a tennis facility for the club. The contractor in turn filed a third-party negligence action against the architect who had provided preliminary design parameters and building specifications for the facility. The District Court summarily dismissed the third-party claim, and the contractor appealed, but the Supreme Court affirmed. Applying Jim's Excavating Serv., Inc. v. HKM Associates, 265 M 494, 878 P2d 248 (1994), and Restatement (Second) of Torts 552 (1976), the court held that the architect owed no duty of care to the contractor because the contractor had no contract for the architect's services and failed to prove that the architect communicated professional information with the intention that the information be relied upon by the contractor. Absent a duty of care, there was no breach, so the third-party action failed as a matter of law, and summary judgment was proper. Glacier Tennis Club at the Summit, LLC v. Treweek Constr. Co., Inc., 2004 MT 70, 320 M 351, 87 P3d 431 (2004). Jim's Excavating was followed in W. Sec. Bank v. Eide Bailly, LLP, 2010 MT 291, 359 Mont. 34, 249 P.3d 35.

No Attorney Negligence Given Reasonable Representation — Jury Verdict Affirmed: Plaintiffs contended that defendant, their attorney, was negligent by failing to obtain and review all relevant documents in order to explain the nature of a business transaction in order for plaintiffs to make an informed decision and that by failing in this duty, the attorney negligently allowed plaintiffs to make a binding commitment to sell the business. After 5 days of trial, which included conflicting testimony from experts for both parties, a jury found that the attorney was not negligent. After reviewing the record, the Supreme Court affirmed. When viewed in the light most favorable to the attorney, there was sufficient credible evidence to support the jury's conclusion that the attorney met the duty of care to plaintiffs. Moreover, it was within the standard of care for the attorney to rely on the opinion of a financial consultant as to the reasonableness of the financial tests contained in the sale agreement. The court declined to reverse a jury verdict that was supported by substantial credible evidence. Byers v. Cummings, 2004 MT 69, 320 M 339, 87 P3d 465 (2004).

No Duty of Care Absent Relationship Between Plaintiff and Insurance Agent: Seal sold saddles and tack to Hart. Hart was to procure insurance on the goods to protect against casualty loss and theft, so Hart contracted with a South Dakota insurance agent for property insurance. Seal was not named in the policy as a loss payee. The goods were subsequently stolen, but the insurer refused to pay on grounds that Hart was not a common carrier and, as owner of the property, was not hauling the property of another. Seal sued the insurance agent for breach of contract and failure to procure insurance on Seal's behalf. The District Court concluded that Seal did not contract with the agent to insure any person, property, or risk in Montana, so no relationship existed between the parties to establish a duty on the agent's behalf to procure insurance for Seal. The Supreme Court affirmed. The question of duty is a problem of the relationship between individuals that imposes upon one a legal obligation for the benefit of the other. Here, the only conversations regarding the procurement of insurance occurred between Hart and the agent. Seal never contacted the agent, so no relationship existed between Seal and the agent that gave rise to a corresponding duty to allow Seal to recover on the claim. The certificate of insurance alone did not constitute a contract to procure insurance or impose a duty on the certificate issuer to procure insurance. Seal v. Hart, 2002 MT 149, 310 M 307, 50 P3d 522 (2002). See also Lu-An-Do, Inc. v. Kloots, 721 NE 2d 507 (Ohio Ct. App. 1999).

Permanent Injunction Inappropriate Limitation of Lawful Irrigation Practices: The Wellses built a home on property adjacent to land that had been flood irrigated by the Youngs for generations. Between 1994 and 1998, the Youngs' land was irrigated three times, and on each occasion, the Wellses experienced flooding in the crawl space of their home. The Wellses sought damages in excess of $80,000 based on tort theories of negligence, nuisance, and trespass. The District Court reasoned that because the irrigation practices predated the construction of the Wellses' home, they could not recover damages or recover on their trespass claim under 85-7-2212. The court also concluded that the nuisance claim was barred by 27-30-101. The court held that the Youngs breached the general obligation imposed by this section because their irrigation practices caused immediate, irreparable, and substantial harm to the Wellses' home, but the negligence claim was disposed of because the Wellses failed to establish that the irrigation practiced breached the standard of care of a reasonable farm irrigator engaged in flood irrigation. Nevertheless, the District Court permanently enjoined the Youngs from irrigating their property because future irrigation without modification of the head ditch would result in an unreasonable and substantial risk of continuing harm and irreparable injury to the Wellses' property. The Youngs moved to vacate the injunction based on the determination that their irrigation practices were lawful, but the motion was denied, so the Youngs appealed. The Supreme Court examined the record for abuse of discretion, noting that a District Court must find a breach of an obligation by the party sought to be enjoined before imposing a permanent injunction. The District Court's general finding that the Youngs breached the duty imposed under this section conflicted with the specific findings that the Youngs did not trespass or create a nuisance and conformed to the applicable standard of care. Absent a specific breach of obligation, the District Court abused its discretion in issuing a permanent injunction enjoining the Youngs from engaging in lawful flood irrigation practices. Wells v. Young, 2002 MT 102, 309 M 419, 47 P3d 809 (2002), distinguishing Madison Fork Ranch v. L&B Lodge Pole Timber Prod., 189 M 292, 615 P2d 900 (1980).

Erroneous Conclusion That Elements of Malicious Prosecution by State Not Established — Judgment as Matter of Law Improper: Plaintiffs were cited by the state for various water quality violations related to their public swimming pools, drinking water, and discharge from a sewage lagoon. The charges were ultimately dropped, and both plaintiffs filed separate actions that were settled, except for plaintiffs' malicious prosecution claims against the state, which were joined for trial by jury. At the close of plaintiffs' case, the state's motion for judgment as a matter of law was granted, so plaintiffs appealed. As set out in Orser v. St., 178 M 126, 582 P2d 1227 (1978), in a civil action for malicious prosecution, plaintiff must introduce sufficient proof of the following elements: (1) a judicial proceeding has been commenced and prosecuted against the plaintiff; (2) the defendant was responsible for litigating, prosecuting, or continuing the proceeding; (3) there is lack of probable cause for the defendant's acts; (4) the defendant was actuated by malice; (5) the proceeding terminated in favor of the plaintiff; and (6) the plaintiff suffered damages. Here, the District Court found that plaintiffs had not met their burden of proof regarding elements three, four, and five. The Supreme Court examined each of those elements—lack of probable cause, malice, and favorable termination of the underlying suit—and concluded that the elements were met, warranting reversal for trial on the merits. Judgment as a matter of law averts trial by jury and is proper only in rare cases when undisputed evidence admits of only one conclusion. Although the proceedings to date in this case did not demonstrate guilt or innocence, plaintiffs nevertheless made out a prima facie case that warranted jury determination. Plouffe v. Dept. of Public Health and Human Services, 2002 MT 64, 309 M 184, 45 P3d 10 (2002), following McGuire v. Armitage, 184 M 407, 603 P2d 253 (1979), Miller v. Watkins, 200 M 455, 653 P2d 126 (1982), and Sacco v. High Country Independent Press, Inc., 271 M 209, 896 P2d 411 (1995), and followed in Seipel v. Olympic Coast Investments, 2008 MT 237, 344 M 415, 188 P3d 1027 (2008).

No Negligence by Irrigation District for Failure to Warn of Unforeseeable Flood: Plaintiffs' property was damaged by an unprecedented flood caused by an ice jam on the Clark Fork River. Plaintiffs alleged that the local irrigation district was liable for breaching its duty to construct and maintain an irrigation system that would protect the property and for failing to warn of the flooding conditions to allow plaintiffs the opportunity to protect their property. The District Court held that the irrigation district had no duty to prevent the flood or to warn of the impending natural disaster, and the Supreme Court affirmed. The first element that plaintiffs must establish in a negligence action is the existence of a duty of care, and the measure of a duty of care owed is the scope of the risk that the negligent conduct foreseeably entails. Thus, the primary factor in determining whether the irrigation district owed a duty of care was whether it was foreseeable, as a matter of law, that the district's acts or omissions would pose a risk of injury to plaintiffs. Here, substantial evidence supported the conclusion that the risk that flooding would damage plaintiffs' property was unforeseeable, so the district had no duty to erect or maintain flood control structures to prevent the unforeseeable event. The district also exercised reasonable care in the maintenance of the irrigation system that was in place. Further, plaintiffs failed to advance any applicable authority that would impose upon the district a duty to warn of the unforeseeable flood because mere knowledge of the dangerous situation, of which plaintiffs themselves had become aware the night of the flood, did not impose a legal duty to warn. Gaudreau v. Clinton Irrigation District, 2001 MT 164, 306 M 121, 30 P3d 1070 (2001), following Estate of Strever v. Cline, 278 M 165, 924 P2d 666 (1996).

Lack of Justification in Relying on Allegedly False Information — Claim of Negligent Misrepresentation Properly Dismissed: Following termination from employment with Bitterroot International Systems, Inc. (Bitterroot), Knutson sought to exercise his buyout rights under the shareholders' agreement. Bitterroot refused to pay and sought rescission on grounds of negligent misrepresentation, alleging that Bitterroot relied on Knutson's allegedly false information regarding the value of stock acquired through purchase of another company. However, the definition of negligent misrepresentation set out in St. Bank of Townsend v. Maryann's, Inc., 204 M 21, 664 P2d 295 (1983), requires that the party asserting that defense was justified in relying on the allegedly false information. In this case, Spencer, majority shareholder and president of both Bitterroot and the company that was acquired, knew the respective values of both companies and their stocks and knew that the book values were disparate at the time of the transaction. Thus, Spencer's assertion that he was misled by Knutson was neither credible nor supported by the record, and the District Court correctly dismissed Spencer's claim of negligent misrepresentation. Knutson v. Bitterroot Int'l Sys., Inc., 2000 MT 203, 300 M 511, 5 P3d 554, 57 St. Rep. 800 (2000).

Misvaluation of Corporate Stock Not Constituting Breach of Fiduciary Duty: Following termination from employment with Bitterroot International Systems, Inc. (Bitterroot), Knutson sought to exercise his buyout rights under the shareholders' agreement. Bitterroot refused to pay and sought rescission on grounds that Knutson breached his fiduciary duty to Bitterroot, arguing that Knutson's mistaken valuation of stock acquired during the purchase of another business constituted a breach of that duty. Bitterroot did not contend that Knutson acted in bad faith, but only that he was wrong about the stock value. Applying the standard in 35-1-443 (now repealed), the Supreme Court found that Knutson's inaccurate stock valuation did not constitute a breach of fiduciary duty and that the District Court did not err in dismissing Bitterroot's claim that Knutson breached his fiduciary obligation. Knutson v. Bitterroot Int'l Sys., Inc., 2000 MT 203, 300 M 511, 5 P3d 554, 57 St. Rep. 800 (2000). See also 18A Am. Jur. 2d Corporations §451 and 18B Am. Jur. 2d Corporations §1705.

Duty of City to Inspect City Property for Hazards: Plaintiff was injured after tripping on a fence wire while walking her dog at night in an unmaintained grassy area on city right-of-way next to a city street. Plaintiff contended that the city was negligent in allowing a dangerous and hazardous condition to exist on a public right-of-way and guilty of negligence per se under 81-4-105 for allowing a public nuisance. The District Court granted summary judgment, determining as a matter of law that the city owed plaintiff no duty of care because: (1) she was not walking on a sidewalk, street, or path of any kind; (2) the city did not invite her to travel in that area; and (3) there were no city lights or signs in the vicinity. On appeal, plaintiff cited Richardson v. Corvallis Pub. School District No. 1, 286 M 309, 950 P2d 748 (1997), contending that the city ignored its duty to maintain the public streets, sidewalks, and rights-of-way within corporate limits in a reasonably safe condition for public travel by never going onto the premises, mowing it, raking it, or removing debris and that if routine maintenance had been done, the wire would have been found and removed. The Supreme Court agreed. The city's contention that it did not owe a duty of care in this case, because there was nothing in the area suggesting that it was a walkway or inviting the public to use it as such, failed under the Richardson test because of the city's neglect in exercising ordinary care or skill in the management of its property. Reasonable minds could differ on whether the city should have taken some action to inspect or maintain the property, so summary judgment was improper and thus reversed for a jury determination of negligence, including possible contributory negligence. Dobrocke v. Columbia Falls, 2000 MT 179, 300 M 348, 8 P3d 71, 57 St. Rep. 718 (2000).

Determination of Whether Publication of "Most-Wanted" List Considered Privileged — Abuse of Conditional Privilege as Jury Question: Hale brought defamation and negligence claims against the Billings Police Department for publishing Hale's photograph and personal information and broadcasting the information on a cable television most-wanted fugitive program. The District Court summarily dismissed Hale's claims on grounds that the communication between the police and the media was privileged, either as a proper discharge of an official duty or as part of a judicial proceeding pursuant to 27-1-804. However, the court neglected to determine as a matter of law whether the privilege was an absolute or conditional privilege. Absent a mandate by law that the police provide information regarding arrest warrants to crime prevention programs, the privilege was, at best, conditional. Thus, it was a matter for the jury to determine whether the discharge of the official duty exercised by the police in providing criminal information was proper to the extent that the police did not abuse the privilege. Further, under Sacco v. High Country Independent Press, Inc., 271 M 209, 896 P2d 411, 52 St. Rep. 407 (1995), statements made by the police as to the facts of the case or the evidence expected to be given are not yet part of the judicial proceeding and are not privileged. Summary judgment was improper. Hale v. Billings Police Dept., 1999 MT 213, 295 M 495, 986 P2d 413, 56 St. Rep. 830 (1999), distinguishing Cox v. Lee Enterprises, Inc., 222 M 527, 723 P2d 238, 43 St. Rep. 1476 (1986).

Public Airing of County's Most-Wanted Fugitive List — Material Facts as to Falsity of Statements Precluding Summary Judgment: Hale brought defamation and negligence claims against the Billings Police Department for publishing Hale's photograph and personal information and broadcasting the information on a cable television most-wanted fugitive program and for failing to pull the information from the program after Hale's arrest. The District Court summarily dismissed Hale's claims on grounds that the information was truthful or, if not truthful, then constitutionally protected and therefore not defamatory. Hale was depicted on the program as a potentially armed and dangerous fugitive. However, Hale's warrant for domestic abuse was chosen randomly from 3,000 to 5,000 outstanding warrants on file, and his whereabouts was known at all times by the police, suggesting that under the plain meaning of the terms, Hale was not accused of using a weapon and thus could not be considered "armed and dangerous", and was not a "most-wanted" suspect or a "fugitive" from justice. Clarifying Roots v. Mont. Human Rights Network, 275 M 408, 913 P2d 638, 53 St. Rep. 205 (1996), the Supreme Court held that it was improper for the District Court to create an artificial dichotomy by distinguishing statements of opinion from statements of fact, thereby granting unqualified immunity to the former. Citing Restatement (Second) of Torts 617 (1965), the court held that if an opinion is not based on disclosed facts and, as a result, creates the reasonable inference that the opinion is based on undisclosed defamatory facts, that opinion is not afforded constitutional protection. Without that protection, genuine issues of fact regarding the falsity of the statements made during the broadcast remained, making summary judgment improper. Further, the issue remained as to what constituted timely notification of Hale's arrest to the media by the police to avoid breach of their duty not to infringe on Hale's rights. Summary judgment was reversed, and the case was remanded. Hale v. Billings Police Dept., 1999 MT 213, 295 M 495, 986 P2d 413, 56 St. Rep. 830 (1999), following Milkovich v. Lorain Journal Co., 497 US 1, 111 L Ed 2d 1, 100 S Ct 2695 (1990).

Special Relationship of Custody or Control by Prerelease Center — Responsibility for Public Safety Within Zone of Risk — Foreseeability: A prerelease center entered a contract with the Department of Corrections to supervise residents like Gardipee, who walked away from the center and subsequently injured Lopez. The District Court granted summary judgment for the center on grounds that the attack on Lopez was unforeseeable. Generally, there is no duty to protect others against harm by third persons, but in this case, the contract created a special relationship of custody or control, in turn creating a special responsibility upon the center to protect those members of the public who would be placed within the foreseeable zone of risk created by negligent supervision of a prerelease resident. As a matter of law, the center owed a duty of reasonable care to all persons present within the zone of danger created by the center's failure to exercise reasonable care in supervising Gardipee. Here, reasonable minds could differ as to whether it was reasonably foreseeable by the center that a failure to supervise Gardipee could pose an unreasonable risk of harm to Lopez in particular. There was a genuine issue of material fact as to whether the center knew or should have known that there was enmity between Gardipee and Lopez and a possibility of violence if Gardipee escaped, as well as whether Gardipee's attack was a superseding cause of the harm to Lopez. Both questions were suitable for resolution by a trier of fact, precluding summary judgment. The Supreme Court reversed and remanded for a trial on the merits. Lopez v. Great Falls Pre-Release Serv., Inc., 1999 MT 199, 295 M 416, 986 P2d 1081, 56 St. Rep. 771 (1999).

Actionable Section 1983 Claim Under State-Created Danger Theory: A government official who, while acting under color of state law, deprives an individual of constitutionally protected rights may be subject to personal liability for civil damages pursuant to 42 U.S.C. 1983. Generally, a government official's failure to protect an individual from harm does not constitute a due process violation. Inaction by the state, even when a danger is known, does not trigger a due process obligation except under the "state-created danger" theory, derived from DeShaney v. Winnebago County Dept. of Social Services 489 US 189, 103 L Ed 2d 249, 109 S Ct 998 (1989), which provides that a constitutional duty to protect may be imposed when state actors have affirmatively acted to create plaintiff's danger or to render plaintiff more vulnerable to it. Adopting the test in Huffman v. County of Los Angeles, 147 F3d 1054 (9th Cir. 1998), the Supreme Court held that to assert an actionable 42 U.S.C. 1983 claim under the state-created danger theory, plaintiff must demonstrate that the state acted affirmatively, with deliberate indifference, in creating a foreseeable danger to plaintiff, leading to deprivation of plaintiff's constitutional rights. In the present case, material facts existed as to whether an officer affirmatively and with deliberate indifference placed a woman in danger, increased her vulnerability to danger, or deprived her of her right to life; thus, summary dismissal of her husband's personal liability claim against the officer was reversible error. Nelson v. Driscoll, 1999 MT 193, 295 M 363, 983 P2d 972, 56 St. Rep. 744 (1999). See also Wood v. Ostrander, 879 F2d 583 (9th Cir. 1989), and Kneipp v. Tedder, 95 F3d 1199 (3rd Cir. 1996).

Public Duty Doctrine as Applied to Law Enforcement Personnel — Exception in Cases of Special Relationship: Trina admitted that she had been drinking when stopped in her vehicle by Officer Driscoll, who nevertheless believed that sufficient probable cause did not exist to arrest the woman. Instead, thinking Trina might be impaired, the officer suggested a ride home or that Trina walk the 2-mile distance and warned Trina about returning to the vehicle. Trina decided instead to walk to a phone and call for a ride and was killed in traffic. Trina's husband brought suit for civil damages under 42 U.S.C. 1983, claiming that the officer breached the duty to protect, in violation of Trina's due process rights. The District Court summarily dismissed the claim, holding that because no probable cause existed for Trina's arrest, the officer had no duty to protect Trina from harm and that without a duty, the action failed. The public duty doctrine provides that a police officer's duty to protect and preserve the peace is owed to the public at large rather than to a particular person, unless a special relationship exists, thus giving rise to a special duty that is more particular than that owed to the public. A special relationship is established: (1) by a statute intended to protect a specific class of persons, of which the plaintiff is a member, from a particular type of harm; (2) when a government agent undertakes specific action to protect a person or property; (3) by governmental actions that reasonably induce detrimental reliance by a member of the public; and (4) under certain circumstances when the agency has actual custody of the plaintiff or of a third person who harms the plaintiff. Relying on Stewart v. Standard Publishing Co., 102 M 43, 55 P2d 694 (1936), the Supreme Court agreed that although the officer may not have initially owed Trina a duty to protect, that duty was assumed as a matter of law when the officer prevented the woman from driving her car and ensured that she did not attempt to drive. The question of whether the duty to protect was breached is a question of fact for the jury, so summary dismissal was improper. Nelson v. Driscoll, 1999 MT 193, 295 M 363, 983 P2d 972, 56 St. Rep. 744 (1999), clarifying and distinguishing Phillips v. Billings, 233 M 249, 758 P2d 772 (1988), and followed in Massee v. Thompson, 2004 MT 121, 321 M 210, 90 P3d 394 (2004). Nelson was followed, as to elements of exception to the public duty doctrine (nonlaw enforcement case), in Orr v. St., 2004 MT 354, 324 M 391, 106 P3d 100 (2004), and Prosser v. Kennedy Enterprises, Inc., 2008 MT 87, 342 M 209, 179 P3d 1178 (2008). See also Krieg v. Massey, 239 M 469, 781 P2d 277, 46 St. Rep. 1839 (1989), Busta v. Columbus Hosp. Corp., 276 M 342, 916 P2d 122 (1996), and Eves v. Anaconda-Deer Lodge County, 2005 MT 157, 327 M 437, 114 P3d 1037 (2005).

Agricultural Lease — No Error in Failure to Give Instruction on Implied Contract Covenant to Farm in Workmanlike Manner — Express Lease Terms Stricter Than Requested Instruction on Implied Term: The Schumachers leased property that they owned to Stephens through an agricultural lease. The lease required Stephens to farm with "diligence and care" and to do "all work necessary . . . and to the best interest of lessor, all in such time and manner as shall be to the best advantage and economy". The Schumachers sued Stephens, alleging that Stephens breached the implied contract covenant of good faith and fair dealing. The District Court refused to give the Schumachers' requested instruction on an implied covenant in the lease that would have required Stephens to farm the property in a "competent, skilled, workmanlike and husbandlike fashion". The Supreme Court noted that: (1) the District Court was correct in not giving an instruction on negligence because the Schumachers' complaint and evidence contained no such theory; (2) the District Court did instruct on the implied covenant of good faith and fair dealing; (3) the standard of care required of Stephens was expressly stated in the lease itself; and (4) the Schumachers had not shown that they were prejudiced by the failure to give the requested instruction. For these reasons, the Supreme Court held that it was not error for the District

Court to refuse to give an instruction on an implied covenant to farm in a workmanlike manner. Schumacher v. Stephens, 1998 MT 58, 288 M 115, 956 P2d 76, 55 St. Rep. 247 (1998).

Agricultural Lease — No Error in Failure to Give Plaintiffs' Instruction on Effect of Material Participation Provisions — Instruction on Mutual Cooperation Held Sufficient: The Schumachers leased property that they owned to Stephens through an agricultural lease. Later, when the Schumachers sued Stephens over Stephens' failure to comply with the terms of the lease, Stephens claimed in defense that the Schumachers had breached the material participation agreements in the lease and that therefore he was excused from compliance. The Schumachers requested an instruction stating that if the jury found that Stephens failed to cooperate with the plaintiffs, then Stephens was not entitled to claim that he was excused from liability because of his contention that the Schumachers breached the material participation agreements in the lease. The District Court refused to give the instruction and instead gave an instruction stating that "the failure of a party to fully perform a contract is excused if his performance is prevented or delayed by the conduct of the other party". The Supreme Court noted that the Schumachers had not shown that they were prejudiced in any way by the failure of the District Court to give the requested instruction. Citing Fillinger v. NW. Agency, Inc., of Great Falls, 283 M 71, 938 P2d 1347 (1997), the Supreme Court held that: (1) a party assigning error to a refused instruction must show that the party was prejudiced by the refusal; and (2) the refused instruction must be reviewed in the context of the instructions that were given and the evidence produced at trial. Under these standards, the Supreme Court held that the instruction given by the District Court was sufficient. Schumacher v. Stephens, 1998 MT 58, 288 M 115, 956 P2d 76, 55 St. Rep. 247 (1998).

Foreseeability of Results of Practical Joke — Substantial Factor Test of Causation — Defense of Superseding Intervening Cause Unavailable: Codefendants Linda and David played an April Fools' Day joke on their friend Dennis by calling him at another friend's residence and feigning distress. In his rush to assist, Dennis was in a car accident and injured plaintiff Kolar. The District Court summarily dismissed Kolar's claim against Linda and David, holding that reasonable minds could not differ as to the issue of foreseeability and that although the results of the practical joke were tragic, they were not in any way foreseeable by Linda and David. The Supreme Court reversed the grant of summary judgment, holding that Dennis's state of mind when he left the friend's residence and the extent to which Kolar's injuries should have been foreseeable by Linda and David were questions of fact for the jury, not susceptible to summary judgment. Because the case involved allegations of contributory negligence, multiple causes, and multiple defendants, the use of the substantial factor test of causation was appropriate. The affirmative defense of superseding intervening cause was not available to defendants involved in a practical joke. Kolar v. Bergo, 280 M 262, 929 P2d 867, 53 St. Rep. 1395 (1996).

Duty of Care of Firearm Owner — Independent Intervening Criminal and Negligent Acts as Superseding Firearm Owner's Negligent Breach of Duty: An 11-year-old boy died as the result of a gunshot wound inflicted with a handgun stolen by the boy and three friends from under the seat of Susanj's vehicle. The boy's mother brought a negligence action against Susanj, claiming that his act of leaving the vehicle unattended and unlocked in a public thoroughfare contributed to the boy's death. The District Court summarily dismissed the action after determining that Susanj owed no legal duty to the boy because: (1) Susanj was unaware of previous thefts in the area that would compel him to lock his vehicle; (2) Susanj did not allow entry into the vehicle; (3) Susanj did not have an open display of the firearm that would lure the boys into the vehicle to steal the weapon; and (4) the boy was not an innocent party, but rather a participant in the burglary. However, the Supreme Court held that given the foreseeability of the risk involved in the improper and unsafe use and storage of a firearm and the strong policy considerations favoring safe and prudent use and storage, as a matter of law, a firearm owner has a duty to the general public to use and store a firearm in a safe and prudent manner, taking into consideration the type of firearm, whether it is loaded or unloaded, whether the ammunition is in close proximity or easily attainable, and the location and circumstances of its use and storage. Susanj's failure to exercise ordinary care in storing a dangerous instrumentality like a loaded handgun and ammunition under the seat of his unlocked vehicle constituted a breach of the duty of care. However, the boys' two intervening criminal acts of theft from the vehicle and the intervening grossly negligent act of one boy waving the gun around with his finger on the trigger and trying to unload the gun while high on marijuana were reasonably unforeseeable and cut off all liability on Susanj's part for the boy's death. Summary dismissal of the negligence action was proper based on the independent superseding criminal and grossly negligent acts. Estate of Strever v. Cline, 278 M 165, 924 P2d 666, 53 St. Rep. 576 (1996), citing Prosser and Keaton on Torts 33, 34, and

44 and Restatement (Second) of Torts (1965) 298 and 302B, following Mang v. Eliasson, 153 M 431, 458 P2d 777 (1969), Limberhand v. Big Ditch Co., 218 M 132, 706 P2d 491 (1985), Phillips v. Billings, 233 M 249, 758 P2d 772 (1988), Maguire v. St., 254 M 178, 835 P2d 755 (1992), and Busta v. Columbus Hosp. Corp., 276 M 342, 916 P2d 122 (1996), overruling Lencioni v. Long, 139 M 135, 361 P2d 455 (1961), Brown v. First Fed. S&L Ass'n of Great Falls, 154 M 79, 460 P2d 97 (1969), and Schafer v. St., 181 M 102, 592 P2d 493 (1979), to the extent that those cases hold that no recovery can be allowed for an injury that results from an intervening act of a third party, overruling that portion of King v. St., 259 M 393, 856 P2d 954 (1993), stating that if a plaintiff's injury is caused by the intervening acts of a third party, the defendant's actions cannot be viewed as the proximate cause of the injury, followed in Starkenburg v. St., 282 M 1, 934 P2d 1018, 54 St. Rep. 214 (1997), and distinguished in Cusenbary v. Mortensen, 1999 MT 221, 296 M 25, 987 P2d 351, 56 St. Rep. 864 (1999). See also Gentry v. Douglas Hereford Ranch, Inc., 1998 MT 182, 290 M 126, 962 P2d 1205, 55 St. Rep. 737 (1998).

Malicious Prosecution Counterclaim — Allowed: The defendant in a personal injury case filed a counterclaim against the plaintiffs, alleging that their negligence was the cause of the automobile accident involving the parties. Subsequently, in his deposition, the defendant admitted that he had been intoxicated at the time of the accident, that he had been driving negligently, and that the plaintiffs had not been negligent. The plaintiffs sought summary judgment to dismiss the defendant's counterclaims, but prior to the hearing, the defendant voluntarily dismissed his counterclaims. The lower court ruled that the plaintiffs could not seek damages for malicious prosecution because the court believed that the defendant's dismissal of his counterclaims was part of the overall settlement and that therefore there had not been a termination of a proceeding in favor of the plaintiffs, one of the required elements of malicious prosecution claims. The Supreme Court, in a case of first impression, held that a claim resolved by settlement rather than by judgment did constitute a termination in favor of the plaintiffs. O'Fallon v. Farmers Ins. Exch., 260 M 233, 859 P2d 1008, 50 St. Rep. 1022 (1993).

Malpractice Action Against Veterinarians to Be Supported by Expert Testimony: Zimmerman argued that the lower court erred in dismissing his suit for malpractice against Robertson, a veterinarian, on the basis that Zimmerman had failed to produce any expert medical testimony supporting his claims. In a case of first impression, the Supreme Court extended the requirement for expert testimony to malpractice suits against veterinarians. Zimmerman v. Robertson, 259 M 105, 854 P2d 338, 50 St. Rep. 703 (1993).

Limited Application of Nondelegable Duty Exception to Respondeat Superior Doctrine: Application of the nondelegable duty exception to the respondeat superior doctrine is limited to instances of safety in which the subject matter is inherently dangerous. The Supreme Court declined to modify the presently accepted version of the doctrine by adopting the exception, set out in section 214 of Restatement (Second) of Agency, that a master or other principal who is under a duty to provide protection for or to have care used to protect others or their property and who confides the performance or duty to a servant or other person is subject to liability to others for harm caused to them by the failure of the agent to perform the duty. Noting that there are several reasons for and against extending the liability of an employer when an intentional tort is committed only because or by virtue of the employment situation, the court opted to leave adoption of such a major doctrinal change to the Legislature. Maguire v. St., 254 M 178, 835 P2d 755, 49 St. Rep. 688 (1992), followed in Estate of Strever v. Cline, 278 M 165, 924 P2d 666, 53 St. Rep. 576 (1996).

Requested Coverage Provided — Malpractice Claim Unfounded: Insureds alleged insurance company malpractice based on a breach of the company's duty to sell insurance to properly cover the insureds' needs. Summary dismissal of the claim was proper in light of insured's admission that the company provided the coverage requested. Kaseta v. NW. Agency of Great Falls, 252 M 135, 827 P2d 804, 49 St. Rep. 183 (1992).

Near Privity Rule Applied to Accountants: The plaintiff brought an action against an accountant for negligent performance of an audit and negligent misrepresentation of financial information. The plaintiff had not retained the defendant but had relied on the audit in purchasing a business from the party that had requested the audit. The Supreme Court adopted the "near privity" rule, stating that an accountant may owe a duty to a third party but only if the accountant knows that a specific third party intends to rely on his work and only if the reliance is in connection to a particular transaction of which the accountant is aware. Thayer v. Hicks, 243 M 138, 793 P2d 784, 47 St. Rep. 1082 (1990).

Discharge From Employment — Injury to Be Expected — Intentional Conduct Exclusion Applied: Employee claimed he was intentionally fired for refusing to violate Montana law, resulting in emotional and mental injury. The employer tendered the suit to National Surety Corporation, which refused to defend on grounds that the policy did not provide coverage for an occurrence of this sort. The District Court agreed, and the Supreme Court affirmed on the basis that the claimed injury fell outside the definition of "occurrence". Although an intentional act may constitute an occurrence when the alleged injury was not the expected or intended result of the conduct, here there was no injury alleged that could not be expected to flow from the termination. Therefore, the intentional conduct exclusion was properly applied. Daly Ditches Irrigation District v. Nat'l Sur. Corp., 234 M 537, 764 P2d 1276, 45 St. Rep. 2112 (1988), distinguishing Lindsay Drilling v. USF&G, 208 M 91, 676 P2d 203 (1984); Millers Mut. Ins. Co. v. Strainer, 204 M 162, 663 P2d 338 (1983); and NW. Nat'l Cas. Co. v. Phalen, 182 M 448, 597 P2d 720 (1979). See also Mary & Alice Ford Nursing Home v. Fireman's Ins., 446 N.Y.S.2d 599 (1982), Commercial Union Ins. Co. v. Superior Court, 242 Cal. Rptr. 454, 196 Cal. App. 3d 1205 (1987), Landa v. Assurance Co. of America, 2013 MT 217, 371 Mont. 202, 307 P.3d 284, and Employers Mut. Cas. Co. v. Fisher Builders, Inc., 2016 MT 91, 383 Mont. 187, 371 P.3d 375.

Elements of Malicious Prosecution Claim: Plaintiffs may only recover damages on a malicious prosecution claim when each of the following six elements exists: (1) a judicial proceeding has been commenced and prosecuted against the plaintiff; (2) defendant was responsible for litigating, prosecuting, or continuing the proceeding; (3) there is lack of probable cause for the defendant's acts; (4) defendant was actuated by malice; (5) the proceeding terminated in favor of the plaintiff; and (6) the plaintiff suffered damages. Davis v. Sheriff, 234 M 126, 762 P2d 221, 45 St. Rep. 1783 (1988), citing Orser v. St., 178 M 126, 582 P2d 1227 (1978). These elements were applied in Plouffe v. Dept. of Public Health and Human Services, 2002 MT 64, 309 M 184, 45 P3d 10 (2002), Hughes v. Lynch, 2007 MT 177, 338 M 214, 164 P3d 913 (2007), and McLeod v. St., 2009 MT 130, 350 M 285, 206 P3d 956 (2009).

First-Party Insurance Bad Faith Claim — When Not Supported: Where plaintiff in making a first-party insurance bad faith claim failed to specify any violation of duty by defendant insurer and made no claimant contact with defendant, no request for defense, and no request for indemnity, the directed verdict for defendant was proper. Davis v. Sheriff, 234 M 126, 762 P2d 221, 45 St. Rep. 1783 (1988).

"Constructive Discharge" Construed: As outlined in Pittman v. Hattiesburg Municipal Separate School District, 644 F2d 1071 (5th Cir. 1981), constructive discharge occurs when an employer deliberately makes an employee's working conditions so intolerable that the employee is forced into an involuntary resignation. The federal District Court found that plaintiff could prove constructive discharge and breach of the covenant of good faith and fair dealing if it was shown that a supervisor's intentional conduct caused plaintiff's mental breakdown, leading to loss of plaintiff's job. Oedewaldt v. J.C. Penney Co., Inc., 687 F. Supp. 517, 45 St. Rep. 1366 (D.C. Mont. 1988). But see Frigon v. Morrison-Maierle, Inc., 233 M 113, 760 P2d 57, 45 St. Rep. 1344 (1988), wherein the Montana Supreme Court declined to recognize the doctrine of constructive discharge beyond discrimination cases and held that the covenant of good faith and fair dealing applied only in cases of employee termination.

Covenant of Good Faith and Fair Dealing Applicable Only to Employee Termination: The assertion that breach of the covenant of good faith and fair dealing is a separate tort from wrongful discharge is correct. However, the covenant is applicable only in cases of employee termination. When there was no express termination and there were insufficient facts to establish constructive discharge, summary dismissal of a charge of breach of the covenant was affirmed. Frigon v. Morrison-Maierle, Inc., 233 M 113, 760 P2d 57, 45 St. Rep. 1344 (1988).

Attorney Not Negligent for Preparation of Fill-in-the-Blank Contracts: Defendant sought indemnification for damages from his former attorney, alleging that but for the attorney's negligence, he would not be in breach of contract. The attorney had prepared fill-in-the-blank contracts for defendant's use in land purchases. The attorney was absolved from liability for defendant's failure to perform under the contract terms because the attorney drafted the contracts with a reasonable degree of care for defendant's purposes, he based the contract on information supplied by defendant, and he made no guarantee of the validity of the instrument. Schilke v. Bean, 232 M 125, 755 P2d 565, 45 St. Rep. 930 (1988).

FELA, Not State Statutory Law, as Providing Remedy for Common Law Claims: Claimant sought compensation from a Federal Employers' Liability Act (FELA) self-insurer for an alleged breach of the common law duty of good faith and fair dealing. Claimant argued that because FELA did not specifically address the problem of unfair claims settlement practices, the duties imposed by Montana statutory and common law were not preempted by FELA and should apply. The federal District Court found no authority for this novel proposition in holding that the rights and duties of an employee and employer subject to FELA depend on the terms of the Act itself and on common law as interpreted by the federal courts; therefore, FELA presents the exclusive remedy in all actions falling within the ambit of the Act to the exclusion of state statutory and common law. Toscano v. Burlington N. RR Co., 678 F. Supp. 1477, 45 St. Rep. 367 (D.C. Mont. 1987).

Summary Judgment Proper Upon Failure to Show Evidence of Due Care: When a fire, caused by a floating power line, burned plaintiff's house and property, the District Court granted partial summary judgment, ruling that Montana Power Company (MPC) negligently failed to exercise the proper duty of care in the inspection and maintenance of its utility lines. On appeal, the Supreme Court affirmed the grant of summary judgment, ruling that when the defendant has a high standard of care and the plaintiff provides clear evidence of negligence, it becomes incumbent upon the defendant to provide evidence to show due care was exercised. If the defendant fails to provide such evidence, summary judgment is proper. Ogden v. Mont. Power Co., 229 M 387, 747 P2d 201, 44 St. Rep. 2068 (1987); on reconsideration, opinion withdrawn and replaced by Ogden v. Mont. Power Co., 229 M 387, 747 P2d 201, 44 St. Rep. 2068 (1987).

Failure of Alter Ego and Principal/Agency Theories in Proving Duty of Parent Company to Provide Safe Workplace — No Separate Liability for Injury Covered by Subsidiary's Workers' Compensation: Plaintiff was an employee of a subsidiary company and argued that the subsidiary was so controlled by the parent company that the corporate cloak should be cast aside allowing suit against the parent company. The Supreme Court found no suggestion that the parent company was engaged directly in the business of the subsidiary or that the parent company was an operating entity engaged in operating its business at the place of injury. There was no indication that the subsidiary was used as a subterfuge to defeat public convenience, justify wrong, or perpetuate fraud; therefore, summary judgment was not precluded by the alter ego or principal/agency theory. Further, the subsidiary had discharged its responsibility for plaintiff by securing workers' compensation insurance, with the result that neither the parent company nor its subsidiary would be separately subject to liability for the injury which was covered by workers' compensation. Thornock v. Pack River Management Co., 227 M 524, 740 P2d 1119, 44 St. Rep. 1284 (1987).

Unlawful Conduct Not Necessarily Bar to Negligence Action: Plaintiff and defendant were engaged in the illegal activity of hunting coyotes from defendant's airplane without a proper permit when the plane crashed. The pari delicto doctrine, found in 1-3-215, does not bar plaintiff's negligence action against the defendant as pilot. Conduct prohibited by law that is not strongly condemned by public policy as a matter of serious criminal conduct or delinquency may not be sufficient to bar recovery. The hunting statute in issue is not of a type involving conduct of which the law so strongly disapproves as a matter of public policy that access to the courts should be denied for tort purposes. In light of this holding, the court overrules two prior Montana cases that relied on the pari delicto doctrine to bar lawsuits. The two are Melville v. Butte-Balaklava Copper Co., 47 M 1, 130 P 441 (1913), and Jackson v. Lomas, 60 M 8, 198 P 434 (1921). Waller v. Engelke, 227 M 470, 741 P2d 385, 44 St. Rep. 1241 (1987). However, see Patten v. Raddatz, 271 M 276, 895 P2d 633, 52 St. Rep. 439 (1995), in which the court applied the doctrine of in pari delicto to bar recovery when prostitution and drug consumption constituted the primary purpose of the contract.

Alleged Violations of Collective Bargaining Agreement Preempted by Federal Labor Law: Although a collective bargaining agreement did not specifically address standards to be applied in a situation where an employee was discharged, tort claims alleging negligence and breach of good faith were substantially dependent on terms in the contract establishing wage schedules, union representation, and adherence to a grievance and arbitration procedure. In determining that summary judgment was proper, the Supreme Court cited Allis-Chalmers v. Lueck, 471 US 202, 85 L Ed 2d 206, 105 S Ct 1904 (1985), and reasoned that preemption of the tort claims by federal law was necessary to ensure a unified body of labor contract law and to preserve the central role of arbitration in labor disputes. Smith v. Mont. Power Co., 225 M 166, 731 P2d 924, 44 St. Rep. 124 (1987). See also Anderson v. TW Corp., 228 M 1, 741 P2d 397, 44 St. Rep. 1293 (1987), where it was held that a party may not avoid the preemptive effect of federal labor law when a dispute involves an interpretation of a union contract by pleading in tort and that vacation pay is one item preempted by operation of federal law.

Duty of Care Owed by General Contractor to Subcontractor's Employee — Inherent Danger Exception: Montana follows the general rule that absent reserved control over the subcontractor's operations, the general contractor and owner are not liable for injuries to subcontractor's employees. However, the duty of care is not delegable by the general contractor or owner to the subcontractor if the work is "inherently dangerous" or involves "peculiar risks", in which case the general contractor or owner must exercise reasonable care to ensure measures are taken to mitigate the risk. In this case, a subcontractor's employee was injured when a ditch he was digging caved in. Standard safety measures had not been employed by the subcontractor although required by the contract. The court found that ditchdigging is not inherently dangerous when done with the standard precautions, and therefore there was no nondelegable duty under the inherent danger exception. A strongly worded dissent joined by three justices would have applied the exception and remanded for a determination by a jury whether there was inherent danger and, if so, whether the general contractor exercised reasonable care to mitigate the danger. Kemp v. Bechtel Constr. Co., 221 M 519, 720 P2d 270, 43 St. Rep. 1022 (1986), overruled in Beckman v. Butte-Silver Bow County, 2000 MT 112, 299 M 389, 1 P3d 348, 57 St. Rep. 466 (2000).

Evidence of Wrongful Discharge — Submission to Jury: The Supreme Court, following its decision in Dare v. Mont. Petroleum Marketing Co., 212 M 274, 687 P2d 1015, 41 St. Rep. 1735 (1984), found that respondent's 28 years of employment gave her a secure and objective basis for believing that if her work was satisfactorily performed, her employment would continue. The court noted that, from evidence presented, the jury could have found that appellants had no fair and honest cause for discharge and in fact had ulterior motives. A case for jury deliberation was presented on the issue of wrongful termination. Flanigan v. Prudential Fed. S&L Ass'n, 221 M 419, 720 P2d 257, 43 St. Rep. 941 (1986).

No Reference to Unfair Claim Settlement Practices Statute — Remand — Suspension of Proceedings Pending Determination of Liability: Appellant Fode asked the Supreme Court to recognize the common-law duty of good faith and fair dealing imposed by 28-1-201 and 28-1-203 without reference to 33-18-201, the unfair claim settlement practices statute. In remanding the case, the court found that Fode's allegations contained in his complaint should be presented to the District Court to determine whether a cause of action existed under 33-18-201; however, all proceedings were suspended until liability was determined in the underlying case. Fode v. Farmers Ins. Exch., 221 M 282, 719 P2d 414, 43 St. Rep. 814 (1986), distinguished in Peris v. Safeco Ins. Co., 276 M 486, 916 P2d 780, 53 St. Rep. 481 (1996).

Insurer Exemption for Intentional Bodily Injury: Insurer was properly granted a summary judgment on its claims that it had no obligation to defend or pay a judgment against the insured, who had struck a coworker in the face twice. The policy excluded bodily injury either expected or intended from the standpoint of the insured. Whether insured intended the specific injuries (left cheek bone broken in three places) was not a question of fact precluding summary judgment. When an assailant strikes another in the face, it is irrelevant for purposes of such an insurance exclusion that the assailant causes a different injury than he subjectively intended. The court will not impose upon the insurer the impossible task of proving that the insured specifically intended to break the victim's cheek bone in three places by striking him with his fist. Mut. Serv. Cas. Ins. Co. v. McGehee, 219 M 304, 711 P2d 826, 42 St. Rep. 2038 (1985), followed in Burns v. Underwriters Adjusting Co., 234 M 508, 765 P2d 712, 45 St. Rep. 2089 (1988), and in Am. St. Ins. Co. v. Willoughby, 254 M 218, 836 P2d 37, 49 St. Rep. 708 (1992).

Attractive Nuisance Not Applicable to Certain Artificial Streams or Bodies of Water: The degree of care of one who maintains on his land an artificial stream or body of water for a useful purpose, where the stream or body of water has natural characteristics, is no greater than the degree of care required of one through whose land flows a natural stream or whose land contains a natural body of water. The owner or user of an artificial stream or body of water having natural characteristics is bound to no special duty of care or precaution for the protection of children who may enter therein, unless there is in or about the artificial stream or body of water some peculiar danger, in the nature of a hidden peril or trap for the unwary, of which the owner or user has or ought to have notice. The doctrine of attractive nuisance as such does not apply to such artificial streams or bodies of water any more than it applies to natural streams or bodies of water. Limberhand v. Big Ditch Co., 218 M 132, 706 P2d 491, 42 St. Rep. 1460 (1985).

Duty of Care Not Dependent on Status of Injured Party: The duty of care of a property owner does not depend on the status of a party injured on the property, whether tenant, social guest, invitee, or trespasser. The question is always whether the landowner exercised ordinary care in the circumstances. Limberhand v. Big Ditch Co., 218 M 132, 706 P2d 491, 42 St. Rep. 1460 (1985), followed in Kaiser v. Whitehall, 221 M 322, 718 P2d 1341, 43 St. Rep. 846 (1986), Estate of Strever v. Cline, 278 M 165, 924 P2d 666, 53 St. Rep. 576 (1996), Richardson v. Corvallis Pub. School District No. 1, 286 M 309, 950 P2d 748, 54 St. Rep. 1422 (1997), and Dobrocke v. Columbia Falls, 2000 MT 179, 300 M 348, 8 P3d 71, 57 St. Rep. 718 (2000), overruling Cereck v. Albertson's

Inc., 195 M 409, 637 P2d 509 (1981), and following Corrigan v. Janney, 192 M 99, 626 P2d 838 (1981). However, see Yager v. Deane, 258 M 453, 853 P2d 1214, 50 St. Rep. 610 (1993).

Negligent Hiring and Negligent Entrustment: Insurer's agent participated in a Dillon rodeo, went to a barbecue at his Dillon home, and then went drinking in Dillon bars. While driving home in a vehicle he leased from a service company that was a wholly owned subsidiary of and had a common board of directors with insurer, he struck plaintiff, who sued insurer for negligent hiring and service company for negligent entrustment of the vehicle to agent. Insurer and service company sought summary judgment. That one to whom a vehicle is entrusted is licensed does not alone negate a finding of negligent entrustment. Since the record showed agent had at least once before been in an accident while intoxicated and it was alleged service company knew or should have known the agent had a propensity to drive while intoxicated, there was a material question of fact whether service company breached the duty not to entrust a vehicle to an incompetent driver, and summary judgment as to the service company was denied. Insurer's motion for summary judgment on the negligent hiring issue was denied, the court stating that it could find no Montana case on the negligent hiring doctrine. The questions of whether insurer should have foreseen that it was hiring a dangerous driver, that it was negligent in hiring the agent, and that the negligence proximately caused plaintiff's injuries were considered to be questions of fact not properly disposed of on summary judgment. The court also indicated that whether agent was acting within the scope of his employment at the time of the accident was not an issue. Vollmer v. Bramlette, 594 F. Supp. 243, 41 St. Rep. 1964 (D.C. Mont. 1984).

Malicious Prosecution of State Employee — Elements Not Shown: Employer brought suit for malicious prosecution against university employee who initiated an investigation against him; the university counsel, who conducted the investigation; and the president of the university. Summary judgment for defendants and dismissal of the suit were proper because two of the prima facie elements of malicious prosecution were not established. The County Attorney, not defendants, initiated and continued the prosecution, and plaintiff's bald assertion that defendants caused the prosecution did not raise a genuine issue as to who initiated it. In addition, the defendants were fulfilling a statutory duty. A second unestablished prima facie element was that the prosecution must have terminated favorably for plaintiff. Here, three charges were brought; plaintiff was acquitted of one, and two were dismissed pursuant to a bargained plea of guilty to a substituted charge arising from the investigation. Vehrs v. Piquette, 210 M 386, 684 P2d 476, 41 St. Rep. 1110 (1984).

Motor Vehicle Accident — Sudden Emergency Instruction Usually Improper: As defendant passed codefendant driving downhill, codefendant speeded up and defendant cut in front of him while only 20 feet from an oncoming vehicle. Codefendant overturned in the other lane, and the next two oncoming vehicles were involved in a collision with him. Defendant's proposed sudden emergency doctrine instruction was properly refused. The instruction should not be given in an ordinary motor vehicle accident case. It is unnecessary and confusing, and the ordinary rules of negligence are applicable and sufficient. Further, a test for giving the instruction is that the perilous situation was not created by the person confronted by it and whom the instruction favors; in this case, whether defendant was negligent was very much in dispute, and the instruction was a comment on the evidence as it implied no negligence on his part. Ewing v. Esterholt, 210 M 367, 684 P2d 1053, 41 St. Rep. 1095 (1984), followed in Cline v. Durden, 246 M 154, 803 P2d 1077, 47 St. Rep. 2306 (1990).

Dual Capacity Doctrine — Products Liability Suit by Employee Against Employer — Employer Not a Manufacturer or Seller of the Product: A workman injured on an oil rig sued his employer, the owner of the rig, for products liability, claiming the rig was defective. The dual capacity doctrine is invoked in workers' compensation cases when the employer may be said to owe some duty to an injured employee distinct from his duties as an employer, commonly, when an employee is injured by a piece of equipment manufactured by the employer. Whether this doctrine exists in Montana is not clear; but the question need not be answered because, even assuming that the doctrine applies in Montana, the facts do not support products liability as to the employer. The employer did not manufacture oil rigs to sell to the public and did not place in the stream of commerce the rig involved or any other rig. Montana law requires one held liable for products liability to have been a seller of the defective product. Mitchell v. Shell Oil Co., 579 F. Supp. 1326, 41 St. Rep. 278 (D.C. Mont. 1984).

Trailer Swinging Into Wrong Lane When Driver Swerves to Avoid Collision — No Negligence — No New Trial: Undisputed evidence showed plaintiff was partly in defendant's lane on two-lane road while driving through a curve and that the approaching defendant responded by swerving to the right to avoid a head-on collision. The swerve caused a trailer that defendant was hauling behind his tractor-trailer truck to swing into plaintiff's lane and collide with plaintiff. There was no evidence that defendant was driving unsafely prior to that or that he was in any way negligent. Defendant acted reasonably and prudently, and plaintiff's actions supported a finding that he was the proximate cause of his injuries. The jury verdict found defendant was not negligent. It was an abuse of discretion and reversible error for the court to grant plaintiff a new trial, for there was sufficient evidence to support the verdict. Shannon v. Hulett, 205 M 345, 668 P2d 228, 40 St. Rep. 1349 (1983).

Insurers' Duty to Act in Good Faith Toward Insured: Insurance companies have a duty, independent of contract and statutes, to act in good faith with their insureds. Any statements in Montana Supreme Court cases that may be or appear to be in conflict with this rule are to that extent expressly overruled. Lipinski v. Title Ins. Co., 202 M 1, 655 P2d 970, 39 St. Rep. 2283 (1982), followed in Stephens v. Safeco Ins. Co. of America, 258 M 142, 852 P2d 565, 50 St. Rep. 467 (1993).

Negligence in Performing Contractual Duty — No Privity Required: A prime contractor contracted separately with a steel supplier to supply steel and with a subcontractor to erect the steel. Because the supplier was delayed in delivering the steel, the subcontractor suffered financial losses. The subcontractor could properly maintain an action against the supplier for negligence in the performance of its duties arising out of the steel supply contract with the prime contractor. Privity of contract was not required. Hawthorne v. Kober Constr. Co., 196 M 519, 640 P2d 467, 39 St. Rep. 294 (1982), followed in Tynes v. Bankers Life Co., 224 M 350, 730 P2d 1115, 43 St. Rep. 2243 (1986), and in Jim's Excavating Serv., Inc. v. HKM Associates, 265 M 494, 878 P2d 248, 51 St. Rep. 623 (1994), in which it was held that a third-party contractor may successfully recover for purely economic loss against a project engineer or architect when the design professional knew or should have foreseen that the particular plaintiff or an identifiable class of plaintiffs was at risk in relying on the information supplied.

Property Owner's Duty Dependent on Status of One on Premises: A property owner's duty toward one on the premises depends upon the status of the person on the premises. Cereck v. Albertson's, Inc., 195 M 409, 637 P2d 509, 38 St. Rep. 1986 (1981), overruled in Limberhand v. Big Ditch Co., 218 M 132, 706 P2d 491, 42 St. Rep. 1460 (1985), and Richardson v. Corvallis Pub. School District No. 1, 286 M 309, 950 P2d 748, 54 St. Rep. 1422 (1997).

Snowbanks From Plowing Parking Lot — Business Invitees: Customer walking from a snowplowed shopping center parking lot toward entrance to a supermarket was a business invitee for purpose of determining the duty owed her by supermarket while she was on the premises. Cereck v. Albertson's, Inc., 195 M 409, 637 P2d 509, 38 St. Rep. 1986 (1981), partially overruled in Limberhand v. Big Ditch Co., 218 M 132, 706 P2d 491, 42 St. Rep. 1460 (1985), and overruled, as to the distinction between liability based upon natural versus altered accumulations of ice or snow that are open and obvious and as to the standard that a property owner is absolved of liability because a dangerous condition upon the premises is open and obvious, in Richardson v. Corvallis Pub. School District No. 1, 286 M 309, 950 P2d 748, 54 St. Rep. 1422 (1997).

Promise to Hold Hearing — Requirement of Independent Consideration: Plaintiff, a custodian at the Yellowstone County Courthouse for 18 years, was discharged. His employment was "at will". After discharge, he was told by the County Commissioners that he would be given a grievance hearing. A letter was later sent to plaintiff, informing him that no hearing would be held. The promise to hold a hearing was not supported by independent consideration. Therefore, it was not an enforceable promise under contract law. Section 39-2-503 (now repealed) was, in effect, a part of the employment contract between plaintiff and the county. A promise to hold a hearing, given at a later date, could not modify that part of the contract without independent consideration unless consented to by both parties in writing. Reiter v. Yellowstone County, 192 M 194, 627 P2d 845, 38 St. Rep. 686 (1981), distinguished in Boreen v. Christensen, 267 M 405, 884 P2d 761, 51 St. Rep. 1014 (1994).

Grounds for Denial of Proposed Jury Instruction — Primary Duty of Avoiding Collision: The appellant claimed error in the trial court's denial of his proposed jury instruction stating that the primary duty of avoiding an accident is on a vehicle approaching from the rear when the vehicle in front has signaled for 100 feet. This was an inaccurate statement of the law, and as given, the jury instructions adequately explained the duties of the passing motorist and the left-turning motorist. Even if it had been a correct statement of the law, the proposed statement would have added nothing to the jury's understanding of the applicable law. Burns v. U&R Express, 191 M 343, 624 P2d 487, 38 St. Rep. 302 (1981). See also Wheeler v. Bozeman, 232 M 433, 757 P2d 345, 45 St. Rep. 1173 (1988).

Tort of Contract Interference: In a case in which a former state employee sued the state for violations of his civil rights, the federal District Court indicated that Montana law recognizes that it is a legal wrong for a person to break up or interfere with any contract relationship between other persons. This tort of contract interference, however, lies only against a third person and not against a party to the contract. In this case the court did not find a tort remedy lying in one party to the contract against another. Holladay v. St., 506 F. Supp. 1317, 38 St. Rep. 285 (D.C. Mont. 1981), followed in King v. St., 259 M 393, 856 P2d 954, 50 St. Rep. 848 (1993).

Evidence of Alteration of Accident Scene After the Accident Excluded: Evidence of subsequent repairs or improvements by a defendant altering the scene of an accident may not be admitted in evidence to show negligence on the part of the defendant. The evidence erroneously admitted here put before the jury the idea that the State, by constructing an additional guardrail at the scene of the accident after the accident, admitted to antecedent negligence. Cech v. St., 183 M 75, 598 P2d 584 (1979), affirmed on rehearing, 184 M 522, 604 P2d 97 (1979).

Breach Induced by Third Party:

Parties to contract cannot impose any liability upon stranger to contract under the terms of the contract, but "every person is bound, without contract, to abstain from injuring the person or property of another, or infringing upon any of his rights" and every person who suffers detriment from the unlawful act or omission of another may recover from the person in fault a compensation therefor in money which is called damages. Thus the law, independent of the contract, imposes upon a stranger the duty not to interfere with performance. Violation of that duty is a tort, the remedy for which is by action in tort, and therefore statutory provisions respecting the pleading of breach of contract have no application. Burden v. Elling St. Bank, 76 M 24, 245 P 958 (1926).

A stranger to a contract who unjustifiably induces a party thereto to break it is responsible in damages to the other party. Simonsen v. Barth, 64 M 95, 208 P 938 (1922).

IMPLIED COVENANT OF GOOD FAITH

No Issue of Material Fact Despite Incomplete Record — Implied Covenant of Good Faith and Fair Dealing Not Breached: A mortgagee claimed that his lender breached the implied covenant of good faith and fair dealing by keeping confusing and possibly inaccurate records and failing to keep him apprised of the exact payment obligation owed each month over a period of over a year prior to refusing to accept further payment. The District Court granted summary judgment to the lender in spite of an incomplete factual record regarding the amount of monthly payment assessed to and paid by the mortgagee. The Supreme Court affirmed, holding that the mortgagee undisputedly defaulted on payment during at least 4 months and there was no evidence that the lender's allegedly incomplete records were due to dishonest practices rather than administrative error. House v. U.S. Bank Nat'l Ass'n, 2021 MT 45, 403 Mont. 287, 481 P.3d 820.

Covenant of Good Faith and Fair Dealing — No Application When Terminated Policy Not Part of Employment Contract: A hospital discontinued a policy whereby it paid employees for their sick leave after 25 years of service. Employees with less than 25 years of service sued the hospital for breach of the covenant of good faith and fair dealing. The District Court granted the hospital summary judgment, and the Supreme Court affirmed. Because the policy at issue was not a part of the employment contract, the courts concluded that the covenant of good faith and fair dealing did not apply. Chipman v. NW. Healthcare Corp., 2014 MT 15, 373 Mont. 360, 317 P.3d 182.

Application of Banking Standards, Not Livestock Industry Standards, to Loan Transaction Involving Cattle — Bank-Customer Relationship Not Giving Rise to Fiduciary Responsibilities: A bank loaned money to a couple to fund their cattle breeding operation. When the couple failed to make loan payments, the bank brought an action to collect and foreclose, and the couple brought a counterclaim that the bank's actions breached the covenant of good faith and fair dealing and the bank's fiduciary duty toward the couple. After the couple paid the amount owing, they became the plaintiffs and the case proceeded on the breach of covenant and fiduciary duty claim. The District Court granted the bank summary judgment on the claim, and on appeal, plaintiffs asserted that the court improperly applied banking standards to the case rather than livestock industry standards, constituting a breach of good faith. The Supreme Court disagreed. In Montana, the relationship between a bank and its customer is generally described as that of debtor and creditor and does not give rise to fiduciary duties except when special circumstances place a bank into the role of adviser. In this case, the bank acted as a creditor and not an adviser, and did not force the cattle sale but simply sought to enforce the repayment provisions of its contract with plaintiffs, so no special circumstances existed. The bank acted in accordance with the contract provisions and comported with prudent banking policy and reasonable commercial standards. It was appropriate for the District Court to apply commercial banking standards to the analysis of the bank's relationship with plaintiffs and plaintiffs' ability to service their loans. Summary judgment for the bank was proper. McCoy v. First Citizens Bank, 2006 MT 307, 335 M 1, 148 P3d 677 (2006). See also Pederson v. Rocky Mtn. Bank, 2012 MT 48, 364 Mont. 258, 272 P.3d 663.

Material Misrepresentation on Application for Credit Life and Disability Insurance — Denial of Coverage Warranted: Schlemmer applied to the North Central Life Insurance Company (North Central) for credit life and disability insurance but misrepresented his health history. If he had answered correctly on the application, he would have been ineligible for the insurance. Nevertheless, he averred by his signature that he understood the form and that his application statements were true, so the policy was issued. Schlemmer later filed a claim for disability payments. North Central investigated, found that Schlemmer had been treated within the previous 2 years for hypertension, chronic obstructive lung disease, and disease or disorder of the kidneys, contrary to his statements in the application, and denied the claim and refunded Schlemmer's premiums. Schlemmer sued for damages, claiming that the application and underwriting procedures used by North Central violated 33-18-201, commonly known as the unfair claims settlement practices law, breached the covenant of good faith and fair dealing, and constituted fraud. Schlemmer also maintained that the District Court erred in failing to rule on whether North Central's agent had knowledge of Schlemmer's condition, which might have created a question of material fact. The Supreme Court affirmed the District Court's rulings that: (1) Schlemmer's claim of ignorance of the contents of the written application could not prevail because the application language was clear and unambiguous and Schlemmer did not deny signing it; (2) Schlemmer materially misrepresented his health on the application; (3) the material misrepresentation was legally sufficient to allow North Central to deny coverage under the policy; and (4) Schlemmer's argument that North Central's agent knew or should have known about Schlemmer's health was mere speculation insufficient to create an issue of fact to defeat North Central's properly supported motion for summary judgment. Further, the Supreme Court declined to consider Schlemmer's argument that the misrepresentation could not serve as a basis to rescind the policy because he did not apply for benefits until more than 2 years after applying for the insurance, pursuant to 33-22-205, because Schlemmer never raised the issue at the District Court level. Schlemmer v. N. Cent. Life Ins. Co., 2001 MT 256, 307 M 203, 37 P3d 63 (2001).

Absence of Genuine Issue of Material Fact Regarding Negligent Installation of Septic System — Summary Judgment Proper: Prior to the Sherrards' purchase of property for building a home and horse arena, they had the county sanitarian issue a resite evaluation that addressed ground water levels and designated appropriate septic systems to service each building. The sanitarian approved a permit for a shallow cap system for the horse arena. The system was subject to state regulations requiring minimum 12-inch trenches and prohibiting installation where the water table reached within 5 feet of the natural ground surface. The Sherrards contracted with Prewett to install the system. Prewett dug a hole for the septic tank, dug 36-inch deep trenches for lateral pipes in the drain field, placed washed gravel and pipes in the trenches, and prepared the system for inspection. The next day, the new county sanitarian inspected the system, found standing ground water in the septic tank and observed water in the lateral trenches, fixed the ground water level at 27 inches below the natural surface, and because the ground water level was too high to meet county and state requirements, revoked the Sherrards' permit. The Sherrards then sued Prewett for negligent installation of the system. The District Court determined that because the ground water depth was less than 5 feet and the shallow cap system could not meet regulations, the object of the contract between the parties was illegal and the Sherrards could not proceed with their contract-based claim. Therefore, the court concluded that no genuine issue of material fact existed and granted summary judgment for Prewett, and the Supreme Court affirmed. The Sherrards' bare denial of the 27-inch ground water level and their speculation about the ground water level at the time that the original permit was issued, were insufficient to raise a genuine issue of material fact because they constituted mere denial, speculation, or conclusory statements. The material fact was not whether the ground water level was precisely 27 inches below the surface, but whether it was 5 feet or more below the surface as required by state regulations. To prevail, the Sherrards needed to come forward with substantial and material evidence with regard to the ground water level at the horse arena, but they failed to do so, so summary judgment was proper. Sherrard v. Prewett, 2001 MT 228, 306 M 511, 36 P3d 378 (2001).

Breach of Fiduciary Duty in Conversion of Corporate Property Without Requisite Notice and Shareholder Approval — Punitive Damages Unavailable Absent Showing of Actual Malice or

Fraud: Phil was two-thirds majority shareholder in Trifad Entertainment, Inc. (Trifad), and Brad was one-third minority shareholder and Trifad director. Following Phil's extradition to Florida on racketeering charges, Brad secured a loan for $15,000, deposited the money in the Trifad account, and then sold virtually all of Trifad's assets to himself for $15,000. In addition, Brad wrote checks on Trifad's account for taxes owed and for estimated tax payments and withdrew one-third of the remaining balance and left two-thirds in the account, all without attempting to contact Phil. Phil later sued Brad for breach of contract, breach of fiduciary duty, breach of the implied covenant of good faith and fair dealing, and conversion and requested punitive damages, contending that Brad's actions were performed with actual malice and constituted actual fraud. At trial, Brad contended that the actions were reasonable considering Phil was in jail facing criminal charges, and Brad cross-claimed for indemnification from Trifad for litigation expenses and liabilities incurred in his capacity as Trifad director. The District Court found for Brad on all counts, but denied corporate indemnification. Both Phil and Brad appealed. The Supreme Court reversed, finding that Brad failed to comply with 35-1-823 (now repealed) by selling corporate property without the requisite notice and shareholder approval. Although contacting Phil would have been difficult, it was not impossible. However, even if Phil had been unavailable for consultation, 35-1-823 (now repealed) does not contain any exceptions to the notice and approval requirements governing the sale of corporate assets. Further, the sale constituted conversion because Brad exercised unauthorized dominion over Trifad property by transferring ownership to himself. The case was remanded for a determination of damages, including possible damages other than those provided in 27-1-320 if peculiar circumstances warranted compensation for future lost income and profits. The District Court erred in concluding that Brad did not breach his fiduciary duties to Trifad; however, absent proof of actual malice or actual fraud, punitive damages were not warranted. Because a breach of fiduciary duty occurred, Brad could not claim to be wholly successful in the action, so Brad's claim for corporate indemnification also failed under 35-1-453 (now repealed). Trifad Entertainment, Inc. v. Anderson, 2001 MT 227, 306 M 499, 36 P3d 363 (2001).

Lawsuit by Shareholder Causing Damages Considered Breach of Fiduciary Duty of Care: Sletteland brought a suit against two other corporate shareholders for charging excessive attorney fees and seeking their removal as corporate directors. The District Court held that the fees were excessive, but found no grounds for removal. The other shareholders filed a counterclaim against Sletteland, alleging that he breached his fiduciary duty in bringing the lawsuit because the timing of the suit caused refinancing of a project to fail, resulting in damage to the corporation and to other shareholders. The District Court agreed, and both parties appealed their respective issues. The Supreme Court reversed on the issue of excessive fees, but affirmed on the issue of breach of fiduciary duty. The fiduciary duty between shareholders of a close corporation is one of utmost good faith and loyalty. Sletteland admittedly knew of the refinancing and, as an attorney and investment banker, also knew the effect that a lawsuit alleging misconduct by board members would have on a refinancing effort. In fact, it appeared that the suit was brought to specifically derail the refinancing. Sletteland was the person who determined the timing of the suit, which was filed immediately before the individuals involved in the refinancing were to meet for discussions, and when asked to withdraw the suit so refinancing could conclude, he refused to do so. Sletteland did not use the care that an ordinarily prudent person would use in a similar situation, resulting in the breach of fiduciary duty. The Supreme Court also affirmed the award of damages. Although future damages could not be calculated exactly in this case, the District Court did not abuse its discretion in basing its calculations on expert testimony of a well-known regional economist. Sletteland v. Roberts, 2000 MT 382, 304 M 21, 16 P3d 1062, 57 St. Rep. 1639 (2000).

Federal Law Applying to Collective Bargaining Agreement Preempts Claim of Violation of Covenant of Good Faith and Fair Dealing — Common-Law Claim for Retaliatory Discharge Not Preempted: Winslow was fired from his job with Montana Rail Link, where he had been employed under a collective bargaining agreement, and brought an action in District Court. In his complaint, Winslow included claims for violation of the covenant of good faith and fair dealing and common-law retaliatory discharge. The District Court dismissed both claims. The Supreme Court affirmed the dismissal of the claim for violation of the covenant of good faith and fair dealing, citing Foster v. Albertsons, Inc., 254 M 117, 835 P2d 720 (1992), for the proposition that such a claim is preempted by federal law because the covenant arises out of the employment contract and that that contract, in the case of a collective bargaining agreement, is governed by federal law. However, the Supreme Court reversed the District Court on dismissal of the common-law wrongful discharge claim, citing Foster for the proposition that a common-law claim, because it does not depend upon interpretation of the employment contract, is an independent claim and is not preempted by the federal Railway Labor Act. Winslow v. Mont. Rail Link, Inc., 2000 MT 292, 302 M 289, 16 P3d 992, 57 St. Rep. 1238 (2000).

Agricultural Lease — No Error in Failure to Give Instruction on Implied Contract Covenant to Farm in Workmanlike Manner — Express Lease Terms Stricter Than Requested Instruction on Implied Term: The Schumachers leased property that they owned to Stephens through an agricultural lease. The lease required Stephens to farm with "diligence and care" and to do "all work necessary . . . and to the best interest of lessor, all in such time and manner as shall be to the best advantage and economy". The Schumachers sued Stephens, alleging that Stephens breached the implied contract covenant of good faith and fair dealing. The District Court refused to give the Schumachers' requested instruction on an implied covenant in the lease that would have required Stephens to farm the property in a "competent, skilled, workmanlike and husbandlike fashion". The Supreme Court noted that: (1) the District Court was correct in not giving an instruction on negligence because the Schumachers' complaint and evidence contained no such theory; (2) the District Court did instruct on the implied covenant of good faith and fair dealing; (3) the standard of care required of Stephens was expressly stated in the lease itself; and (4) the Schumachers had not shown that they were prejudiced by the failure to give the requested instruction. For these reasons, the Supreme Court held that it was not error for the District Court to refuse to give an instruction on an implied covenant to farm in a workmanlike manner. Schumacher v. Stephens, 1998 MT 58, 288 M 115, 956 P2d 76, 55 St. Rep. 247 (1998).

Agricultural Lease — No Error in Failure to Give Plaintiffs' Instruction on Effect of Material Participation Provisions — Instruction on Mutual Cooperation Held Sufficient: The Schumachers leased property that they owned to Stephens through an agricultural lease. Later, when the Schumachers sued Stephens over Stephens' failure to comply with the terms of the lease, Stephens claimed in defense that the Schumachers had breached the material participation agreements in the lease and that therefore he was excused from compliance. The Schumachers requested an instruction stating that if the jury found that Stephens failed to cooperate with the plaintiffs, then Stephens was not entitled to claim that he was excused from liability because of his contention that the Schumachers breached the material participation agreements in the lease. The District Court refused to give the instruction and instead gave an instruction stating that "the failure of a party to fully perform a contract is excused if his performance is prevented or delayed by the conduct of the other party". The Supreme Court noted that the Schumachers had not shown that they were prejudiced in any way by the failure of the District Court to give the requested instruction. Citing Fillinger v. NW. Agency, Inc., of Great Falls, 283 M 71, 938 P2d 1347 (1997), the Supreme Court held that: (1) a party assigning error to a refused instruction must show that the party was prejudiced by the refusal; and (2) the refused instruction must be reviewed in the context of the instructions that were given and the evidence produced at trial. Under these standards, the Supreme Court held that the instruction given by the District Court was sufficient. Schumacher v. Stephens, 1998 MT 58, 288 M 115, 956 P2d 76, 55 St. Rep. 247 (1998).

Questionable Basis for Denial of Claim — Directed Verdict Inappropriate: Under common law and 33-18-242, an insurer cannot be held liable for bad faith in denying a claim if the insurer had a reasonable basis for contesting the claim or the claim amount. As determined in St. Paul Fire & Marine Ins. Co. v. Cumiskey, 204 M 350, 665 P2d 223 (1983), an insurer may file a declaratory judgment action to obtain a determination of the validity, continuance, or coverage of the policy, the extent of liability, or the insurer's duty under the policy. However, a directed verdict is not required simply because a reasonable basis may exist to deny coverage. If reasonable people could draw different conclusions about whether an insurer had a reasonable basis for contesting a claim, the issue becomes more than a question of law and a directed verdict is inappropriate. Palmer v. Farmers Ins. Exch., 261 M 91, 861 P2d 895, 50 St. Rep. 1210 (1993). However, see Landa v. Assurance Co. of America, 2013 MT 217, 371 Mont. 202, 307 P.3d 284 (holding summary judgment proper when a reasonable basis in law for denying coverage existed).

Extent of Obligation of Good Faith and Fair Dealing Measured by Justifiable Expectations of Parties: Talley argued that because the covenant of good faith and fair dealing is implied into every contract, the community college that employed him as a part-time instructor breached the covenant by not hiring him back after his term contract expired. However, the nature and extent of the obligation of good faith and fair dealing is measured by the justifiable expectations of the parties. Because Talley's contract had a "no-tenure" clause that precluded any justifiable expectation of continued employment, allegations of breach of the covenant of good faith and fair dealing were not reasonable. Talley v. Flathead Valley Community College, 259 M 479, 857 P2d 701, 50 St. Rep. 889 (1993).

Good Faith Required in Exercise of General Right to Assign Debts Under Restructuring Agreement — Summary Judgment Inappropriate: The District Court relied on Carma Developers v. Marathon Dev. Calif., Inc., 826 P2d 710 (Calif. 1992), in granting summary judgment to defendants who contended that the implied covenant of good faith and fair dealing could not be used to override the specific provisions of a restructuring agreement allowing the assignment of plaintiff's debts. The Supreme Court distinguished Carma in holding that summary judgment was improper when a genuine issue of material fact existed as to whether the covenant was breached by defendant's discretionary use of the power of assignment to assign the notes to plaintiff's partner. Simmons Oil Corp. v. Holly Corp., 258 M 79, 852 P2d 523, 50 St. Rep. 433 (1993).

Breach of Covenant of Good Faith and Fair Dealing Based on Collective Bargaining Agreement as Preempted by Federal Law: Any implied covenant of good faith and fair dealing in the employment context arises from the underlying contract of employment. An underlying contract based on a collective bargaining agreement is subject to the application of federal rather than state law on questions involving the existence and breach of the implied covenant. Foster v. Albertsons, Inc., 254 M 117, 835 P2d 720, 49 St. Rep. 638 (1992), followed in Miller v. Glacier County, 257 M 422, 851 P2d 401, 50 St. Rep. 339 (1993), and Winslow v. Mont. Rail Link, Inc., 2000 MT 292, 302 M 289, 16 P3d 992, 57 St. Rep. 1238 (2000). See also Teamsters Union v. Lucas Flour Co., 369 US 95, 7 L Ed 2d 593, 82 S Ct 571 (1962), and Paige v. Henry J. Kaiser Co., 826 F2d 857 (9th Cir. 1987).

Fiduciary Duty Between Shareholders in Close Corporation When No Other Type of Relationship Exists: The fiduciary duty between stockholders of a close corporation is one of utmost good faith and loyalty. However, the controlling group should not be stymied by a minority stockholder's grievances if the controlling group can demonstrate a legitimate business purpose and the minority stockholder cannot demonstrate a less harmful alternative. If called on to settle a dispute between the stockholders, the court must weigh the legitimate business purpose, if any, against the practicability of a less harmful alternative. Daniels v. Thomas, Dean & Hoskins, Inc., 246 M 125, 804 P2d 359, 47 St. Rep. 2293 (1990), citing Donahue v. Rodd Electrotype Co. of New England, Inc., 328 NE 2d 505 (Mass. 1975), and Wilkes v. Springside Nursing Home, Inc., 353 NE 2d 657 (Mass. 1976), and distinguishing Skierka v. Skierka Bros., Inc., 192 M 505, 629 P2d 214 (1981), Deist v. Wachholz, 208 M 207, 678 P2d 188 (1984), and Dunfee v. Baskin-Robbins, 221 M 447, 720 P2d 1148 (1986).

In Warren v. Campbell Farming Corp., 2011 MT 324, 363 Mont. 190, 271 P.3d 36, the Montana Supreme Court, in answering a certified question from the Tenth Circuit Court of Appeals, revisited the Daniels test and concluded that the Daniels test does not apply to claims involving director conflict of interest transactions. However, the Daniels test does apply to minority shareholders' claims of breach of fiduciary duties against majority shareholders.

No Evidence Alleged Fraud Benefit to Defendant: The plaintiff argued that the defendant bank's failure to disclose that certain escrow payments had not been applied by the bank as the plaintiff had been led to believe they would be applied constituted constructive fraud. The Supreme Court ruled that the evidence did not support the claim because the bank did not gain any advantage by the nondisclosure. Kitchen Krafters, Inc. v. Eastside Bank of Mont., 242 M 155, 789 P2d 567, 47 St. Rep. 602 (1990).

Covenant of Good Faith and Fair Dealing Inapplicable to Lateral Transfer: Following the rationale set out in Frigon v. Morrison-Maierle, Inc., 233 M 113, 760 P2d 57, 45 St. Rep. 1344 (1988), the Supreme Court found it inappropriate to apply the covenant of good faith and fair dealing to a termination following the refusal of an employee to accept a lateral transfer of employment. Finstad v. Mont. Power Co., 241 M 10, 785 P2d 1372, 47 St. Rep. 39 (1990).

Occasional Compliments From Employer — No Expectation of Job Security: During her year-long employment, plaintiff received compliments on her work from persons other than her employer and occasional compliments from her employer, but her immediate supervisor was continually critical of her performance. The implied covenant of good faith and fair dealing did not arise in this situation because the employer gave plaintiff no reasonable expectation of job security. Objective manifestations of job security must come from the employer, not from persons outside the work place, in order to establish an expectation of job security. Karell v. Am. Cancer Soc'y, 239 M 168, 779 P2d 506, 46 St. Rep. 1593 (1989).

Discharge From Employment — Injury to Be Expected — Intentional Conduct Exclusion Applied: Employee claimed he was intentionally fired for refusing to violate Montana law, resulting in emotional and mental injury. The employer tendered the suit to National Surety Corporation, which refused to defend on grounds that the policy did not provide coverage for an occurrence of this sort. The District Court agreed, and the Supreme Court affirmed on the basis that the claimed injury fell outside the definition of "occurrence". Although an intentional act may constitute an occurrence when the alleged injury was not the expected or intended result of the conduct, here there was no injury alleged that could not be expected to flow from the termination. Therefore, the intentional conduct exclusion was properly applied. Daly Ditches Irrigation District v. Nat'l Sur. Corp., 234 M 537, 764 P2d 1276, 45 St. Rep. 2112 (1988), distinguishing Lindsay Drilling v. USF&G, 208 M 91, 676 P2d 203 (1984); Millers Mut. Ins. Co. v. Strainer, 204 M 162, 663 P2d 338 (1983); and NW. Nat'l Cas. Co. v. Phalen, 182 M 448, 597 P2d 720 (1979). See also Mary & Alice Ford Nursing Home v. Fireman's Ins., 446 N.Y.S.2d 599 (1982), Commercial Union Ins. Co. v. Superior Court, 242 Cal. Rptr. 454, 196 Cal. App. 3d 1205 (1987), Landa v. Assurance Co. of America, 2013 MT 217, 371 Mont. 202, 307 P.3d 284, and Employers Mut. Cas. Co. v. Fisher Builders, Inc., 2016 MT 91, 383 Mont. 187, 371 P.3d 375.

Reciprocal Duty of Good Faith and Fair Dealing Between Employer and Employee — Character of Employee Relevant to Expectation of Job Security: The Supreme Court applied the holding in Los Angeles Mem. Coliseum Comm'n v. NFL, 791 F2d 1356 (9th Cir. 1986), in finding that the implied covenant of good faith and fair dealing mandated a reciprocal duty in the employment relationship, applicable to both employer and employee. Breach by one party served to negate any breach by the other party, so that neither party was entitled to recovery. This rule applied only narrowly to factual contexts where both breaches concerned the same issue and occurred during one episode of the relationship. In the present case, an employee who breached the covenant could not then complain of unfair dealing by the employer. The District Court improperly excluded evidence of specific misconduct related to the employee's character because the alleged misconduct was relevant to whether the employee had a reasonable expectation of job security and could thus claim protection under the covenant. Barrett v. ASARCO Inc., 234 M 229, 763 P2d 27, 45 St. Rep. 1865 (1988). See also Flanigan v. Prudential Fed. S&L, 221 M 419, 720 P2d 257, 43 St. Rep. 941 (1986), Dare v. Mont. Petroleum Mkting. Co., 212 M 274, 687 P2d 1015, 41 St. Rep. 1735 (1984), and Story v. Bozeman, 259 M 207, 856 P2d 202, 50 St. Rep. 761 (1993).

Firing Not Due to Economic Necessity: There was sufficient evidence presented to rebut the employer's claim that the employee plaintiff was discharged because of economic necessity, thus supporting submission of the case to the jury based on breach of the implied covenant of good faith and fair dealing. Kerr v. Gibson's Prod. Co. of Bozeman, Inc., 226 M 69, 733 P2d 1292, 44 St. Rep. 462 (1987).

Failure to Promptly Investigate Claims and Coverage — Bad Faith: A jury found no debatable question of insurance coverage. Liability for exercising bad faith was proper when evidence indicated the insurance company failed to promptly investigate insured's claims and coverage by taking 9 months for an investigation that could have been done professionally in 2 weeks, failed to inform insured of potential coverage under an extended benefits policy provision, and failed to provide coverage for large claims after accepting premiums and paying smaller previous claims. Tynes v. Bankers Life Co., 224 M 350, 730 P2d 1115, 43 St. Rep. 2243 (1986).

Explicit Contractual Provision Giving Greater Protection Than Implied Covenant of Good Faith and Fair Dealing — No Application of Covenant: Where a collective bargaining agreement provided explicitly that employees could be discharged "only for just cause", the Supreme Court declined to imply the covenant of good faith and fair dealing to the employment relationship since the contractual agreement provided greater protection than the implied covenant. Such a covenant generally applies to "at will" employment contracts. Brinkman v. St., 224 M 238, 729 P2d 1301, 43 St. Rep. 2163 (1986). See also Riley v. Warm Springs St. Hosp., 229 M 518, 748 P2d 455, 44 St. Rep. 2183 (1987).

Franchisor's Right to Determine Franchise Location — Duty to Reasonably Consider Relocation: Appellant franchisor had the sole contractual right to determine location of the franchise; however, the law imposed a duty to reasonably consider facts regarding relocation. The Supreme Court found evidence that vital information was withheld from respondents and from the vice president in charge of authorizing relocation which, if believed, would provide a basis for finding appellant acted unreasonably, thereby breaching its duty to exercise good faith. The evidence was sufficient to warrant submission to the jury on the question of good faith. Dunfee v. Baskin-Robbins, Inc., 221 M 447, 720 P2d 1148, 43 St. Rep. 964 (1986).

No Question of Fiduciary Duty When Judgment Based Only on Good Faith and Fair Dealing: Appellant argued that District Court prejudiced its interests by improperly instructing the jury that, as franchisor, appellant owed a fiduciary duty to respondents as franchisees. The Supreme

Court noted that a franchise relationship is inherently a business relationship rather than a fiduciary relationship. However, the questioned jury instruction was found to be primarily definitional; therefore, the Supreme Court found it unnecessary to rule on whether the special facts of the case gave rise to a fiduciary duty since the District Court only held appellant to the responsibility of acting in good faith and fair dealing with respondents. Dunfee v. Baskin-Robbins, Inc., 221 M 447, 720 P2d 1148, 43 St. Rep. 964 (1986).

Evidence of Wrongful Discharge — Submission to Jury: The Supreme Court, following its decision in Dare v. Mont. Petroleum Marketing Co., 212 M 274, 687 P2d 1015, 41 St. Rep. 1735 (1984), found that respondent's 28 years of employment gave her a secure and objective basis for believing that if her work was satisfactorily performed, her employment would continue. The court noted that, from evidence presented, the jury could have found that appellants had no fair and honest cause for discharge and in fact had ulterior motives. A case for jury deliberation was presented on the issue of wrongful termination. Flanigan v. Prudential Fed. S&L Ass'n, 221 M 419, 720 P2d 257, 43 St. Rep. 941 (1986).

Negligence as Proper Basis for Recovery — Wrongful Discharge: A negligence claim and a claim for breach of implied covenant of good faith and fair dealing may arise out of the same occurrence, include the same facts, and only involve different theories of law; therefore, negligence is a proper basis for recovery in wrongful termination cases. Flanigan v. Prudential Fed. S&L Ass'n, 221 M 419, 720 P2d 257, 43 St. Rep. 941 (1986), following Crenshaw v. Bozeman Deaconess Hosp., 213 M 488, 693 P2d 487, 41 St. Rep. 2251 (1984).

Instruction Given on Constructive Fraud — Instruction on Bad Faith Superfluous: The District Court instructed the jury on constructive fraud but not on breach of the implied covenant of good faith and fair dealing, which plaintiff contended was error. The Supreme Court noted that the jury found no breach of duty under the instruction on constructive fraud, which does not require a showing of fraudulent intent. An instruction on bad faith would require plaintiff to prove intentional concealment. The court held that if plaintiff could not meet the burden of proof on constructive fraud, she could not meet the higher burden of proof on bad faith; thus, the instruction would have been superfluous. Bushnell v. Cook, 221 M 296, 718 P2d 665, 43 St. Rep. 825 (1986), partially overruled in Cechovic v. Hardin & Associates, Inc., 273 M 104, 902 P2d 520, 52 St. Rep. 854 (1995).

No Bad Faith Instruction in Absence of Actual Knowledge of Defects — Knowledge Not Imputed: Plaintiff contended that District Court erred in not instructing the jury on breach of the implied covenant of good faith and fair dealing, arguing that the covenant should have been applied to a real estate partnership and to a development partnership. The Supreme Court found no error in refusing to instruct as against the real estate partnership because it was not shown at trial that the partnership had actual knowledge of claimed defects in the land necessary to constitute bad faith. The court further held that while knowledge may be imputed to a real estate partnership as a member of a development partnership, it cannot be imputed from the development partnership to the real estate partnership. Bushnell v. Cook, 221 M 296, 718 P2d 665, 43 St. Rep. 825 (1986).

Inadequate Jury Instruction — Implied Covenant of Good Faith: The District Court instructed the jury on the implied covenant of good faith and fair dealing, stating that good faith means honesty in fact in the conduct or transaction concerned and then equating the implied covenant to an obligation imposed by law on defendants to do nothing to deprive plaintiffs of the benefits of their commercial transaction. On appeal, defendants argued that the implied covenant had no application in a case involving an arms-length contract. The Supreme Court, relying on its decision in Nicholson v. United Pac. Ins. Co., 219 M 32, 710 P2d 1342, 42 St. Rep. 1822 (1985), held that a breach of the implied covenant which results in damages can give rise to an action in tort, but that in order to recover additional punitive damages, plaintiffs must prove that defendants' actions in breaching the implied covenant met the requirements of 27-1-221. The tort of breach of the implied covenant of good faith and fair dealing requires more than a lack of honesty in fact. The instruction given to the jury on this issue inadequately defined the tort. McGregor v. Cushman/Mommer, 220 M 98, 714 P2d 536, 43 St. Rep. 206 (1986), followed in Noonan v. First Bank Butte, 227 M 329, 740 P2d 631, 44 St. Rep. 1124 (1987). See also Dunfee v. Baskin-Robbins, Inc., 221 M 447, 720 P2d 1148, 43 St. Rep. 964 (1986).

Covenant of Good Faith and Fair Dealing — General Test for Contracts Covered: Plaintiff, who owned a building and two construction companies, and defendant insurance company signed a lease for office space in a building. Plaintiff was to renovate the space, and the two were to confer on and mutually approve the renovation plans. Disagreements arose on the plans. Plaintiff claimed he had difficulties contacting defendant. Defendant rescinded the lease on the ground that it had continually invested more time and money than plaintiff and that from a business standpoint the lease was no longer feasible. After failing in an attempt to contact defendant's president, plaintiff sent a notice of default and sued. The court affirmed an award of punitive damages to plaintiff. The court declined to extend the tort of breach of an implied covenant of good faith and fair dealing to all contracts of any type, including arms-length and substantially equal bargaining power contracts, but stated that: (1) whether breach of a contract constitutes the tort depends on whether there has been some impermissible activity; (2) the nature and extent of an implied covenant of good faith and fair dealing is measured in a particular contract by the justifiable expectations of the parties and, whether performing or breaching, each party has a justifiable expectation that the other will act as a reasonable person; (3) a party who acts arbitrarily, capriciously, or unreasonably exceeds the justifiable expectations of the other party, and the other party should be compensated for damages resulting from the culpable conduct; and (4) for punitive damages to be awarded for breach of an implied covenant of good faith and fair dealing in a contract breach situation, the breach must amount to oppression, fraud, or malice. Nicholson v. United Pac. Ins. Co., 219 M 32, 710 P2d 1342, 42 St. Rep. 1822 (1985), followed in Weinberg v. Farmers St. Bank of Worden, 231 M 10, 752 P2d 719, 45 St. Rep. 391 (1988), and in McJunkin v. Kaufman, 229 M 432, 748 P2d 910, 44 St. Rep. 2111 (1987). See also Shiplet v. First Sec. Bank of Livingston, Inc., 234 M 166, 762 P2d 242, 45 St. Rep. 1816 (1988), and Mann Farms, Inc. v. Traders St. Bank of Poplar, 245 M 234, 801 P2d 73, 47 St. Rep. 2094 (1990), replacing previous opinion, subsequently withdrawn, at 47 St. Rep. 1557 (1990).

Commission of Bad Faith Tort Against Depositor by Bank: The District Court did not err in instructing the jury to consider recovery by bank depositor against the bank under bad faith tort principles and to accordingly consider punitive damages. The depositor and his nephew opened a checking account with a card requiring the signatures of both on checks. They then formed a partnership. The nephew induced the bank to change the card so that he could issue checks without the depositor's signature. The bank did not notify the depositor of the change or obtain his authorization for it. The bank told depositor his signature was not needed but did not tell him about the new card, and depositor disagreed. Later the bank told him it would not change its policy of honoring checks signed only by the nephew. When depositor's attorney told bank not to do so, the bank stated the card required only one signature and the bank would not change the card unless both the nephew and the depositor requested it. The bank then told depositor the card was lost but later that day produced both cards. Depositor sued, and the bank subsequently took various negative and detrimental actions against his credit status, refused loans of a type formerly granted, canceled his ready reserve account, and refused to pay several items presented before he was notified that the account had been canceled. Tribby v. NW. Bank of Great Falls, 217 M 196, 704 P2d 409, 42 St. Rep. 1133 (1985).

INJURY TO PERSON

Duty Not to Injure Others — Application to Law Enforcement Officers: A law enforcement officer responded to a neighborhood disturbance and observed the suspect running into a driveway, over a retaining wall, and into the plaintiff's yard. The plaintiff came out of his house to investigate the commotion. The officer heard the plaintiff approaching, turned around to see the plaintiff, and tackled the plaintiff due to self-protection instinct. The plaintiff later reported a torn rotator cuff and sued the officer, alleging state law negligence and a 42 U.S.C. 1983 violation. The case was removed to federal court and appealed to the Ninth Circuit Court. The Ninth Circuit Court certified the following state law question, as reformulated by the Montana Supreme Court: "Under Montana law, when a plaintiff claims he was injured directly by an officer's affirmative acts, does the public-duty doctrine exclude all duties that may arise pursuant to generally applicable principles of negligence?" The Supreme Court found that the public duty doctrine is not so broad as to provide an exemption from the statutory duty imposed by 27-1-701 and 28-1-201 to not injure others as a result of lack of ordinary care. In other words, although the public duty doctrine provides that an officer does not owe a legal duty to an individual plaintiff when the plaintiff alleges harm suffered from the officer's breach of the general duty to protect and preserve the peace, a law enforcement officer is not exempt from owing a duty of care to a plaintiff directly injured by the officer's affirmative acts. Bassett v. Lamantia, 2018 MT 119, 391 Mont. 309, 417 P.3d 299.

Student Not Subject to Restraint on Liberty — No Custodial or Special Relationship: A high school student was caught on campus with a tin of chewing tobacco and was disciplined by being suspended from all extracurricular activities. The student became distraught upon realizing the suspension would bar him from the state wrestling tournament; he went home and committed suicide that afternoon. The student's mother sued the school board and the superintendent, alleging that her son's death was the direct and proximate result of the school board's negligence. The District Court granted summary judgment to the board. On appeal, the Supreme Court held that because suicide is generally considered a deliberate intervening act, the board was entitled to summary judgment. Because the student had no history of mental health problems, the suicide was unforeseeable, and therefore the board owed no legal duty to the student. Additionally, the mother could not show a special relationship between the student and the school board because the board had no obligation to exercise custodial care over the student, who was not in the custody of the board and was in his own home when he committed suicide. Gourneau v. Hamill, 2013 MT 300, 372 Mont. 182, 311 P.3d 760.

Premises Liability — Duty of Care to Independent Contractor — Status Irrelevant: After the plaintiff slipped and fell while working and sustained personal injuries, the plaintiff sued the defendant who owned the building and leased space to the third party for whom the plaintiff contracted to provide cleaning services. The District Court, relying on construction law cases, granted summary judgment to the defendant, concluding that the defendant owed no duty of care to the plaintiff because the plaintiff was an independent contractor working for a third party. On appeal, the Supreme Court reversed, concluding that the plaintiff's status as an independent contractor was not relevant in an ordinary premises liability case and that the status of an injured party does not affect a property owner's general duty of care, which depends on the degree of ordinary care that a reasonable person would use under the same or similar circumstances. Steichen v. Talcott Properties, LLC, 2013 MT 2, 368 Mont. 169, 292 P.3d 458.

Admissibility of Infectious Disease Specialist Testimony — Qualified to Testify on Standard of Care and Causation for Radiologist's Procedure: Plaintiffs, as representatives of the estate of a deceased patient, filed a medical malpractice claim against a radiologist and a hospital based on allegations that the defendants departed from the applicable standard of care by failing to adhere to proper infection control measures, which negligently caused the patient's death. On a summary judgment motion, the District Court excluded the testimony of the plaintiffs' proposed expert witness, an infectious disease specialist, on the grounds that he was not qualified to testify as an expert under 26-2-601 because he is not a radiologist and does not perform the procedure at issue. On appeal, the Supreme Court determined that the infectious disease specialist satisfied the requirements of 26-2-601 based on his qualifications and that the District Court's holding to the contrary was an abuse of discretion. The proposed expert was qualified to give testimony regarding the standard of care for the radiologist and the hospital as well as an opinion regarding causation. Beehler v. E. Radiological Associates, P.C., 2012 MT 260, 367 Mont. 21, 289 P.3d 131, distinguishing Butler v. Domin, 2000 MT 312, 302 Mont. 452, 15 P.3d 1189.

No Duty of Care Owed by School District for Student's Unforeseeable Conduct: A student handed in a typing assignment that contained violent themes and unspecified threats. The student was counseled, but no subsequent actions were taken. About 17 months later, the student ran over a woman in an incident that resembled one of the themes in the typing assignment. The victim sued the school district for negligence, but summary judgment was granted for the school district on grounds that no duty was owed to the victim. On appeal, the Supreme Court held that, based on the facts known to the school district at the time of its allegedly negligent conduct, it was not foreseeable that 17 months later the student would intentionally run over a pedestrian off school grounds after school hours. The school district therefore had no duty to protect the victim from the student, so summary judgment for the school district was proper. Emanuel v. Great Falls School District, 2009 MT 185, 351 M 56, 209 P3d 244 (2009), distinguishing Prindel v. Ravalli County, 2006 MT 62, 331 M 338, 133 P3d 165 (2006), Lopez v. Great Falls Pre-Release Serv., Inc., 1999 MT 199, 295 M 416, 986 P2d 1081 (1999), and LaTray v. Havre, 2000 MT 119, 299 M 449, 999 P2d 1010 (2000).

Reasonable Foreseeability of Intentional or Reactive Striking Between Boys With Sticks: During a lacrosse game in gym class between 14-year-old high school freshman boys, one student struck another in the eye with a lacrosse stick. The District Court found that the striking was foreseeable as a matter of law and was not an intervening cause that severed the causal chain. On appeal, the Supreme Court agreed. It was clearly foreseeable that intentional or reactive striking would occur under these circumstances, and the striking was not an intervening cause sufficient to break the causal chain. Partial summary judgment for plaintiff on the issue was proper. Larchick v. Diocese of Gt. Falls-Billings, 2009 MT 175, 350 M 538, 208 P3d 836 (2009), following Fisher v. Swift Transp. Co., Inc., 2008 MT 105, 342 M 335, 181 P3d 601 (2008). See also Prindel v. Ravalli County, 2006 MT 62, 331 M 338, 133 P3d 165 (2006).

Nondelegable Duty to Provide Safe Workplace — Availability of Contributory Negligence Defense: The District Court held that defendant employer owed plaintiff employee a nondelegable duty of care to maintain a safe workplace and that employer's breach of that duty caused plaintiff's injuries as a matter of law. The District Court then allowed defendant to argue contributory negligence, which plaintiff asserted was an improper delegation of defendant's safe workplace duty. While recognizing the nondelegable duty under 50-71-201, the Supreme Court also noted that 27-1-702 imposes on a plaintiff the duty to conform to a standard of conduct for plaintiff's own protection so that plaintiff's conduct does not constitute a legally contributing cause that operates along with defendant's negligence in bringing about plaintiff's harm. Citing Edie v. Gray, 2005 MT 224, 328 M 354, 121 P3d 516 (2005), and Giambra v. Kelsey, 2007 MT 158, 338 M 19, 162 P3d 134 (2007), the court harmonized the two concepts by holding that establishing the existence of negligence per se settles only the questions of duty and breach, but a plaintiff must still prove causation before recovering damages, and a jury may weigh or compare evidence of negligence from a statutory violation that constitutes a proximate cause of the injury along with other evidence of negligence on the part of both parties. As provided in Shannon v. Howard S. Wright Constr. Co., 181 M 269, 593 P2d 438 (1979), and Stepanek v. Kober Constr., 191 M 430, 625 P2d 51, 38 St. Rep. 385 (1981), contributory negligence remains available as a defense to a defendant who has breached its nondelegable duty to provide a safe workplace if evidence demonstrates that: (1) the employee has some reasonable means or opportunity to avoid the hazard without endangering employment; or (2) the harm in question was not a reasonably foreseeable consequence of the employer's breach of the safety duty. In this case, the evidence created a genuine issue of material fact as to whether plaintiff had been contributorily negligent, so it was proper for the trial court to submit the issue to the jury and for the jury to apportion negligence between the parties in reaching a verdict. Olson v. Shumaker Trucking & Excavating Contractors, Inc., 2008 MT 378, 347 M 1, 196 P3d 1265 (2008).

No Exception Shown to Rule on Nonliability of Owner to Employee of Subcontractor — Summary Judgment Proper: Fabich filed for damages from an injury received after a fall from scaffolding while working as an employee of a subcontractor at defendant's power plant. The District Court found that defendant was not liable and granted summary judgment for defendant. Fabich appealed on grounds that the court incorrectly rejected Fabich's theories of liability. Generally, an owner, employer, or general contractor does not have a duty to prevent injuries to an independent contractor's employees, but Fabich asserted that defendant nevertheless had a duty under three recognized exceptions to the general rule, claiming that defendant negligently exercised retained control, that the activity was inherently dangerous, and that defendant had a nondelegable duty (see Umbs v. Sherrodd, Inc., 246 M 373, 805 P2d 519 (1991), and Beckman v. Butte-Silver Bow County, 2000 MT 112, 299 M 389, 1 P3d 348 (2000)). The Supreme Court examined each exception and affirmed summary judgment. First, Fabich's theory of negligence in exercising retained control failed because defendant did not retain control over the working circumstances. Second, the theory of inherently dangerous activity failed because the hazards associated with the job were normally encountered in the workplace and did not call for particular precautions. Third, there was nothing in the contract establishing that defendant assumed responsibility for initiating, maintaining, and supervising safety precautions, so defendant had no nondelegable duty. Absent a genuine issue of material fact regarding defendant's liability, summary judgment was proper. Fabich v. PPL Mont., LLC, 2007 MT 258, 339 M 289, 170 P3d 943 (2007).

Evidence of Driver's Conduct Allowed to Establish Passenger's Comparative Negligence: Elisha was killed while riding on Jason's motorcycle after Jason failed to negotiate a turn. Elisha's parents sued the state for negligence in constructing and maintaining the road. Although he was a nonparty, the state sought to introduce evidence of Jason's alleged intoxication, excessive speed, and misaimed headlight in an attempt to establish Elisha's alleged comparative negligence. The District Court disallowed the evidence, but on appeal, the Supreme Court reversed. Under Buck v. St., 222 M 423, 723 P2d 210 (1986), a driver's negligence cannot be imputed to a passenger for purposes of comparative negligence. However, if sufficient evidence exists to show that in the exercise of ordinary care the passenger should have chosen not to ride with an intoxicated driver, the jury should be instructed on the separate issue of negligence involving the passenger and should decide the issue of the passenger's comparative negligence. Additionally, a finding that the passenger was subjectively aware of the driver's alleged negligence or intoxication is not required before the passenger may be found comparatively negligent. Faulconbridge v. St., 2006 MT 198, 333 M 186, 142 P3d 777 (2006).

Introduction by Defendant of Nonparty Conduct Allowed Only to Show That Conduct Was Superseding Intervening Cause of Plaintiff's Damages: Elisha was killed while riding on Jason's motorcycle after Jason failed to negotiate a turn. Elisha's parents sued the state for negligence in constructing and maintaining the road. Although he was a nonparty, the state sought to introduce evidence of Jason's alleged intoxication, excessive speed, and misaimed headlight. The state recognized that Montana law precludes a defendant from apportioning liability to a nonparty, but argued that evidence of Jason's conduct was admissible to negate causation pursuant to Pula v. St., 2002 MT 9, 308 M 122, 40 P3d 364 (2002), and to rebut breach of duty. The District Court disallowed the evidence. On appeal, the Supreme Court affirmed. After revisiting Pula, the court concluded that a defendant may introduce nonparty conduct only to demonstrate that the conduct was a superseding intervening cause of plaintiff's damages, which means an unforeseeable event that occurs after the defendant's original act of negligence. The question then became whether Jason's conduct was foreseeable and whether the state, as the entity that designed and maintained the road, might reasonably have foreseen as probable that Jason might drive in a negligent manner. The court cited Buck v. St., 222 M 423, 723 P2d 210 (1986), for the holding that driver error is anticipated and that the fact that a driver was arguably negligent does not cut off the state's liability for negligence in the design and maintenance of a road. Faulconbridge v. St., 2006 MT 198, 333 M 186, 142 P3d 777 (2006), followed in Larchick v. Diocese of Gt. Falls-Billings, 2009 MT 175, 350 M 538, 208 P3d 836 (2009).

Failure to Admit Person to Jail When Committed by Competent Authority — Negligence Per Se Argument Not Considered for First Time on Appeal: Russell violated the terms of his suspended sentence and was ordered to report to the county jail no later than 8 a.m. on December 28, 1998. When Russell appeared at the jail, a written order of commitment could not be found, so Russell was turned away. When Prindel was subsequently injured by Russell, Prindel argued that failure to admit Russell to jail constituted negligence per se on the part of the county. However, Prindel did not allege any elements of negligence per se in the action, so the Supreme Court declined to address the issue on appeal. Prindel v. Ravalli County, 2006 MT 62, 331 M 338, 133 P3d 165 (2006).

Failure to Admit Person to Jail When Committed by Competent Authority Negligent Violation of Duty of Care: Russell violated the terms of his suspended sentence and was ordered to report to the county jail no later than 8 a.m. on December 28, 1998. When Russell appeared at the jail, a written order of commitment could not be found, so Russell was turned away. On December 30, Russell stabbed Prindel at a party, and Russell was sentenced to life in prison for attempted deliberate homicide. Prindel subsequently sued the county, alleging that the failure to incarcerate Russell on the 28th, despite a court order that Russell begin serving a sentence on that day, amounted to negligence that proximately caused Prindel's injury. The District Court granted summary judgment to the county, concluding that the county had no duty to prevent Russell from injuring Prindel and that the issue of causation need not be addressed. On appeal, the Supreme Court reversed. The county's argument that it had no duty of care without a written order was without merit because the oral pronouncement of sentence constituted the competent authority to incarcerate Russell, and the jail's ignorance of the commitment order did not diminish the court order's status as a competent authority. The county had a special relationship of custody under 7-32-2205 to take Russell into custody for the protection of the public, and failure to do so was negligence as a matter of law. Russell posed a foreseeable risk, Prindel was a foreseeable plaintiff, and the county owed a duty to Prindel to exercise reasonable care to protect him against Russell. Reasonable minds could differ as to whether Russell's act of stabbing Prindel was so unforeseeable as to sever the chain of causation, so summary judgment for the county was error. Prindel v. Ravalli County, 2006 MT 62, 331 M 338, 133 P3d 165 (2006), following Lopez v. Great Falls Pre-Release Serv., Inc., 1999 MT 199, 295 M 416, 986 P2d 1081 (1999), and LaTray v. Havre, 2000 MT 119, 299 M 449, 999 P2d 1010 (2000).

No Showing That Defendants' Actions in School Bus Incident More Than Likely Caused Student's Physical and Mental Injuries — Factors in Judicial Determination of Duty of Care — Summary Dismissal of School District Liability Proper: A student returning home on a school bus from a performance with the school pep band asked the director to stop the bus so that the student could use the restroom, but the director refused. The student was subsequently disciplined by the school for various actions related to the incident and soon after became seriously ill. The student and his parents filed an action against the school district, the director, and the bus driver, alleging that various breaches of the duty of care triggered or accelerated the student's development of diabetes and caused his posttraumatic stress disorder. The District Court granted summary judgment for defendants, and on appeal, the Supreme Court affirmed. The existence of a duty of care depends on the foreseeability of the risk and on a weighing of the policy considerations for and against the imposition of liability, including: (1) moral blame attributable to defendant's conduct; (2) prevention of future harm; (3) extent of the burden placed on defendant; (4) consequences to the public of imposing a duty; and (5) availability of insurance for the risk involved. Further, the law of torts holds a defendant liable only for injuries to others that were to the defendant at the time reasonably foreseeable. A defendant owes a duty with respect to risks and hazards whose likelihood made the conduct unreasonably dangerous and hence negligent in the first instance. The specific injury need not be foreseeable, rather the question is whether defendant could have foreseen that the conduct would result in injury to plaintiff. The District Court here concluded that defendants owed no duty of care because the student's injuries were not foreseeable, which was an erroneous focus on the particular injury rather than on the foreseeability that defendants' conduct could result in the injury. However, if a plaintiff fails to offer proof of any one of the elements of negligence—duty, breach, causation, and damages—then summary judgment in favor of defendant is proper. The question remained whether plaintiffs' experts adequately established causation, and the Supreme Court held that they did not. The experts testified that defendants' conduct could have caused or accelerated the student's injuries, but under Butler v. Domin, 2000 MT 312, 302 M 452, 15 P3d 1189 (2000), the testimony did not meet the threshold of establishing that defendants' actions more than likely caused the injuries. Absent a causal connection between defendants' actions and the student's injuries, summary judgment for defendants was proper. Hinkle v. Shepherd School District No. 37, 2004 MT 175, 322 M 80, 93 P3d 1239 (2004), distinguishing Kolar v. Bergo, 280 M 262, 929 P2d 867 (1996).

Duty of State to Maintain University Library in Safe Condition: Plaintiff's child fell through the second story railing at the Montana State University-Bozeman library and suffered brain injuries. Just weeks before, another child fell thorough the same stairway. In determining negligence, the District Court granted plaintiff partial summary judgment on the issue of duty of care and breach of the duty. The state appealed. The Supreme Court affirmed, holding that the state had a duty of ordinary care to prevent children from falling through the railing at the public building and that the state breached that duty because the state had notice from the previous accident that there was a defect, yet the state did not cure, remove, or warn of the defect. Foreseeability was established at the time of the previous accident, so the state was liable despite a relatively accident-free history at the library and the fact that the building was grandfathered in under an older version of the building code in effect when the building was constructed. Henricksen v. St., 2004 MT 20, 319 M 307, 84 P3d 38 (2004), following Wiley v. Glendive, 272 M 213, 900 P2d 310 (1995).

No Prejudicial Error in Failure to Give Negligent Homicide Mental State Instruction in Wrongful Death Action When Other Instructions Adequately Reflect Negligence: Samson's son was killed by Bercier, a youth who walked away from a nonsecure, supervised licensed youth group home. Samson sued the state for foreseeable negligence. To boost the theory of foreseeability, Samson offered a jury instruction that defined Bercier's conduct as reckless and postulated therefrom that the conduct was foreseeable because of Bercier's background, seeking to undermine the state's theory that the shooting was an unforeseeable accident. The District Court refused to offer the instruction, instead instructing the jury on elements of wrongful death, and Samson appealed. The state argued that the mental state of Bercier was not a controlling issue and contended that it was not necessary to instruct the jury on the mental state of negligent homicide because the instructions as a whole properly included the key concepts of a wrongful death action. The Supreme Court agreed with the state. The fundamental issue concerned the state's negligence, not Bercier's mental state. Nevertheless, Samson was still able to present the foreseeability theory under the instructions that were given, so failure to give Samson's offered instruction did not result in prejudice to Samson's case. It is within a District Court's discretion to decide how to instruct the jury, taking into account the theories of the contending parties, and absent an abuse of discretion, the District Court was affirmed. Samson v. St., 2003 MT 133, 316 M 90, 69 P3d 1154 (2003). See also Busta v. Columbus Hosp. Corp., 276 M 342, 916 P2d 122 (1996).

State Not Liable for Unforeseeable Accident — Intervening Criminal Act of Third Person — Expert Testimony on Foreseeability Proper: Samson's son was killed by Bercier, a youth who walked away from a nonsecure, supervised licensed youth group home. Samson sued the state for negligence. The jury returned a verdict for the state, and Samson appealed. Rather than retry the case and evaluate the facts to determine whether the state was negligent, the Supreme Court reviewed the verdict to determine if there was substantial evidence to support it and determined that there was. In order to sustain a negligence action, plaintiff must establish a legal duty on the part of defendant, a breach of that duty, causation, and damages. In cases involving a dispute over the intervening criminal act of a third party, foreseeability must be analyzed twice—first with regard to the existence of a legal duty and second with regard to proximate causation.

Samson contended that the District Court erred in allowing the state to present evidence in the form of expert testimony and to argue that the shooting was an unforeseeable accident. The state argued that the expert testimony was relevant and aided the jury. Given the need to determine the foreseeability of Bercier's actions, the expert testimony was properly allowed. Further, in cases alleging an intervening cause, juries must be instructed that the specific injury to plaintiff need not have been foreseen. Samson v. St., 2003 MT 133, 316 M 90, 69 P3d 1154 (2003), affirming Lacock v. 4B's Restaurants, Inc., 277 M 17, 919 P2d 373 (1996). See also Lopez v. Great Falls Pre-Release Serv., Inc., 1999 MT 199, 295 M 416, 986 P2d 1081 (1999), and St. v. LaTray, 2000 MT 262, 302 M 11, 11 P3d 116 (2000).

Proximate Cause Determination Needed in Alleging Negligence Per Se or Common-Law Negligence in Swimming Pool Drowning — Summary Judgment Proper: Following a drowning at the swimming pool of Custer's Inn, the estate of the victim filed a wrongful death action, alleging that the inn's negligence per se in failing to comply with state swimming pool safety statutes and regulations was the proximate cause of the drowning. In granting the inn's motion for summary judgment, the District Court ruled that the estate had failed to plead common-law negligence. On appeal, the Supreme Court outlined the five elements established in VanLuchene v. St., 244 M 397, 797 P2d 932 (1990), to prove negligence per se and the four elements established by the court in numerous decisions necessary to prove common-law negligence. In affirming the District Court's grant of summary judgment for the inn, the court ruled that under either theory of negligence, a plaintiff's claim must fail as a matter of law if the defendant's conduct did not cause the alleged damages. In this case, the estate failed to establish any material dispute that the failure of the inn to comply with swimming pool safety statutes and regulations was the proximate cause of the victim's drowning death. Schwabe v. Custer's Inn Associates, 2000 MT 325, 303 M 15, 15 P3d 903, 57 St. Rep. 1370 (2000), overruled in Giambra v. Kelsey, 2007 MT 158, 338 M 19, 162 P3d 134 (2007), to the extent that Schwabe held that breach of a statutory duty under a negligence per se claim may also carry the added advantage of foreclosing common law defenses.

Duty of City to Inspect City Property for Hazards: Plaintiff was injured after tripping on a fence wire while walking her dog at night in an unmaintained grassy area on city right-of-way next to a city street. Plaintiff contended that the city was negligent in allowing a dangerous and hazardous condition to exist on a public right-of-way and guilty of negligence per se under 81-4-105 for allowing a public nuisance. The District Court granted summary judgment, determining as a matter of law that the city owed plaintiff no duty of care because: (1) she was not walking on a sidewalk, street, or path of any kind; (2) the city did not invite her to travel in that area; and (3) there were no city lights or signs in the vicinity. On appeal, plaintiff cited Richardson v. Corvallis Pub. School District No. 1, 286 M 309, 950 P2d 748 (1997), contending that the city ignored its duty to maintain the public streets, sidewalks, and rights-of-way within corporate limits in a reasonably safe condition for public travel by never going onto the premises, mowing it, raking it, or removing debris and that if routine maintenance had been done, the wire would have been found and removed. The Supreme Court agreed. The city's contention that it did not owe a duty of care in this case, because there was nothing in the area suggesting that it was a walkway or inviting the public to use it as such, failed under the Richardson test because of the city's neglect in exercising ordinary care or skill in the management of its property. Reasonable minds could differ on whether the city should have taken some action to inspect or maintain the property, so summary judgment was improper and thus reversed for a jury determination of negligence, including possible contributory negligence. Dobrocke v. Columbia Falls, 2000 MT 179, 300 M 348, 8 P3d 71, 57 St. Rep. 718 (2000).

Notice of Defect Not Required Before Landowner's Duty of Care Exists Toward Persons Injured on Property — Sullivan and Buck Overruled: Plaintiff was injured after tripping on a fence wire while walking her dog at night in an unmaintained grassy area on city right-of-way next to a city street. The District Court determined that under Montana law, a city must have notice of a defect in its streets and sidewalks before being held liable for an accident occurring as a result of the defect, citing Wiley v. Glendive, 272 M 213, 900 P2d 310 (1995), and since the city had no notice of the wire, it could not be held liable. The Supreme Court distinguished the Wiley pronouncement of required notice as based largely on dicta and went on to examine the cases that Wiley was based on, including Sullivan v. Butte, 104 M 225, 65 P2d 1175 (1937), and Buck v. St., 222 M 423, 723 P2d 210 (1986). The court then overruled Sullivan and Buck to the extent that notice of a defect is required before a landowner, whether it be the state, a city, a corporation, or a private individual, has a duty of care to persons injured on the landowner's property and instead applied Richardson v. Corvallis Pub. School District No. 1, 286 M 309, 950 P2d 748 (1997), which established the standard for premises liability based on the landlord's exercise of ordinary care or skill in the management of property. A property owner who never maintains the land will never have notice of defects until someone is injured. It would not make sense to hold that landowners who never inspect or maintain their property are not exposed to liability because they could not discover a defect, while landowners who do inspect and maintain their property are exposed to liability. Thus, the District Court erred in concluding that the city's failure to have notice of the wire precluded relief against it as a matter of law. Dobrocke v. Columbia Falls, 2000 MT 179, 300 M 348, 8 P3d 71, 57 St. Rep. 718 (2000). See also Brown v. Demaree, 272 M 579, 901 P2d 567 (1995).

Double Analysis of Foreseeability in Dispute Over Intervening Act of Third Party — Duty of Police to Protect Hospital Worker From Intoxicated Person in Voluntary Custody: Havre police received a report of two girls fighting downtown. They responded and found two intoxicated women fighting, one of whom appeared to require medical treatment. LaTray was working as a nurse at a hospital emergency room when police officers delivered the woman for treatment, accompanied by her sister. The injured woman was placed in protective custody, but neither woman was arrested. When attempting to administer medical care to the injured woman, LaTray was intentionally assaulted and injured by the sister, and LaTray filed an action against the city police officers for negligently failing to exercise proper control over the sister. The District Court found that because the intentional assault was not reasonably foreseeable as a matter of law, there was no duty owed LaTray by the city, and summary judgment was granted to the city. The Supreme Court held that intervening criminal acts of third persons are not automatically unforeseeable as a matter of law, but rather must be addressed in the foreseeability context on a case-by-case basis (see Starkenburg v. St., 282 M 1, 934 P2d 1018 (1997)). Although foreseeability is ordinarily analyzed only under the duty element of negligence, in a dispute over intervening criminal acts of a third party, foreseeability must be analyzed twice: first with regard to the existence of a legal duty and, second, with regard to proximate causation (see Lopez v. Great Falls Pre-Release Serv., Inc., 1999 MT 199, 295 M 416, 986 P2d 1081 (1999)). The city relied on Phillips v. Billings, 233 M 249, 758 P2d 772 (1988), arguing that because LaTray did not claim the existence of a special relationship or otherwise show that the officers owed LaTray a greater duty of care than that owed to the general public, the city owed LaTray no duty of care. The Supreme Court noted that Phillips has been clarified in Nelson v. Driscoll, 1999 MT 193, 295 M 363, 983 P2d 972 (1999), which stated that a duty to protect third persons arises only when a police officer actually makes an arrest or otherwise takes possession or custody of an individual. Although the officers did not actually arrest the sister or otherwise have a basis for taking her into custody in this case, the officers voluntarily undertook possession or custody in transporting her to the hospital and consequently harbored the ability to control her actions and prevent an unreasonable risk of harm to third persons like LaTray, who falls within the scope of the risk that negligent supervision would foreseeably entail. Thus, the Supreme Court held that, as a matter of law, the city owed a duty of reasonable care to adequately supervise the sister so as to prevent harm to a third person who would foreseeably be placed within the scope of risk arising from negligent supervision. Whether the city breached that duty is an issue for the jury because the causal issue of intervening acts of third parties normally involves questions of fact. Viewed in the light most favorable to LaTray, there was sufficient evidence of the sister's irascible conduct to raise a jury question as to whether she posed a danger to those around her on the day in question, and reasonable jurors could differ as to whether she presented a foreseeable risk of injury to persons in her immediate vicinity. These contested issues of material fact precluded a grant of summary judgment as a matter of law, and the case was reversed and remanded for a new trial. LaTray v. Havre, 2000 MT 119, 299 M 449, 999 P2d 1010, 57 St. Rep. 497 (2000), followed, with regard to appropriateness of summary judgment on issues of negligence, in Prindel v. Ravalli County, 2006 MT 62, 331 M 338, 133 P3d 165 (2006). See also Morrow v. FBS Ins. Montana-Hoiness LaBar, Inc., 230 M 262, 749 P2d 1073 (1988), and Estate of Strever v. Cline, 278 M 165, 924 P2d 666 (1996).

No Duty Constituting Negligence When Danger or Risk Unforeseeable — Summary Judgment Proper Absent Material Fact Regarding Legal Duty: The father could not reasonably foresee that, by giving his child permission to go to a friend's house to play, the child would go to the house of a different friend, participate along with other children in burning a photograph using gasoline, and be burned when another friend accidentally kicked the container of flaming gasoline onto his child. The duty element of negligence turns primarily on foreseeability, and if a reasonably prudent defendant can foresee neither any danger of direct injury nor any risk from an intervening cause, there is no negligence. Ordinarily, negligence actions involve questions of fact and are not susceptible to summary judgment, but in this case, reasonable minds could not differ regarding the absence of material fact regarding any duty owed by the father, so summary judgment was proper as a matter of law. Poole v. Poole, 2000 MT 117, 299 M 435, 1 P3d 936, 57 St. Rep. 489 (2000), following Busta v. Columbus Hosp. Corp., 276 M 342, 916 P2d 122 (1996). See also Lopez v. Great Falls Pre-Release Serv., Inc., 1999 MT 199, 295 M 416, 986 P2d 1081 (1999), and Gourneau v. Hamill, 2013 MT 300, 372 Mont. 182, 311 P.3d 760.

Inherent Danger of Trenching Activity — Vicarious Liability of Employer for Injuries Caused by Subcontractor's Failure to Reduce Risks: Beckman was working to replace a waterline in a trench in Butte when the trench collapsed. At the time, Beckman was an employee of an independent contractor who had been hired by a developer to replace the city waterline as part of the upgrade to another project that the developer was constructing, as required by Butte-Silver Bow. Beckman filed a complaint against Butte-Silver Bow, seeking damages for personal injuries sustained in the collapse. Under Umbs v. Sherrodd, Inc., 246 M 373, 805 P2d 519 (1991), employers are generally not liable for the torts of their independent contractors, except when: (1) there is a nondelegable duty based on a contract; (2) the activity is inherently or intrinsically dangerous; and (3) the general contractor negligently exercises control reserved over a subcontractor's work. The District Court found that trenching activity was not inherently or intrinsically dangerous and granted Butte-Silver Bow's motion for summary judgment. The court, citing Kemp v. Bechtel Constr. Co., 221 M 519, 720 P2d 270 (1986), ruled as a matter of law that trenching activities did not fall under the inherently dangerous exception because Beckman's injury could have been avoided through standard precautions. On appeal, the Supreme Court decided that the analysis of the inherently dangerous activity exception in Kemp was manifestly wrong, and overruled that case and its progeny. Instead, the court reaffirmed the holding in Ulmen v. Schwieger, 92 M 331, 12 P2d 856 (1932), in which it was determined that the vicarious liability of an employer of a subcontractor was contingent on the nature of the work performed and not on the existence of standard precautions. An employer is therefore vicariously liable for injuries to others caused by a subcontractor's failure to take precautions to reduce unreasonable risks associated with engaging in an inherently dangerous activity. Risks associated with people working in trenches where a cave-in can cause death or serious bodily injury are well recognized in the construction industry as intrinsically or inherently dangerous and are recognized as such as a matter of law. Beckman v. Butte-Silver Bow County, 2000 MT 112, 299 M 389, 1 P3d 348, 57 St. Rep. 466 (2000), overruling Micheletto v. St., 244 M 483, 798 P2d 989 (1990), and Kemp v. Big Horn County Elec. Co-op, Inc., 244 M 437, 798 P2d 999 (1990). Beckman was followed in Cunnington v. Gaub, 2007 MT 12, 335 M 296, 153 P3d 1 (2007).

Material Question Whether County Negligently Exercised Control Over Subcontractor as Precluding Summary Judgment: Beckman was working to replace a waterline in a trench in Butte when the trench collapsed. At the time, Beckman was an employee of an independent contractor who had been hired by a developer to replace the city waterline as part of the upgrade to another project that the developer was constructing, as required by Butte-Silver Bow. Beckman filed a complaint against Butte-Silver Bow, seeking damages for personal injuries sustained in the collapse. Under Umbs v. Sherrodd, Inc., 246 M 373, 805 P2d 519 (1991), employers are generally not liable for the torts of their independent contractors, except when: (1) there is a nondelegable duty based on a contract; (2) the activity is inherently or intrinsically dangerous; and (3) the general contractor negligently exercises control reserved over a subcontractor's work. The District Court cited Micheletto v. St., 244 M 483, 798 P2d 989 (1990), and Kemp v. Big Horn County Elec. Co-op, Inc., 244 M 437, 798 P2d 999 (1990), in holding that the county did not assume a nondelegable duty of safety by contract, finding that Butte-Silver Bow never agreed to supervise the safety of the trenching operations and therefore did not assume a nondelegable duty based on contract that extended to Beckman. Thus, summary judgment was granted to Butte-Silver Bow. On appeal, the Supreme Court noted that the District Court correctly recognized the distinction between a nondelegable contractual duty and a duty based on the negligent exercise of retained control. However, Micheletto and Kemp provide an incorrect statement of the doctrine of retained control. Here, despite the lack of a written contract, the county retained the means with which to both discover and cure any unreasonably dangerous conditions. The terms of the water mains extension document, which provided that the county may supervise the water extension project, required the county to furnish a qualified construction inspector to monitor work performed during the installation of the water supply system and required that the materials and methods of construction conform to county requirements. The terms, combined with the fact that county employees were present during the trenching operation, constituted sufficient facts to preclude summary judgment for the county. The case was reversed and remanded. Beckman v. Butte-Silver

Bow County, 2000 MT 112, 299 M 389, 1 P3d 348, 57 St. Rep. 466 (2000). See also Stepanek v. Kober Constr., 191 M 430, 625 P2d 51 (1981).

Expert Testimony Necessary to Establish Applicable Standard of Care Owed by Physician Who Treats Referred Patient — Functional Capacities Evaluation: Even though a physician-patient relationship may not exist when a test is administered at the request of a third party, a physician nevertheless owes a duty to an examinee who is not that physician's patient to exercise care commensurate with the examiner's professional training and experience. The standard of care applicable to the administration of a functional capacities evaluation (FCE) can be established only through expert testimony that takes into account the training and experience of the physical therapist relative to administering the FCE. Romans v. Lusin, 2000 MT 84, 299 M 182, 997 P2d 114, 57 St. Rep. 363 (2000). See also Webb v. T.D., 287 M 68, 951 P2d 1008, 54 St. Rep. 1502 (1997).

Plaintiff's Burden to Establish Prima Facie Case Not Relieved by Res Ipsa Loquitur: In order for the doctrine of res ipsa loquitur to apply, permitting an inference of negligence on the part of one in control of an instrumentality that causes injury, not only must the elements of the doctrine be met, but plaintiff also has the burden of making a prima facie case that defendant breached a duty of care. Here, plaintiff did not establish the standard of care applicable to administration of a functional capacities evaluation through expert testimony, nor did plaintiff establish a breach of the standard by the person who administered the test. Absent a prima facie case, res ipsa loquitur did not apply and summary judgment for defendant was proper. Romans v. Lusin, 2000 MT 84, 299 M 182, 997 P2d 114, 57 St. Rep. 363 (2000). See also Clark v. Norris, 226 M 43, 734 P2d 182, 44 St. Rep. 444 (1987).

Physician's Standard of Care Toward Examinee Sent to Physician by Examinee's Employer or Insurer or by Some Other Third Party: At the request of the workers' compensation insurer of an injured worker's employer, a physician examined the worker. He reported his findings to, and his fee was paid by, the insurer. He wrote the worker a letter telling her that she had a back sprain, that no treatment was needed, and that she had an impairment rating of 2% of the whole person. She went back to work, suffered a severely herniated disc in her back, and has significant physical limitations as a result. She sued the doctor for negligence. He claimed that he did not have a physician-patient relationship with her and therefore had no duty of care toward her. The Supreme Court held that based on 27-1-701, a physician who performs an examination of an employee, insured, or other person at the request of a third party has a duty to exercise the level of care required by the physician's professional training and experience and the duty to exercise ordinary care to: (1) discover those conditions that pose imminent danger to the examinee's physical and mental well-being; (2) take reasonable steps to communicate any such condition to the examinee; and (3) ensure that when the physician advises an examinee about a condition, the advice comports with the standard of care for the profession. The court stated that it was not thereby concluding that the physician has the same duty of care as toward a patient. Webb v. T.D., 287 M 68, 951 P2d 1008, 54 St. Rep. 1502 (1997), followed in Romans v. Lusin, 2000 MT 84, 299 M 182, 997 P2d 114, 57 St. Rep. 363 (2000).

Criminal Acts by Parolee Held Reasonably Foreseeable — Negligence of State Found in Supervising Parolee: Corliss was paroled, after serving time for an execution-style slaying with a handgun, under the condition that he not possess a firearm. While on a visit, with the approval of his parole officer, to Washington state to look for work, Corliss failed to return to Montana within the established time, failed to see a parole officer in Washington, had a temporary restraining order obtained against him by a girlfriend because of threats made to her and her family, and had an altercation with his wife involving a handgun. In neither instance of violence did Corliss's parole officer investigate the circumstances of the violence. Later, Corliss shot and killed one friend of his girlfriend and injured another. Both the estates of the deceased woman and the wounded woman brought actions against the state for negligent supervision of Corliss's parole. Citing Estate of Strever, 278 M 165, 924 P2d 666 (1996), the Supreme Court held that although in the usual case the criminal acts of a third party may not be foreseeable, lack of foreseeability is not established in Montana as a matter of law because the facts of a case may indicate that criminal acts should have been foreseen and held that criminal acts of a third party should be treated like any other intervening superseding act and the foreseeability of that act should be determined by the factfinder. The Supreme Court therefore held that the District Court properly denied the state's motion for a directed verdict. Starkenburg v. St., 282 M 1, 934 P2d 1018, 54 St. Rep. 214 (1997). See also Lopez v. Great Falls Pre-Release Serv., Inc., 1999 MT 199, 295 M 416, 986 P2d 1081, 56 St. Rep. 771 (1999).

Injury While Lifting Door Not Part of Continuous Sequence Establishing Proximate Cause: Bossard injured his arm while lifting a sliding door on Johnson's property back onto its track. The Supreme Court held that although Johnson knew that the door could come off its track, he could not foresee that Bossard would injure his arm lifting the door into place and that therefore there was a link missing in the chain of causation, thus negating proximate cause. Bossard v. Johnson, 265 M 272, 876 P2d 627, 51 St. Rep. 494 (1994).

Licensee or Invitee — Duty of Care: While visiting her son Brian and his family in Texas for the holidays, Doris was asked to show the family home to prospective buyers while Brian was at work. To enhance the appearance of the kitchen, Doris washed and waxed the floor, but she slipped on a wet spot and broke her hip and then sued Brian for negligence. Doris maintained that she was an invitee because her showing the house conferred an economic benefit on Brian and that Brian therefore had a duty to exercise reasonable care to eliminate a condition that posed an unreasonable risk of harm to her, of which he had either actual or constructive knowledge. Brian maintained that his mother was only a licensee because the primary purpose of her visit was to spend time with the family and that the incidental chores undertaken by her as licensee did not convert her status to that of invitee. (See also Prestwood v. Taylor, 728 SW 2d 455 (Tex. Ct. App. 1987).) The trial court properly held that Doris was a licensee because there was no evidence of business dealings between the parties or actual pecuniary benefit to Brian. Brian's liability was conditioned on his actual knowledge that the defect existed and that it was dangerous. (See also St. v. Tennison, 509 SW 2d 560 (Tex. 1974).) Absent proof of his actual knowledge of the dangerous condition, Brian had no duty to warn Doris or to repair the defect. Barrows v. Barrows, 256 M 78, 844 P2d 119, 49 St. Rep. 1145 (1992).

No Duty Owing to Student Injured in Extracurricular Activity During Summer: The plaintiff, a high school student, sustained injuries while attending a privately sponsored summer cheerleading clinic. She sued her high school district as the party responsible for its students during extracurricular activities and as principal of its agent, the cheerleading adviser, for negligent supervision. In the plaintiff's appeal of summary judgment in favor of the school district, the Supreme Court held that a school does not owe a duty to a student for an extracurricular activity during the summer months when the activity is governed by independent parties. Rollins v. Blair, 235 M 343, 767 P2d 328, 46 St. Rep. 39 (1989).

Summary Judgment Proper — No Reasonable Difference of Opinion That Defendant Did Not Cause Injury: Plaintiff parents appealed a summary judgment order in an action alleging a university's negligence caused injury to their minor daughter who had consumed alcohol and was involved in a motorcycle accident while under the supervision of a university program. Although the university assumed a custodial role similar to that of a high school when it undertook to have plaintiffs' daughter live on its campus, supervised by university personnel, and thus was charged with exercising reasonable care, there was no room for a reasonable difference of opinion as to whether someone other than the defendant university was the intervening cause of the daughter's injury. Therefore, summary judgment for the university based on proximate cause was proper. Graham v. Mont. St. Univ., 235 M 284, 767 P2d 301, 45 St. Rep. 2389 (1988).

Questions of Anticipated Harm and Duty of Ordinary Care as Material Issues of Fact — Summary Judgment Improper: In reversing a summary judgment as improper, the Supreme Court found that material questions of fact for a jury existed on the issues of whether: (1) the town of Whitehall should have anticipated that harm would be caused by the condition of the sidewalk despite the knowledge and obviousness of the condition; and (2) the town of Whitehall exercised ordinary care to keep the sidewalk reasonably safe. Even if it appeared that recovery under these issues was very remote, they constituted genuine issues of material fact; therefore, summary judgment was not appropriate. Kaiser v. Whitehall, 221 M 322, 718 P2d 1341, 43 St. Rep. 846 (1986). However, see Yager v. Deane, 258 M 453, 853 P2d 1214, 50 St. Rep. 610 (1993).

Lack of Contract — Breach of Warranty Sounded in Tort Rather Than Contract: Plaintiff was injured in 1979 while spraying weeds. He brought suit in 1984 against the producers, distributors, and sellers of the herbicide and spraying equipment, claiming counts in strict liability in tort, tortious misrepresentation, negligence, and contract for breach of sellers' warranty. Plaintiff had no direct written contract with any of the defendants. The District Court found that there was no contract from which to imply the warranties which plaintiff claimed were breached. The court reasoned that without a contract the breach of warranty claims sounded in tort rather than contract; therefore, the warranty claims were barred by the 3-year tort Statute of Limitations. On appeal, plaintiff contended that one of the longer contract Statutes of Limitations in 27-2-202 or 30-2-725 should apply. The Supreme Court disagreed, noting that the implied covenants of good faith and fair dealing, fitness for a particular purpose, merchantability, and workmanlike performance are imposed by law regardless of contract and that, absent a contract, breach of the implied covenants sounds in tort, not contract. The District Court judgment was affirmed. Bennett v. Dow Chem. Co., 220 M 117, 713 P2d 992, 43 St. Rep. 221 (1986).

"Substantial Factor" Rule to Apply:

The substantial factor rule applies when two causes concur to bring about an injury and either cause would have been sufficient for the result. Thus, it applied in this case when the necessity for amputation of the leg of a state prison inmate could have been caused either by the inmate's preexisting condition of arteriosclerosis of the blood vessels of the legs or by the negligence of doctors treating him for an ingrown toenail. Kyriss v. St., 218 M 162, 707 P2d 5, 42 St. Rep. 1487 (1985).

The Supreme Court stated its approval of the "legal cause" (substantial factor) instruction in this medical malpractice case involving alleged concurrent and subsequent tortfeasors (surgeon, nurses, and radiologist). The court stated that the rule was developed primarily for cases such as the one under consideration in which application of the "but for" (proximate cause) rule would allow each defendant to escape responsibility because the conduct of one or more others would have been sufficient to produce the same result. Rudeck v. Wright, 218 M 41, 709 P2d 621, 42 St. Rep. 1380 (1985), followed in Kyriss v. St., 218 M 162, 707 P2d 5, 42 St. Rep. 1487 (1985).

Contractor's Duty to Subcontractor: Sections 50-71-201 and 50-71-202 require a contractor to furnish a subcontractor with a safe place to work. A subcontractor is an employee of the contractor for purposes of 50-71-201. Cain v. Stevenson, 218 M 101, 706 P2d 128, 42 St. Rep. 1428 (1985).

Surgeon's Failure to Remove Foreign Object Negligence Per Se: In this medical malpractice action, the Supreme Court adopted the rule of negligence per se in holding that a surgeon is negligent as a matter of law when he leaves a foreign object inside his patient during surgery. The surgeon bears the responsibility of the surgical procedure. Other persons also may be negligent and liable as concurrent tortfeasors or subsequent tortfeasors, but the surgeon who initially was negligent and whose original negligence set in motion the concurrent and following negligent acts or omissions should not be allowed to avoid his liability. Rudeck v. Wright, 218 M 41, 709 P2d 621, 42 St. Rep. 1380 (1985), distinguished, with regard to liability for negligent design and supervision of a water pipeline project, in Jim's Excavating Serv., Inc. v. HKM Associates, 265 M 494, 878 P2d 248, 51 St. Rep. 623 (1994).

Jury Instructions — "Locality Rule" Standard Not Relevant for Judging Medical Specialist — "Loss of Chance": Woman sued her doctor, a national board certified orthopedic surgeon, for damages for alleged negligent medical treatment. Defendant had treated plaintiff for misdiagnosed knee problems for 4 months without ordering diagnostic X-rays before referring plaintiff for surgery to out-of-state doctor who discovered a giant cell tumor in plaintiff's knee. Plaintiff alleged that defendant's failure to order diagnostic films early in treatment resulted in her losing any chance to have less radical surgery and preserve her natural knee. Jury returned verdict in favor of defendant, and plaintiff appealed. Supreme Court vacated District Court judgment and remanded for new trial. Supreme Court held that District Court committed reversible error by instructing jury on the "locality rule" as appropriate standard of care rather than giving plaintiff's proposed instruction holding board certified specialists to national standards of the specialty. Supreme Court also held that on retrial, plaintiff is entitled to a "loss of chance" instruction. The trier of fact should determine whether defendant's negligence was a substantial factor in reducing plaintiff's chances of obtaining a better result rather than whether plaintiff would have obtained a better result with earlier diagnosis. Aasheim v. Humberger, 215 M 127, 695 P2d 824, 42 St. Rep. 235 (1985); holding explained and extended to include Board-certified family practitioners in Glover v. Ballhagen, 232 M 427, 756 P2d 1166, 45 St. Rep. 1168 (1988).

Respondeat Superior — Accident Caused by Insurance Agent: Defendant insurance company's agent participated in a Dillon rodeo, went to a barbecue at his Dillon home, and in the evening consumed alcohol at several Dillon bars. On the way home from the bars, he struck plaintiff while driving an auto the agent leased from insurer's wholly owned service company, which had a common board of directors with insurer. Plaintiff sued defendants under respondeat superior. There was evidence agent sold insurance as a result of participating in group recreational and social activities. Summary judgment for insurer was refused because there was a fact question as to whether agent's activities during the night in question were within the course and scope of his work as an insurance agent. However, summary judgment was granted in favor of the service company as there was no evidence that agent was acting as the agent of the service company at the time of the accident. Vollmer v. Bramlette, 594 F. Supp. 243, 41 St. Rep. 1964 (D.C. Mont. 1984).

Employee Suit Against Employer's Parent Corporation — Mere Holding Company Not Liable: Under the workers' compensation law provision that an employee may sue a third party in tort for causing injury to an employee, the employee may sue the parent corporation of a subsidiary corporation for which the employee works but must establish that the parent corporation had an independent duty toward the employee. In the present case, the facts failed to establish that any duty was breached by the parent corporation. The parent corporation was simply a holding company that carried on no business other than operating through its subsidiaries. Any negligence of the subsidiary employer in regard to employee's products liability theory could not be passed on to the parent corporation. Mitchell v. Shell Oil Co., 579 F. Supp. 1326, 41 St. Rep. 278 (D.C. Mont. 1984).

Children Under One's Control — Duty of Care: A father sued YMCA for injury allegedly incurred by his 6-year-old son, who was found submerged in the YMCA pool by a lifeguard. The jury was properly charged that when a person undertakes the control or supervision of a child, he has the duty to use reasonable care to protect the child from injury and that though he is not an insurer of the child's safety he is required to use reasonable care commensurate with the reasonably foreseeable risk of harm to which the child might be subjected while under the person's control and supervision. The instruction expressed the idea that the reasonable care to be accorded must be commensurate with the child's age and maturity. The father's counsel fully argued the proper standard of care, and the father's substantial rights were not prejudiced by failure to give his requested instructions stating that a greater degree of care is owed to a child than to an adult. Johnson v. YMCA, 201 M 36, 651 P2d 1245, 39 St. Rep. 1937 (1982).

Snowbanks — Jury Question: In a customer's suit against a supermarket for injuries sustained when she fell while climbing over a snowbank created by the plowing of the parking lot, summary judgment for the supermarket was reversed and the case remanded for trial, as it could reasonably be inferred that the piling of snow in front of the store entrance increased the hazard created by the natural accumulation of snow and ice and that the supermarket should have anticipated the injuries received as a result of the dangerous condition. The snowbank was between the parking lot and the store and had a path cut through it that customer did not use as it had a water puddle in it and she assertedly believed she could not step over it. Cereck v. Albertson's, Inc., 195 M 409, 637 P2d 509, 38 St. Rep. 1986 (1981), overruled, as to the distinction between liability based upon natural versus altered accumulations of ice or snow that are open and obvious and as to the standard that a property owner is absolved of liability because a dangerous condition upon the premises is open and obvious, in Richardson v. Corvallis Pub. School District No. 1, 286 M 309, 950 P2d 748, 54 St. Rep. 1422 (1997).

Snowbanks From Plowing Parking Lot — Duty of Property Owner: A property owner may be held liable for falls on accumulations of ice and show where the hazard created by the natural accumulation is increased or a new hazard is created by an affirmative act of the property owner; even where such a condition is actually known or obvious, a property owner may be held liable if he should have anticipated that injuries would result from the dangerous condition. Cereck v. Albertson's, Inc., 195 M 409, 637 P2d 509, 38 St. Rep. 1986 (1981), overruled, as to the distinction between liability based upon natural versus altered accumulations of ice or snow that are open and obvious and as to the standard that a property owner is absolved of liability because a dangerous condition upon the premises is open and obvious, in Richardson v. Corvallis Pub. School District No. 1, 286 M 309, 950 P2d 748, 54 St. Rep. 1422 (1997).

Availability of Affirmative Defenses to Railroad — Absolute Liability: Plaintiff was employed by a subsidiary of Burlington Northern and was injured in an accident involving Burlington's railroad cars. The Supreme Court decided the federal Safety Appliance Act applied despite the fact the railroad cars involved in the accident were on a siding where loading operations were handled by the subsidiary. Noting that the U.S. Supreme Court has declared that the question of whether a railroad can assert contributory negligence or assumption of risk as a defense in a case involving a nonrailroad employee depends entirely on state law, the Supreme Court cited its 1966 holding that, where the theory of absolute liability applies, liability is established when it is proved that a statute has been violated and there is a proximate cause connection between the violation and the resulting injuries. Proximate cause in a case under the Safety Appliance Act is decided using the definition that prevails under state law. Comparing the 1966 case under the Scaffolding Act with this case, the Supreme Court denied the defendant the two defenses. The Supreme Court also noted that railroad employees are entitled to a more liberal standard imposing liability than nonrailroad employees. Reynolds v. Burlington N., 190 M 383, 621 P2d 1028, 37 St. Rep. 1883 (1980).

Duty to Provide Safe Working Place — Railroad Employee: In a case brought by an employee injured while working for a subsidiary of a railroad, the Supreme Court held that the plaintiff was owed the duty to provide him with a safe place to work. Noting that giving the jury information about the subsidiaries might well have been highly prejudicial to the defendant railroad, the Supreme Court nonetheless felt obliged to consider it in this case. The plaintiff was working directly in the operations of the railroad in every sense of the word. The railroad would not be absolved of the responsibility to provide a safe place to work for employees who are technically employed by a subsidiary corporation but whose employment is directly related to the operations of a railroad. Closeness of the businesses of the parent and subsidiary companies was a factor in the court's conclusion that both corporations owed the duty to provide the plaintiff with a safe place to work. Reynolds v. Burlington N., 190 M 383, 621 P2d 1028, 37 St. Rep. 1883 (1980), distinguished in Thornock v. Pack River Management Co., 227 M 524, 740 P2d 1119, 44 St. Rep. 1284 (1987).

Corporate Employee: Where employee of foreign corporation allegedly placed crate of oranges in aisle of corporation's store resulting in injury to customer when he tripped over the crate, action against foreign corporation and its resident employee, who was joined as John Doe, was not served with process, and did not appear, was not removable by corporation to federal court on ground of diversity of citizenship. Jensen v. Safeway Stores, Inc., 24 F. Supp. 585 (D.C. Mont. 1938).

INJURY TO PROPERTY

Nuisance Action Based on Negligence — Elements of Claim: A woman used hanging bird feeders, ground feeding, and a heated bird bath to attract birds to her property. Her neighbor supplied evidence that the birds congregated on their shared property line and created a high level of excrement, feathers, carcasses, and noise. The Justice Court concluded that although the woman's activities may not have created a nuisance in different surroundings, the close proximity of the properties, the power line running between the yards, the distribution of trees, and the manner of feeding created a nuisance under the circumstances. The Supreme Court upheld the Justice Court's conclusion that the elements of nuisance were satisfied in this situation,. The Supreme Court noted that a nuisance action based on negligence consists of something done lawfully but so carelessly or negligently as to create a potential for harm to another, and all persons have a general duty of care to abstain from injuring the person or property of another. The Supreme Court found that the remedy imposed by the Justice Court was overly broad and substituted a narrower injunction in order to avoid depriving the woman of the enjoyment of her property. Simpkins v. Speck, 2019 MT 120, 395 Mont. 509, 443 P.3d 428.

Negligence During House Moving — Breach of House Moving Agreement — Remand for Determination of Causation and Damages: Kelly entered an agreement with Hall to move four of Kelly's housing units. Hall agreed to obtain cargo insurance on each unit but did not do so. During the move, two units were damaged, and Kelly filed a claim against Hall's insurer for remuneration. The claim was denied, and the insurer sought a declaratory judgment against both Hall and Kelly. Kelly filed negligence and breach of contract claims against Hall, and Hall counterclaimed for breach of contract against Kelly. The District Court concluded that Kelly failed to establish negligence, that both parties breached the contract, and that neither party could recover against the other. On appeal, the Supreme Court affirmed the finding that Hall breached the contract by failing to obtain cargo insurance and that, based on the presumption against conditions precedent and inconclusive evidence, Kelly also breached the contract and thus could not recover breach of contract damages. However, there was no evidence to rebut Kelly's negligence claim, nor did the District Court address the damages that Hall conceded occurred during the move. Because it was error to find that Kelly failed to establish negligence, the case was remanded for trial on causation and damages. Scottsdale Ins. Co. v. Hall, 2003 MT 188, 316 M 460, 73 P3d 819 (2003).

Mortgagee's Right to Assert, on Mortgagee's Behalf, Mortgagor's Contract and Tort Claims for Damage to Property: The mortgagee alleged that the engineering firm hired by the mortgagor knowingly laid improper pipe in the land, resulting in the state's disapproval of the pipe. The mortgagee could not sue the engineering firm for breach of contract and for breach of professional duty owed to the mortgagor under the theory that the mortgagee was a direct creditor of the mortgagor and was entitled to execute on any asset of the mortgagor and that the contract and breach of professional duty claims were assets. The mortgagee would have to be a judgment creditor of the mortgagor with a claim against the mortgagor that had been reduced to judgment before the mortgagee could sue the engineering firm for breach of the firm's contract with and professional duty to the mortgagor. Turner v. Kerin & Associates, 283 M 117, 938 P2d 1368, 54 St. Rep. 522 (1997).

Mortgagee's Right to Sue Mortgagor and Third Party for Impairment of Security Interest — Suit by Mortgagee Acquiring Security Interest After Damage by Third Party: A mortgagee can sue a mortgagor for actions or inactions that impair the mortgagee's security interest. The mortgagee can also sue a third party for damage to the property that impairs the security interest. In this case, a mortgagee who acquired mortgages from a prior mortgagee could sue a third party in tort for impairment of the security interest caused by damage to the property that occurred while the prior mortgagee held the mortgages. Allowable damages are the extent of the outstanding debt. The third party was an engineering firm alleged to have knowingly laid improper pipe in a subdivision. The state refused to approve the pipe. Turner v. Kerin & Associates, 283 M 117, 938 P2d 1368, 54 St. Rep. 522 (1997).

Damage to Prescriptive Easement — Injunction Denied: The District Judge properly denied the plaintiffs' request for an injunction and their claim for damages for rutting and disrepair of the roadway where the testimony showed that plaintiffs kept the roadway up despite use of it by defendants and defendants' use of the roadway was consistent with defendants' interest in the land. Marta v. Smith, 191 M 179, 622 P2d 1011, 38 St. Rep. 28 (1981).

Negligence in Maintenance of an Irrigation Ditch: Although plaintiff's contention that an owner of an irrigation ditch is not an absolute insurer is correct where the testimony shows: (1) that there were erosion and cutting away of the cross-claimants' soil on both sides of the ditch; (2) that there had been "bad washing"; and (3) that it would take $5,500 to make the irrigation system suitable to prevent further washing on cross-claimants' land and to repair past damage, there was substantial evidence to support the findings of negligence and damages of $5,500. Marta v. Smith, 191 M 179, 622 P2d 1011, 38 St. Rep. 28 (1981).

Trespass: Where defendant had plaintiffs' permission to enter upon plaintiffs' land for seismograph operations and defendant, after protests by the plaintiff landowners, caused explosions which damaged a spring, defendant was a trespasser ab initio and could be liable irrespective of negligence. Francis v. Sun Oil Co., 135 M 307, 340 P2d 824 (1959).

28-1-202. Obligation of one who unilaterally decides to render service.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

28-1-203. Enforcement of obligations arising by operation of law.

Case Notes

No Reference to Unfair Claim Settlement Practices Statute — Remand — Suspension of Proceedings Pending Determination of Liability: Appellant Fode asked the Supreme Court to recognize the common-law duty of good faith and fair dealing imposed by 28-1-201 and 28-1-203 without reference to 33-18-201, the unfair claim settlement practices statute. In remanding the case, the court found that Fode's allegations contained in his complaint should be presented to the District Court to determine whether a cause of action existed under 33-18-201; however, all proceedings were suspended until liability was determined in the underlying case. Fode v. Farmers Ins. Exch., 221 M 282, 719 P2d 414, 43 St. Rep. 814 (1986), distinguished in Peris v. Safeco Ins. Co., 276 M 486, 916 P2d 780, 53 St. Rep. 481 (1996).

Where Contractual Obligation Not Assumed by Defendant, Suit for Breach Wrong Remedy: Where receiver of vendor company assigned contract of sale to another company without assumption by the latter of the vendor's obligation thereunder and assignee sold the property to a third person subject to the rights of the deceased owner's estate, in a suit for breach of contract against the assignee company by the personal representatives of the deceased purchaser, judgment for plaintiff was erroneous in absence of proof that defendant had assumed the obligations of the vendor. Under the facts, the assignee became a trustee for the original vendee by operation of law. Thompson v. Lincoln Nat'l Life Ins. Co., 114 M 521, 138 P2d 951 (1943), followed, with regard to lack of implied assumption of contractual obligations absent assignment of contractual rights, in Davey v. Nessan, 252 M 397, 830 P2d 92, 49 St. Rep. 294 (1992).

28-1-211. Implied covenant of good faith and fair dealing.

Compiler's Comments

Applicability: Section 2 of Ch. 571, L. 1987, provided: "This act applies to causes of action arising after the effective date of this act." Effective July 1, 1987.

Case Notes

DECISIONS AFTER 1987 ENACTMENT

State-Mandated Reduction in Compensation for Contract Attorneys — Memorandum of Understanding — No Violation of Contract Clause — Budget Cut Reductions Permissible: The petitioners were attorneys who contracted with the office of state public defender (OPD) to provide legal services for indigent clients. To become an OPD contract attorney, the petitioners signed a contract, referred to as a memorandum of understanding (MOU), with OPD. In March 2018, OPD announced a reduction to the hourly contract rate and a reduction of pay for case-related travel time in order to implement budget cuts effective for any services rendered on or after April 1, 2018. The petitioners pursued a class action lawsuit in District Court against the state, seeking declaratory relief, injunctive relief, and damages for breach of contract and violation of the contract clause in Art. II, sec. 31, Mont. Const. The state, in turn, filed a motion for summary judgment based on legal interpretation of the MOU under contract law. The District Court granted the state's motion and the Supreme Court affirmed, reasoning that nothing in the MOU indicated that the compensation rates were locked in place for the duration of the petitioners' representation. Additionally, the MOU's language clearly provided for prospective modification of compensation rates at the state's discretion, which was limited by both 47-1-121 and the implied covenant of good faith and fair dealing. Brooke v. St., 2020 MT 187, 400 Mont. 435, 468 P.3d 351.

Covenant of Good Faith and Fair Dealing — Properly Pleaded When Existence of Contract Alleged: A mortgagee obtained a loan for a residential property and fell behind on payments. The mortgagee contacted the bank for assistance to modify monthly payments, and alleged that the bank instructed her to stop making monthly mortgage payments in order to qualify for a loan assistance program. The mortgagee stopped making payments but never qualified for the assistance program. The mortgagee defaulted on the loan but continued to reside on the property. The mortgagee received at least nine notices of sale over an 8-year period, each of which, the mortgagee alleged, accelerated all amounts due. The deed of trust contained a provision stating the procedure that the lender was required to follow to provide notice to the mortgagee prior to accelerating the loan. As a result, the mortgagee sued, alleging six causes of action, one of which was a breach of the implied covenant of good faith and fair dealing, based in contract and based on the "special relationship" criteria giving rise to a tort. The District Court dismissed the mortgagee's breach of contract claims. On appeal, the Supreme Court reversed, determining that because the mortgagee alleged that a contract existed and created a special relationship, and that the lender breached the implied covenant by not acting honestly and failing to observe reasonable commercial standards of fair dealing, the mortgagee sufficiently pleaded both a contractual breach of the implied covenant and a tortious breach of the implied covenant sufficient to survive a Rule 12(b)(6), M.R.Civ.P. (Title 25, ch. 20), motion. Puryer v. HSBC Bank USA, 2018 MT 124, 391 Mont. 361, 419 P.3d 105.

No Duty to Recover Funds Under Contract — No Breach of Contract or Covenant of Good Faith and Fair Dealing — Statute of Limitations for Equitable Relief Expired: The plaintiff contracted with Bancard Services, Inc. (Bancard), one of the defendants, for Bancard to provide processing services to the plaintiff's ATMs located throughout Montana. Bancard subcontracted with a third-party payment processor to assist in processing transactions, and an agent of the third party made a data entry error that transferred $285,000 of the plaintiff's funds to an out-of-state individual, Leland Ruzicka, and B&B Lounge (collectively Ruzicka), also defendants in the case. Bancard was able to recover all but $35,000 of the plaintiff's funds. Eventually, the plaintiff sued both Bancard and Ruzicka for the outstanding $35,000. The plaintiff also filed several contractual related claims against Bancard. The District Court granted summary judgment to the defendants because Bancard did not have an obligation to recover the funds under the parties' contract and because the statute of limitations had expired on the unjust enrichment claims against Ruzicka. Grizzly Sec. Armored Express, Inc. v. Bancard Serv., LLC, 2016 MT 287, 385 Mont. 307, 384 P.3d 68.

Tortious Breach — Existence of Contract Required: A claim for tortious breach of the implied covenant of good faith and fair dealing was based on an alleged, invalid oral contact that modified an existing, written contract. Because the claim of tortious breach was based on the invalid oral modification, the court properly granted summary judgment to the defendants. Morrow v. Bank of America, N.A., 2014 MT 117, 375 Mont. 38, 324 P.3d 1167, following Knucklehead Land Co., Inc. v. Accutitle, Inc., 2007 MT 301, 340 Mont. 62, 172 P.3d 116.

Covenant of Good Faith and Fair Dealing — No Application When Terminated Policy Not Part of Employment Contract: A hospital discontinued a policy whereby it paid employees for their sick leave after 25 years of service. Employees with less than 25 years of service sued the hospital for breach of the covenant of good faith and fair dealing. The District Court granted the hospital summary judgment, and the Supreme Court affirmed. Because the policy at issue was not a part of the employment contract, the courts concluded that the covenant of good faith and fair dealing did not apply. Chipman v. NW. Healthcare Corp., 2014 MT 15, 373 Mont. 360, 317 P.3d 182.

Absence of Evidence of Violation of Standards of Commercial Reasonableness — Implied Covenant of Good Faith and Fair Dealing Not Breached: Plaintiff contended that defendant title companies breached the implied covenant of good faith and fair dealing during a foreclosure sale. Plaintiff presented an expert who opined that defendants did not conduct the sale in the same manner as the expert, but offered no conclusion that defendants' administration of the sale demonstrated a violation of accepted and reasonable commercial standards. Absent evidence of defendants' failure to act in accordance with industry practices, the District Court did not err in holding that defendants did not breach the implied covenant of good faith and fair dealing. Knucklehead Land Co., Inc. v. Accutitle, Inc., 2007 MT 301, 340 M 62, 172 P3d 116 (2007).

Justifiable Cause to Terminate Contractual Relationship — No Breach of Contract or Tortious Interference With Business Relations: In 2000, optometrist Hardy enrolled as a Vision Service Plan (VSP) member with defendant. The agreement provided for automatic annual renewal unless either party terminated the agreement, or VSP could terminate the agreement at any time if Hardy failed to comply with VSP policies, rules, and procedures. One condition for continued membership was that the member maintain majority ownership and complete control of all aspects of the optometric practice. Unbeknownst to VSP, Hardy had previously entered a franchise agreement with another optical supplier that contravened certain provisions of the VSP agreement, so VSP terminated Hardy's agreement. Hardy sued VSP, alleging breach of contract and tortious interference with Hardy's business relations. The District Court granted summary judgment to VSP, and Hardy appealed, but the Supreme Court affirmed. Hardy had no justifiable expectation of a continued contractual relationship with VSP after breaching VSP's policies. The VSP agreement was unambiguous as a matter of law, and VSP had just cause to terminate the agreement based on Hardy's actions in enrolling as a franchisee with another company on terms that violated the VSP agreement. Hardy's tortious interference claim also failed absent evidence that VSP unlawfully engaged in activities to damage Hardy's business. Summary judgment for VSP was proper. Hardy v. Vision Serv. Plan, 2005 MT 232, 328 M 385, 120 P3d 402 (2005).

Summary Judgment on Breach of Contract Affirmed — Wrongful Discharge Claim Reversed for Determination of Whether Claimant Was Employee or Independent Contractor: Tvedt brought a claim for breach of contract, wrongful termination, and indemnification of expenses, alleging that defendant group had breached the covenant of good faith and fair dealing, waived the at-will clauses in their employment agreement, and mischaracterized Tvedt as an independent contractor, rather than an employee. Defendant group moved for summary judgment and filed a contingent counterclaim stating that in the event that Tvedt was found to be defendant group's employee, then defendant group's obligation to pay Tvedt the contract value should cease and all payments made to Tvedt should be returned. The District Court determined that Tvedt was not an employee and granted summary judgment to defendant group on all claims, and Tvedt appealed. The Supreme Court affirmed summary judgment on the breach of covenant issue because Tvedt was given adequate notice of termination, defendant group was exercising the specific language of the at-will termination provision of the contract, and Tvedt did not demonstrate that defendant group had waived the right to enforce that provision. However, the court reversed summary judgment on the wrongful discharge claim because the District Court incorrectly applied defendant group's novation argument and because genuine issues of fact remained whether Tvedt was an employee or independent contractor and whether a manager's agreement that recognized Tvedt individually was in effect at the time of termination. Remand was ordered because the District Court never considered whether Tvedt was entitled to relief for wrongful discharge as a matter of law and, if so, whether the claim for indemnification was appropriate. Tvedt v. Farmers Ins. Group of Co., 2004 MT 125, 321 M 263, 91 P3d 1 (2004).

No Duty of Insurer to Notify Claimant of Limitation on Workers' Compensation Medical Benefits: Wiard's workers' compensation benefits were terminated because of failure to file a medical claim within the 60-month period required in 39-71-704. Wiard contended that the failure of the insurer to notify him of the statutory limit violated Title 33, ch. 18, commonly known as the Unfair Trade Practices Act, and the implied covenant of good faith and fair dealing. The Supreme Court disagreed. The rights and duties of the parties were imposed by the provisions of the Workers' Compensation Act, and nothing in that Act established an affirmative duty on the insurer to inform Wiard of the 60-month limitation on the duration of his medical benefits. Wiard v. Liberty NW. Ins. Corp., 2003 MT 295, 318 M 132, 79 P3d 281 (2003).

When Claim for Relief Accrues for Failure of Construction Contract to Be Awarded to Lowest Bidder — No Negligence by Engineering Firm in Handling of Bidding Process on Public Works Contract: The city of Glasgow hired an engineering firm to prepare plans, specifications, and bid documents for a municipal sewer improvement project, including review of bid results and bid award recommendations. Debcon, Inc. (Debcon), submitted the lowest bid, but the engineering firm's review showed significant mathematical errors in Debcon's bid and some question as to the ability of Debcon to perform. The engineering firm recommended that the contract be awarded to a different bidder, and Debcon sued both the city and the engineering firm, alleging negligence in the award of the construction contract. The District Court concluded that Debcon lacked standing to assert a duty of care owed to it by the city and that the negligence claim against the engineering firm must also fail as a matter of law because the firm owed no duty of care to Debcon, an essential element for asserting negligence as a claim for relief. Debcon did not appeal the judgment in favor of the city, but did appeal the judgment in favor of the firm. The Supreme Court cited a long line of cases back to 1910 for the proposition that, absent a duty, no breach of duty can be established and no negligence action can be maintained. An unsuccessful bidder has no standing in mandamus or otherwise to control the discretion in the award of a contract to the lowest responsible bidder, which may not be the lowest pecuniary bidder. A claim for relief from the award of a public contract accrues under the following conditions: (1) plaintiff must timely assert its claim as an aggrieved taxpayer; (2) the claim must seek a remedy, such as an injunction, writ of mandamus, or declaratory judgment, that will protect the rights of the aggrieved taxpayer from the potential harm that will occur; and (3) plaintiff must then show that the process by which the public works contract was awarded resulted from an abuse of discretion, i.e., that discretion was tainted by an act of bad faith, fraud, corruption, or arbitrariness. The Supreme Court in this case declined to follow Debcon's contention that a new duty of care should be constructed from whole cloth that would allow Debcon, as the aggrieved low bidder, to recover lost profits or other expectancy damages under a negligence theory. The District Court properly concluded that the engineering firm, serving as project engineer for the city of Glasgow, did not owe Debcon, as a failed bidder, a duty of care in its handling of the public works contract bidding process under a negligence theory. Debcon's claim for relief was a claim for which relief could not be granted as a matter of law. Further, Debcon did not enjoy contractual privity with the engineering firm, so absent a statutory provision that would sustain a bad faith claim, a claim of bad faith did not lie. Summary judgment in favor of the engineering firm was proper. Debcon, Inc. v. Glasgow, 2001 MT 124, 305 M 391, 28 P3d 478 (2001), following O'Brien v. Drinkenberg, 41 M 538, 111 P 137 (1910), and its progeny, Koich v. Cvar, 111 M 463, 110 P2d 964 (1941), and State ex rel. Sletten Constr. Co. v. Great Falls, 163 M 307, 516 P2d 1149 (1973), and followed, with regard to standing to challenge the letting of a contract to provide public school transportation, in Hickey v. Baker School District No. 12, 2002 MT 322, 313 M 162, 60 P3d 966 (2002).

Lawsuit by Shareholder Causing Damages Considered Breach of Fiduciary Duty of Care: Sletteland brought a suit against two other corporate shareholders for charging excessive attorney fees and seeking their removal as corporate directors. The District Court held that the fees were excessive, but found no grounds for removal. The other shareholders filed a counterclaim against Sletteland, alleging that he breached his fiduciary duty in bringing the lawsuit because the timing of the suit caused refinancing of a project to fail, resulting in damage to the corporation and to other shareholders. The District Court agreed, and both parties appealed their respective issues. The Supreme Court reversed on the issue of excessive fees, but affirmed on the issue of breach of fiduciary duty. The fiduciary duty between shareholders of a close corporation is one of utmost good faith and loyalty. Sletteland admittedly knew of the refinancing and, as an attorney and investment banker, also knew the effect that a lawsuit alleging misconduct by board members would have on a refinancing effort. In fact, it appeared that the suit was brought to specifically derail the refinancing. Sletteland was the person who determined the timing of the suit, which was filed immediately before the individuals involved in the refinancing were to meet for discussions, and when asked to withdraw the suit so refinancing could conclude, he refused to do so. Sletteland did not use the care that an ordinarily prudent person would use in a similar situation, resulting in the breach of fiduciary duty. The Supreme Court also affirmed the award of damages. Although future damages could not be calculated exactly in this case, the District Court did not abuse its discretion in basing its calculations on expert testimony of a well-known regional economist. Sletteland v. Roberts, 2000 MT 382, 304 M 21, 16 P3d 1062, 57 St. Rep. 1639 (2000).

Real Estate Sale — Alleged Breach of Covenant Held Not to Require Expert Testimony: May sued a Bozeman real estate company and agent over the terms of the sale of his property, alleging a breach of the covenant. The Supreme Court held that the District Court improperly dismissed the claim and held that expert testimony was not necessary to establish reasonable commercial standards. The Supreme Court also held, distinguishing Crenshaw v. Bozeman Deaconess Hosp., 213 M 488, 693 P2d 487 (1984), that if the duty of good faith and fair dealing requires both honesty and commercially reasonable conduct, then that duty can be breached by dishonesty or commercially unreasonable conduct and that it does not require expert testimony to prove dishonesty. Because the Supreme Court had held that there was sufficient evidence of fraud to survive a summary judgment motion, the Supreme Court also held that there was sufficient evidence of breach of the covenant to survive that motion and reversed the District Court. May v. ERA Landmark Real Estate of Bozeman, 2000 MT 299, 302 M 326, 15 P3d 1179, 57 St. Rep. 1256 (2000).

Federal Preemption:

In a case involving discharge from employment from a job covered by a collective bargaining agreement and the federal Railway Labor Act, the Supreme Court held, citing Foster v. Albertsons, Inc., 254 M 117, 835 P2d 720 (1992), that a claim for the breach of the covenant of good faith and fair dealing is preempted by federal law because the covenant arises out of the employment contract and that that contract, in the case of a collective bargaining agreement, is governed by federal law. However, the Supreme Court reversed the District Court on dismissal of a common-law wrongful discharge claim, citing Foster for the proposition that a common-law claim, because it does not depend upon interpretation of the employment contract, is an independent claim and is not preempted by the federal Railway Labor Act. Winslow v. Mont. Rail Link, Inc., 2000 MT 292, 302 M 289, 16 P3d 992, 57 St. Rep. 1238 (2000).

The method of handling a claim filed under the Federal Employees Health Benefits Act is governed exclusively by that federal Act and is not subject to a state law that imposes an implied covenant of good faith and fair dealing. Nitschke v. Blue Cross of Mont., 45 St. Rep. 229 (1988); opinion withdrawn but issue affirmed in Nitschke v. Blue Cross of Mont., 231 M 113, 751 P2d 175, 45 St. Rep. 473 (1988).

Failure to Effectuate Insurance Settlement in Good Faith as Independent Cause of Action: Under 33-18-201, an insurer is required to attempt in good faith to effectuate prompt, fair, and equitable settlements of claims in which liability has become reasonably clear. A violation of this provision gives rise to an independent cause of action under 33-18-242. Because the continuing duty of good faith is not ended by commencement of a lawsuit by an insured, that duty can be breached by an insurer's postfiling conduct, including the actions of attorneys conducting the insurer's defense. Amendment of the claim to include an action under 33-18-242 related back to the original claim and was properly allowed. Further, third-party defendant's alleged failure to conduct a reasonable investigation and its subsequent refusal to pay the claim, although occurring more than 2 years before commencement of plaintiff's cause of action, were, if proved, ostensibly part of the bad faith postjudgment conduct. Thus, the evidence of those acts was not time-barred. Federated Mut. Ins. Co. v. Anderson, 1999 MT 288, 297 M 33, 991 P2d 915, 56 St. Rep. 1152 (1999), following Safeco Ins. Co. v. Ellinghouse, 223 M 239, 725 P2d 217, 43 St. Rep. 1689 (1986), and Palmer v. Farmers Ins. Exch., 261 M 91, 861 P2d 895, 50 St. Rep. 1210 (1993).

Exceptions to Requirement for Matching Terms in Offer Made Under Right of First Refusal: A right of first refusal does not give the rightholder the power to compel an unwilling owner to sell, but merely requires the owner, when and if a decision is made to sell, to offer the property first to the rightholder at the stipulated price. The preemptive right ripens into an option when the owner elects to sell, at which point the owner has the contractual obligation to offer the property to the optionee on the same terms and conditions as the offer made to the owner by a third party. (See 77 Am. Jur. 2d Vendor Purchaser § 40 (1997).) In order that each party to the contract receives the benefit bargained for, under Miller v. LeSea Broadcasting, Inc., 87 F3d 224 (7th Cir. 1996), three exceptions to the requirement for the exact matching of terms have been recognized: (1) the grantor of the option can waive exact matching; (2) proper names need not be matched; and (3) the grantor of the option may not act in bad faith, including procuring from the third party terms that the grantor knows are unacceptable to the optionee for the purpose of discouraging exercise of the right of first refusal. As long as the conditions of the sale are commercially reasonable, imposed in good faith, and not specifically designed to defeat the right of first refusal, the optionee is obliged to match the offer if the right is to be exercised. Here, although attorneys for the parties engaged in discussions concerning whether poison pill provisions included in an offer were an attempt to dissuade exercise of the right of first refusal, the discussions were not found to impact the effective exercise of the right, so the District Court's conclusion that the right had been properly exercised was not in error. Kennedy v. Dawson, 1999 MT 265, 296 M 430, 989 P2d 390, 56 St. Rep. 1078 (1999). See also Story v. Bozeman, 242 M 436, 791 P2d 767, 47 St. Rep. 850 (1990), and Lee v. Shaw, 251 M 118, 822 P2d 1061 (1992).

Agricultural Lease — No Error in Failure to Give Instruction on Implied Contract Covenant to Farm in Workmanlike Manner — Express Lease Terms Stricter Than Requested Instruction on Implied Term: The Schumachers leased property that they owned to Stephens through an agricultural lease. The lease required Stephens to farm with "diligence and care" and to do "all work necessary . . . and to the best interest of lessor, all in such time and manner as shall be to the best advantage and economy". The Schumachers sued Stephens, alleging that Stephens breached the implied contract covenant of good faith and fair dealing. The District Court refused to give the Schumachers' requested instruction on an implied covenant in the lease that would have required Stephens to farm the property in a "competent, skilled, workmanlike and husbandlike fashion". The Supreme Court noted that: (1) the District Court was correct in not giving an instruction on negligence because the Schumachers' complaint and evidence contained no such theory; (2) the District Court did instruct on the implied covenant of good faith and fair dealing; (3) the standard of care required of Stephens was expressly stated in the lease itself; and (4) the Schumachers had not shown that they were prejudiced by the failure to give the requested instruction. For these reasons, the Supreme Court held that it was not error for the District Court to refuse to give an instruction on an implied covenant to farm in a workmanlike manner. Schumacher v. Stephens, 1998 MT 58, 288 M 115, 956 P2d 76, 55 St. Rep. 247 (1998).

Agricultural Lease — No Error in Failure to Give Plaintiffs' Instruction on Effect of Material Participation Provisions — Instruction on Mutual Cooperation Held Sufficient: The Schumachers leased property that they owned to Stephens through an agricultural lease. Later, when the Schumachers sued Stephens over Stephens' failure to comply with the terms of the lease, Stephens claimed in defense that the Schumachers had breached the material participation agreements in the lease and that therefore he was excused from compliance. The Schumachers requested an instruction stating that if the jury found that Stephens failed to cooperate with the plaintiffs, then Stephens was not entitled to claim that he was excused from liability because of his contention that the Schumachers breached the material participation agreements in the lease. The District Court refused to give the instruction and instead gave an instruction stating that "the failure of a party to fully perform a contract is excused if his performance is prevented or delayed by the conduct of the other party". The Supreme Court noted that the Schumachers had not shown that they were prejudiced in any way by the failure of the District Court to give the requested instruction. Citing Fillinger v. NW. Agency, Inc., of Great Falls, 283 M 71, 938 P2d 1347 (1997), the Supreme Court held that: (1) a party assigning error to a refused instruction must show that the party was prejudiced by the refusal; and (2) the refused instruction must be reviewed in the context of the instructions that were given and the evidence produced at trial. Under these standards, the Supreme Court held that the instruction given by the District Court was sufficient. Schumacher v. Stephens, 1998 MT 58, 288 M 115, 956 P2d 76, 55 St. Rep. 247 (1998).

Covenant of Good Faith and Fair Dealing Not Breached When Mortgage Allowed Partial Release: Because the bank did not owe a duty to the mortgagors to maintain the mortgage contract until full payment of the debt, the mortgagors were not deprived of a contractual benefit when the bank partially released the mortgage. Therefore, the mortgagors could not successfully claim breach by the bank of the implied covenant of good faith and fair dealing. The claim did not relate to the contract but rather to peripheral aspects of the mortgagors' relationship with the bank. Weldon v. Mont. Bank, 268 M 88, 885 P2d 511, 51 St. Rep. 1178 (1994).

Failure to Conform With Literal Language of Administrative Rule Not Illegal and Therefore Not Justification for Breach of Contract: Lewis subcontracted to do the electrical work on five units being built by Huyser. In the first four units, some of the rough-in wiring was covered, but the electrical inspector did not require that all the wiring be visible even though the literal language of the administrative rule indicated that it should be. On the fifth unit, shelving had been installed before the inspection. Lewis insisted that it all be taken down, claiming that he could lose his license if it was not. Huyser had some of the shelving removed, exposing some of the rough-in wiring. Lewis refused to complete the work, and Huyser hired another electrician to complete the job. Lewis sued for payment, and Huyser counterclaimed. The lower court found for Huyser on the basis that the inspector had informed Lewis that he would not lose his license and that the inspector would accept part of the rough-in wiring being exposed. The Supreme Court affirmed, holding that the administrative rule should be reasonably interpreted to allow for waiver by the inspector of the requirement that all rough-in wiring be exposed. The Supreme Court further held that violation of the rule was not a statutory ground for losing an electrical license. The rule having been waived, the contract was not contrary to the policy of express law so that Lewis had a good faith duty to perform the remainder of the contract. Lewis v. Huyser, 264 M 141, 870 P2d 95, 51 St. Rep. 192 (1994).

Extent of Obligation of Good Faith and Fair Dealing Measured by Justifiable Expectations of Parties: Talley argued that because the covenant of good faith and fair dealing is implied into every contract, the community college that employed him as a part-time instructor breached the covenant by not hiring him back after his term contract expired. However, the nature and extent of the obligation of good faith and fair dealing is measured by the justifiable expectations of the parties. Because Talley's contract had a "no-tenure" clause that precluded any justifiable expectation of continued employment, allegations of breach of the covenant of good faith and fair dealing were not reasonable. Talley v. Flathead Valley Community College, 259 M 479, 857 P2d 701, 50 St. Rep. 889 (1993).

Rights Under Written Contract Not Obliterated by Implied Obligation — Nonrenewal of Term Contract: Farris was hired under a term contract that lasted 1 year. The contract provided for nonrenewal with adequate notice. After signing term contracts for 3 consecutive years, Farris was notified that employment would be discontinued. Farris sought to invoke the implied covenant of good faith and fair dealing, contending that the employer's oral negotiations implied permanent employment and objective manifestations of job security. However, consideration of the oral negotiations was barred by the parol evidence rule of 28-2-904, under which oral stipulations are superseded by a written contract. Consideration of representations of permanent employment made after the contract was signed was barred by 28-2-1602, which allows only written or executed oral agreement to affect the validity of a written contract. The Supreme Court cited Carma Developers v. Marathon Dev. Calif., Inc., 826 P2d 710 (Calif. 1992), for the proposition that no obligation can be implied that would result in the obliteration of a right expressly given under a written contract. In interpreting a contract, an implication should not be made when the contrary is indicated in clear and express words. Farris v. Hutchinson, 254 M 334, 838 P2d 374, 49 St. Rep. 717 (1992), distinguishing at-will dismissal under a written contract in Stark v. Circle K Corp., 230 M 468, 751 P2d 162 (1988), and Prout v. Sears, Roebuck & Co., 236 M 152, 772 P2d 288 (1989), and followed in Talley v. Flathead Valley Community College, 259 M 479, 857 P2d 701, 50 St. Rep. 889 (1993).

No Bad Faith When Party Takes Advantage of Transaction Structure in Real Estate Transaction: An insurer who was a party to a real estate transaction did not breach the implied covenant of good faith by telling the insureds that it was considering taking a deed in lieu of foreclosure and later deciding to proceed with strict judicial foreclosure. The insurer's availing itself of the structure of the transaction as established by the agreement, made while insureds were represented by counsel, did not rise to the level of a bad faith violation of either the arbitrary, capricious, or unreasonable standard of Nicholson v. United Pac. Ins. Co., 219 M 32, 710 P2d 1342 (1985), or the dishonesty or commercial unreasonableness standard of Story v. Bozeman, 242 M 436, 791 P2d 767 (1990). Davey v. Nessan, 252 M 397, 830 P2d 92, 49 St. Rep. 294 (1992).

Bank's Failure to Advance More Money Under Line of Credit: Bank refused an additional loan requested by borrowers who already had a line of credit, stating that borrowers' only business customer and sole source of income for repayment of the line of credit was 84 days late in payments and appeared incapable of paying its bills. The line of credit provided that it did not constitute a commitment to make future advances and that any future advances would be at bank's discretion. In bank's suit to recover under the line of credit, it was not error to refuse borrowers' motion to amend counterclaims to state a cause of action for breach of the implied covenant of good faith and fair dealing. The line of credit gave bank discretion to deny future loans. There was no evidence that the discretion was misused to deprive borrowers of the benefit of the line of credit. Borrowers, after discovery, failed to raise sufficient facts to withstand a motion for summary judgment on the issue. Richland Nat'l Bank & Trust v. Swenson, 249 M 410, 816 P2d 1045, 48 St. Rep. 730 (1991).

Nature of Covenant — Test for Breach: An implied covenant of good faith and fair dealing exists in every contractual relationship, and a breach of the covenant is a breach of the contract. The standard of compliance is honesty in fact and the observance of reasonable commercial standards of fair dealing in the trade. Each party to the contract has a justified expectation that the other will act in a reasonable manner in performing, or in efficiently breaching, the contract. When a party uses discretion conferred by the contract to act dishonestly or outside of accepted commercial practices to deprive the other party of the benefit of the contract, the contract is breached. Richland Nat'l Bank & Trust v. Swenson, 249 M 410, 816 P2d 1045, 48 St. Rep. 730 (1991), following Story v. Bozeman, 242 M 436, 791 P2d 767 (1990).

Bank's Forcing Ranch to Sell Cattle Not Contractual Breach of Implied Covenant: In its counterclaim, the defendant ranch alleged that the plaintiff bank had breached the implied covenant of good faith and fair dealing by forcing the ranch to sell all of its cattle to reduce the amount of its outstanding loan from the bank. The Supreme Court held that there was no breach of the covenant because the evidence indicated that the cattle were scattered in various locations without adequate feed for their survival and that selling them was the only solution in light of the facts. First Sec. Bank & Trust of Miles City v. VZ Ranch, 247 M 453, 807 P2d 1341, 48 St. Rep. 255 (1991). See also Winchell v. U.S. Dept. of Agriculture, 961 F2d 1442 (1992).

No Special Relationship When Contract Entered for Profit: In its counterclaim involving a tort action, the defendant alleged that the bank had breached the implied covenant of good faith and fair dealing. The Supreme Court held that no special relationship can exist between the parties when the motivation for entering into the contract is for profit. In the absence of a special relationship, there can be no breach of the implied covenant. First Sec. Bank & Trust of Miles City v. VZ Ranch, 247 M 453, 807 P2d 1341, 48 St. Rep. 255 (1991).

When Actionable Cause for Termination Arises: On June 16, 1987, Martin was told her position was to be terminated as of July 17, 1987. After receiving notice, Martin discovered the position had not been eliminated but was to be filled by the company's new president's personal secretary from his former job. Martin filed suit alleging wrongful discharge, breach of the implied covenant of good faith and fair dealing, and negligence. On July 1, 1987, the Wrongful Discharge From Employment Act became effective. The District Court held that the Act precluded Martin's claims for breach of the implied covenant and negligence because the claim had not fully accrued until the date of termination. On appeal, Martin conceded that the claim for negligence was properly dismissed in light of Heltborg v. Modern Mach., 244 M 24, 795 P2d 954 (1990), but disputed dismissal of the breach of covenant claim, contending that a cause of action begins at the time of breach, which in this case occurred upon receipt of the notice of termination, and that all decisions made leading to the discharge occurred prior to notification. The Supreme Court, citing Del. St. College v. Ricks, 449 US 250, 66 L Ed 2d 431, 101 S Ct 498 (1980), and Chardon v. Fernandez, 454 US 6, 70 L Ed 2d 6, 102 S Ct 28 (1981), agreed with Martin that the cause of action accrued upon notice of termination and held that it was the decision to terminate and the act thereupon that caused the end result. It was at that point that legal redress could first be sought. Martin v. Special Resource Management, Inc., 246 M 181, 803 P2d 1086, 47 St. Rep. 2319 (1990), followed in Walch v. Univ. of Mont., 260 M 496, 861 P2d 179, 50 St. Rep. 1186 (1993), distinguishing Allison v. Jumping Horse Ranch, Inc., 255 M 410, 843 P2d 753 (1992).

Fiduciary Duty Between Shareholders in Close Corporation When No Other Type of Relationship Exists: The fiduciary duty between stockholders of a close corporation is one of utmost good faith and loyalty. However, the controlling group should not be stymied by a minority stockholder's grievances if the controlling group can demonstrate a legitimate business purpose and the minority stockholder cannot demonstrate a less harmful alternative. If called on to settle a dispute between the stockholders, the court must weigh the legitimate business purpose, if any, against the practicability of a less harmful alternative. Daniels v. Thomas, Dean & Hoskins, Inc., 246 M 125, 804 P2d 359, 47 St. Rep. 2293 (1990), citing Donahue v. Rodd Electrotype Co. of New England, Inc., 328 NE 2d 505 (Mass. 1975), and Wilkes v. Springside Nursing Home, Inc., 353 NE 2d 657 (Mass. 1976), and distinguishing Skierka v. Skierka Bros., Inc., 192 M 505, 629 P2d 214 (1981), Deist v. Wachholz, 208 M 207, 678 P2d 188 (1984), and Dunfee v. Baskin-Robbins, 221 M 447, 720 P2d 1148 (1986).

In Warren v. Campbell Farming Corp., 2011 MT 324, 363 Mont. 190, 271 P.3d 36, the Montana Supreme Court, in answering a certified question from the Tenth Circuit Court of Appeals, revisited the Daniels test and concluded that the Daniels test does not apply to claims involving director conflict of interest transactions. However, the Daniels test does apply to minority shareholders' claims of breach of fiduciary duties against majority shareholders.

Tort of Bad Faith — Not Available for Most Contract Actions — Breach: In a contract action, the Supreme Court ruled that a breach of the implied covenant of good faith and fair dealing constituted a breach of the contract and that only contract damages would be available to the prevailing party. The court stated that tort-type damages would not be available for a breach of the covenant. The court also held that the tort of bad faith would apply only in exceptional circumstances to discourage oppression in contracts that necessarily give one party a superior position. Every contract, regardless of the type, contains an implied covenant of good faith and fair dealing. A breach of the covenant is a breach of the contract. Story v. Bozeman, 242 M

436, 791 P2d 767, 47 St. Rep. 850 (1990), followed in Mann Farms, Inc. v. Traders St. Bank of Poplar, 245 M 234, 801 P2d 73, 47 St. Rep. 2094 (1990) (replacing previous opinion, subsequently withdrawn, at 47 St. Rep. 1557 (1990)), Lachenmaier v. First Bank Sys., Inc., 246 M 26, 803 P2d 614, 47 St. Rep. 2244 (1990), Wise v. Sebena, 248 M 32, 808 P2d 494, 48 St. Rep. 309 (1991), Citizens First Nat'l Bank of Wolf Point v. Moe Motor Co., 248 M 495, 813 P2d 400, 48 St. Rep. 528 (1991), Keller v. Dooling, 248 M 535, 813 P2d 437, 48 St. Rep. 554 (1991), Haines Pipeline Constr., Inc. v. Mont Power Co., 251 M 422, 830 P2d 1230, 48 St. Rep. 1102 (1991), McNeil v. Currie, 253 M 9, 830 P2d 1241, 49 St. Rep. 312 (1992), and Kneeland v. Luzenac America, Inc., 1998 MT 136, 289 M 201, 961 P2d 725, 55 St. Rep. 541 (1998). See also Winchell v. U.S. Dept. of Agriculture, 961 F2d 1442 (1992).

All Bank Transactions Not Subject to Implied Covenant: The bank refused to release funds from escrow in the manner requested by the plaintiff. The plaintiff suffered monetary damages as a result of the bank's actions. The Supreme Court ruled that damages alone are not sufficient to prove the existence of the implied covenant of good faith and fair dealing and that the covenant does not arise in every transaction involving a bank. O'Bagy v. First Interstate Bank of Missoula, 241 M 44, 785 P2d 190, 47 St. Rep. 69 (1990).

Remand Upon Failure to Instruct on Justifiable Expectations of Parties in Employment Contract Relationship: The Supreme Court remanded after finding the trial court failed to tell the jury the nature and extent of the implied covenant of good faith and fair dealing. The instructions informed the jury that as a matter of law the employer owed the covenant to the employee but failed to mention that the covenant is measured in a particular contract by the justifiable expectations of the parties, as required under Nicholson v. United Pac. Ins. Co., 219 M 32, 710 P2d 1342, 42 St. Rep. 1822 (1985). Although not binding on the parties or the trial court on retrial, the Supreme Court set out suggested instructions explaining in detail application of the covenant. Hobbs v. Pac. Hide & Fur Depot, 236 M 503, 771 P2d 125, 46 St. Rep. 544 (1989).

Breach of Contract Required for Bad Faith Liability to Attach: When an underlying contract subsumes the entirety of the relationship between parties, Montana law requires an initial finding that one party breached the contract in order to have liability for bad faith and conduct attach. Mont. Bank of Circle v. Ralph Meyers & Son, Inc., 236 M 236, 769 P2d 1208, 46 St. Rep. 324 (1989), followed in Citizens First Nat'l Bank of Wolf Point v. Moe Motor Co., 248 M 495, 813 P2d 400, 48 St. Rep. 528 (1991). See also Mann Farms, Inc. v. Traders St. Bank of Poplar, 245 M 234, 801 P2d 73, 47 St. Rep. 2094 (1990), replacing previous opinion, subsequently withdrawn, at 47 St. Rep. 1557 (1990).

Failure to Renegotiate Defaulted Note — No Breach of Good Faith: The Supreme Court has never held that a Montana bank is under a duty to renegotiate a defaulted loan. Absent evidence that such a duty exists, a claim that a bank breached the covenant of good faith by failing to renegotiate a defaulted loan was properly dismissed. Mont. Bank of Circle v. Ralph Meyers & Son, Inc., 236 M 236, 769 P2d 1208, 46 St. Rep. 324 (1989), followed in Citizens First Nat'l Bank of Wolf Point v. Moe Motor Co., 248 M 495, 813 P2d 400, 48 St. Rep. 528 (1991)

Summary Judgment Proper — Surety Relationship: Plaintiff was held liable to bank as surety on a note. Summary judgment granted to the bank was proper as to plaintiff's counterclaim for the bank's breach of the implied covenant of good faith and fair dealing. Plaintiff's citation of Weinberg v. Farmers St. Bank of Worden, 231 M 10, 752 P2d 719, 45 St. Rep. 391 (1988), as authority that banks have a fiduciary duty toward their customers is misguided as to plaintiff. The only connection between plaintiff and the bank is the surety agreement, and Weinberg does not state that there is a fiduciary duty in such a relationship. Mont. Bank of Livingston v. Old Saloon, Inc., 235 M 244, 766 P2d 878, 45 St. Rep. 2354 (1988).

Payment Withheld in Anticipation of Breach: When employee sent letter to employer stating terms substantially different from original oral contract, employer withheld employee's pay. Court held that the employer's action was reasonable and in good faith and did not breach the contract. The employer had reasonable grounds to believe the employee would breach the contract and thus give the employer a claim for damages; therefore, the employer was entitled to withhold performance until he received assurance of the employee's intent to fulfill the contract. This is the rule stated in section 251 of the Restatement (Second) of Contracts (1979). Julian v. Mont. St. Univ., 229 M 362, 747 P2d 196, 44 St. Rep. 2046 (1987).

DECISIONS PRIOR TO 1987 ENACTMENT

No Bank Duty to Make Further Loans After Loan Repaid: Recovery for breach of a covenant of good faith and fair dealing requires an enforceable contract to which the covenant attaches. The nature and extent of the covenant is measured by the justifiable expectations of the parties.

When a bank contracted to loan an attorney money, when the bank loaned various amounts at various times, and when the whole amount owed was repaid, the bank had no obligation to enter into another contract to loan more money and the attorney's claimed "justifiable expectations" that the bank would continue to loan him money had no contract to which they could be attached. Absent an express or implied contract, there could be no covenant, no justifiable expectations of continued credit, and no breach of covenant. Cate v. First Bank (N.A.)-Billings, 262 M 429, 865 P2d 277, 50 St. Rep. 1624 (1993).

Procedurally Improper and Unsubstantiated Claim of Bank Alteration of Records: In an attorney's action against a bank for breach of a covenant of good faith and fair dealing, the attorney filed a motion for summary judgment in which he for the first time claimed that the bank had altered his banking records and that the alterations made it liable as a matter of law and precluded summary judgment for the bank. He presented no evidence of alteration, did not modify his complaint to add the alteration claim, attempted to have his expert on the alleged alteration added to the witness list a month after the deadline for presentation of expert witness lists, and submitted, on appeal, letters from his expert that were not part of the record below. He presented no legal authority under which the bank's alleged actions and manner of keeping his records were illegal. It was not error to deny his motion. Cate v. First Bank (N.A.)-Billings, 262 M 429, 865 P2d 277, 50 St. Rep. 1624 (1993).

Existence of Covenant of Good Faith and Fair Dealing Not Implied in Employment of Corporate Officer: Mannix argued that the board of directors had breached the covenant of good faith and fair dealing when they fired him. The Supreme Court held that the covenant was not implied in the employment relationship between Mannix and the corporation and that Mannix acknowledged that he was aware when hired that he served at the discretion of the board of directors. Mannix v. Butte Water Co., 249 M 372, 854 P2d 834, 50 St. Rep. 691 (1993).

No Showing of Breach of Good Faith Covenant: The Supreme Court, in a case involving a contract for the purchase of one bank by another bank, held that Kuhns had presented no evidence that the defendant had not made a good faith effort to obtain approval of the sale by the Federal Reserve Board. Kuhns v. Scott, 259 M 68, 853 P2d 1200, 50 St. Rep. 685 (1993).

Elements of "Special Relationship" Necessary to Support Tort Claim of Bad Faith: The essential elements of a special relationship necessary to support a tort claim of bad faith, as set out in Wallis v. Kroehler Mfg. Co., 207 Cal. Rep. 123 (1984), are: (1) the contract must be such that the parties are in inherently unequal bargaining positions; (2) the motivation for entering the contract must be a nonprofit motivation (i.e., to secure peace of mind, security, or future protection); (3) ordinary contract damages are not adequate because they do not require the party in the superior position to account for its actions and they do not make the inferior party whole; (4) one party is especially vulnerable because of the type of harm it may suffer and of necessity places trust in the other party to perform; and (5) the other party is aware of this vulnerability. If substantial evidence is not presented in support of each and all of the elements, the court shall direct that there is no special relationship. Simmons Oil Corp. v. Holly Corp., 258 M 79, 852 P2d 523, 50 St. Rep. 433 (1993). These elements were applied in Stephens v. Safeco Ins. Co. of America, 258 M 142, 852 P2d 565, 50 St. Rep. 467 (1993). See also Story v. Bozeman, 242 M 436, 791 P2d 767 (1990), and Warrington v. Great Falls Clinic, LLP, 2019 MT 111, 395 Mont. 432, 443 P.3d 369.

Good Faith Required in Exercise of General Right to Assign Debts Under Restructuring Agreement — Summary Judgment Inappropriate: The District Court relied on Carma Developers v. Marathon Dev. Calif., Inc., 826 P2d 710 (Calif. 1992), in granting summary judgment to defendants who contended that the implied covenant of good faith and fair dealing could not be used to override the specific provisions of a restructuring agreement allowing the assignment of plaintiff's debts. The Supreme Court distinguished Carma in holding that summary judgment was improper when a genuine issue of material fact existed as to whether the covenant was breached by defendant's discretionary use of the power of assignment to assign the notes to plaintiff's partner. Simmons Oil Corp. v. Holly Corp., 258 M 79, 852 P2d 523, 50 St. Rep. 433 (1993).

Seizure of Collateral by Bank Not Bad Faith: The plaintiffs sued the defendant bank for breach of the covenant of good faith and fair dealing. The Supreme Court held that the relationship between the parties was contractual and that the plaintiffs' assertion that they only signed blank documents rather than documents pledging collateral to secure bank loans was not supported by the evidence. The court ruled that under the law applicable at the time, the bank did not act in bad faith in seizing the collateral when the plaintiffs defaulted on their loans. Stott v. Fox, 246 M 301, 805 P2d 1305, 47 St. Rep. 2040 (1990).

No Question of Fiduciary Duty When Judgment Based Only on Good Faith and Fair Dealing: Appellant argued that District Court prejudiced its interests by improperly instructing the jury that, as franchisor, appellant owed a fiduciary duty to respondents as franchisees. The Supreme Court noted that a franchise relationship is inherently a business relationship rather than a fiduciary relationship. However, the questioned jury instruction was found to be primarily definitional; therefore, the Supreme Court found it unnecessary to rule on whether the special facts of the case gave rise to a fiduciary duty since the District Court only held appellant to the responsibility of acting in good faith and fair dealing with respondents. Dunfee v. Baskin-Robbins, Inc., 221 M 447, 720 P2d 1148, 43 St. Rep. 964 (1986).

Bad Faith Claim Suspended Until Liability Determined: Plaintiff sued defendant, insurer of another driver, following a three-car accident. Defendant denied any liability on the part of its insured and refused to pay any part of plaintiff's claim. Plaintiff then filed a bad faith action against defendant. The District Court granted summary judgment. The Supreme Court reversed and remanded the case. The court overruled Klaudt v. Flink, 202 M 247, 658 P2d 1065, 40 St. Rep. 64 (1983), to the extent that Klaudt allowed a bad faith claim to be pursued although liability for an accident had not been determined. The court noted several problems in this procedure and held that all proceedings in a bad faith case alleging violations of the insurance laws which require a showing that liability be reasonably clear are suspended until the liability issues of the underlying case are determined by judgment or settlement. The bad faith case may be filed to toll the Statute of Limitations, but no discovery may be engaged. A favorable District Court judgment for the plaintiff is sufficient to trigger discovery in the bad faith case. Fode v. Farmers Ins. Exch., 221 M 282, 719 P2d 414, 43 St. Rep. 814 (1986), distinguished in Peris v. Safeco Ins. Co., 276 M 486, 916 P2d 780, 53 St. Rep. 481 (1996).

Breach of Covenant of Good Faith in Conducting Insurance Claim: In a foreclosure action, the insured, Britton, cross-claimed against Farmers Insurance Group (FIG) for the full amount of coverage provided by FIG's policy and for further compensatory and punitive damages by reason of "bad faith". FIG responded to the foreclosure action by setting up as a cross-claim against Britton its right under its partial assignment of mortgage and requesting foreclosure against Britton. FIG further defended against Britton's cross-claim by alleging that Britton had intentionally set the fire, had been guilty of fraud with respect to his interest in the property, and had not submitted a proper proof of loss. On appeal, the Supreme Court found that prior to filing its answer to Britton's cross-claim, FIG neither rejected Britton's proof of loss nor informed him in writing or otherwise of their contention of arson. Also, FIG's evidence regarding Britton's involvement in setting the fire was circumstantial, and there was no evidence of potential financial gain for Britton from the policy proceeds. The jury decision that FIG breached the implied covenant of good faith and fair dealing in conducting the claim was upheld. Britton v. Farmers Ins. Group, 221 M 67, 721 P2d 303, 43 St. Rep. 641 (1986).

Inadequate Jury Instruction — Implied Covenant of Good Faith: The District Court instructed the jury on the implied covenant of good faith and fair dealing, stating that good faith means honesty in fact in the conduct or transaction concerned and then equating the implied covenant to an obligation imposed by law on defendants to do nothing to deprive plaintiffs of the benefits of their commercial transaction. On appeal, defendants argued that the implied covenant had no application in a case involving an arms-length contract. The Supreme Court, relying on its decision in Nicholson v. United Pac. Ins. Co., 219 M 32, 710 P2d 1342, 42 St. Rep. 1822 (1985), held that a breach of the implied covenant which results in damages can give rise to an action in tort, but that in order to recover additional punitive damages, plaintiffs must prove that defendants' actions in breaching the implied covenant met the requirements of 27-1-221. The tort of breach of the implied covenant of good faith and fair dealing requires more than a lack of honesty in fact. The instruction given to the jury on this issue inadequately defined the tort. McGregor v. Cushman/Mommer, 220 M 98, 714 P2d 536, 43 St. Rep. 206 (1986), followed in Noonan v. First Bank Butte, 227 M 329, 740 P2d 631, 44 St. Rep. 1124 (1987). See also Dunfee v. Baskin-Robbins, Inc., 221 M 447, 720 P2d 1148, 43 St. Rep. 964 (1986).

Contract Dispute — Damages — Harmless Error: Plaintiffs, sellers of a motel, sued for repossession of the motel and the defendants counterclaimed for actual and punitive damages. The District Court jury awarded judgment in favor of the defendants. The plaintiffs appealed, claiming the District Court erred by instructing the jury that an oral waiver could alter a written contract and by submitting to the jury an issue of bad faith between the parties. The Supreme Court held that the defendants' testimony as to the plaintiffs' waiver was sufficient to uphold the jury decision and that the failure of the District Court to distinguish between damages arising from a breach of contract provision and damages for the tort of bad faith is in this case harmless in view of the jury verdict awarding only compensatory damages. Thiel v. Johnson, 219 M 271, 711 P2d 829, 42 St. Rep. 2010 (1985).

Breach of Good Faith Obligation — Punitive Damages: A breach of the obligation of good faith imposed by this section, in and of itself, is not sufficient to support an award of punitive damages. There must be some oppressive, malicious, or fraudulent conduct, beyond a breach of the statutory good faith obligation, to support an award of punitive damages. This statement of dictum was made by the court in holding that the plaintiff bank properly foreclosed on a mortgage on real property pledged as collateral for business loans after the bank had refused to extend the note unless the principal balance was reduced substantially. Cent. Bank of Mont. v. Eystad, 219 M 69, 710 P2d 710, 42 St. Rep. 1850 (1985).

Covenant of Good Faith and Fair Dealing — General Test for Contracts Covered: Plaintiff, who owned a building and two construction companies, and defendant insurance company signed a lease for office space in a building. Plaintiff was to renovate the space, and the two were to confer on and mutually approve the renovation plans. Disagreements arose on the plans. Plaintiff claimed he had difficulties contacting defendant. Defendant rescinded the lease on the ground that it had continually invested more time and money than plaintiff and that from a business standpoint the lease was no longer feasible. After failing in an attempt to contact defendant's president, plaintiff sent a notice of default and sued. The court affirmed an award of punitive damages to plaintiff. The court declined to extend the tort of breach of an implied covenant of good faith and fair dealing to all contracts of any type, including arms-length and substantially equal bargaining power contracts, but stated that: (1) whether breach of a contract constitutes the tort depends on whether there has been some impermissible activity; (2) the nature and extent of an implied covenant of good faith and fair dealing is measured in a particular contract by the justifiable expectations of the parties and, whether performing or breaching, each party has a justifiable expectation that the other will act as a reasonable person; (3) a party who acts arbitrarily, capriciously, or unreasonably exceeds the justifiable expectations of the other party, and the other party should be compensated for damages resulting from the culpable conduct; and (4) for punitive damages to be awarded for breach of an implied covenant of good faith and fair dealing in a contract breach situation, the breach must amount to oppression, fraud, or malice. Nicholson v. United Pac. Ins. Co., 219 M 32, 710 P2d 1342, 42 St. Rep. 1822 (1985), followed in Randolf V. Peterson, Inc. v. J.R. Simplot Co., 239 M 1, 778 P2d 879, 46 St. Rep. 1463 (1989), Tresch v. Norwest Bank of Lewistown, 238 M 511, 778 P2d 874, 46 St. Rep. 1459 (1989), and in McJunkin v. Kaufman, 229 M 432, 748 P2d 910, 44 St. Rep. 2111 (1987). See also Lachenmaier v. First Bank Sys., Inc., 246 M 26, 803 P2d 614, 47 St. Rep. 2244 (1990).

Commission of Bad Faith Tort Against Depositor by Bank: The District Court did not err in instructing the jury to consider recovery by bank depositor against the bank under bad faith tort principles and to accordingly consider punitive damages. The depositor and his nephew opened a checking account with a card requiring the signatures of both on checks. They then formed a partnership. The nephew induced the bank to change the card so that he could issue checks without the depositor's signature. The bank did not notify the depositor of the change or obtain his authorization for it. The bank told depositor his signature was not needed but did not tell him about the new card, and depositor disagreed. Later the bank told him it would not change its policy of honoring checks signed only by the nephew. When depositor's attorney told bank not to do so, the bank stated the card required only one signature and the bank would not change the card unless both the nephew and the depositor requested it. The bank then told depositor the card was lost but later that day produced both cards. Depositor sued, and the bank subsequently took various negative and detrimental actions against his credit status, refused loans of a type formerly granted, canceled his ready reserve account, and refused to pay several items presented before he was notified that the account had been canceled. Tribby v. NW. Bank of Great Falls, 217 M 196, 704 P2d 409, 42 St. Rep. 1133 (1985). See also Flanigan v. Prudential Fed. S&L Ass'n, 221 M 419, 720 P2d 257, 43 St. Rep. 941 (1986).

Punitive Damages Proper in Action for Breach of Implied Covenant of Good Faith and Fair Dealing and for Negligent Investigation: The plaintiff was properly granted punitive damages for the hospital's breach of implied covenant of good faith and fair dealing and for negligence in investigating the charges for which plaintiff was dismissed from employment as a probationary employee. Crenshaw v. Bozeman Deaconess Hosp., 213 M 488, 693 P2d 487, 41 St. Rep. 2251 (1984).

Lender's Failure to Honor Renegotiated Loan Payments: Bank's employee, Johnson, told defendants that their note with the bank would be renegotiated to allow further time for payment. Another employee then refused to renegotiate, and he offset defendants' checking account balance against the note without telling defendants, after defendants told him they had relied on Johnson and would not be able to pay on the note's due date. Several of defendants' checks were then dishonored due to insufficient funds. If a duty to exercise good faith is imposed by law rather than by a contract, breach of the duty is tortious and punitive damages are thus recoverable if the conduct is sufficiently culpable. Here, punitive damages could have been granted on the basis of malice, fraud, oppression, or all three, and a new trial was granted because the judge refused to submit the punitive damages issue to the jury. First Nat'l Bank of Libby v. Twombly, 213 M 66, 689 P2d 1226, 41 St. Rep. 1948 (1984). See also Flanigan v. Prudential Fed. S&L Ass'n, 221 M 419, 720 P2d 257, 43 St. Rep. 941 (1986), and Dunfee v. Baskin-Robbins, Inc., 221 M 447, 720 P2d 1148, 43 St. Rep. 964 (1986).

Tort of Breach of Duty to Deal Fairly and in Good Faith in Employment Relationship — Punitive Damages Recoverable: Section 27-1-221 only exempts breach of contract actions from its provisions. Breach of the duty owed to deal fairly and in good faith in the employment relationship is a tort for which punitive damages may be recovered if defendant's conduct is sufficiently culpable. Gates v. Life of Montana, 205 M 304, 668 P2d 213, 40 St. Rep. 1287 (1983).

Law Review Articles

Commercial Bad Faith: Tort Recovery for Breach of Implied Covenant in Ordinary Commercial Contracts, Tremper, 48 Mont. L. Rev. 349 (1987).

Survey: Good Faith and Fair Dealing: An Analysis of Recent Cases, Hubble, 48 Mont. L. Rev. 193, 202 through 211 (1987).

The Continuing Development of the Tort of Bad Faith in Montana, Graham & Luck, 45 Mont. L. Rev. 43 (1984).

Part 3
Joint Obligations

Part Case Notes

Reversal of Mislabeled Award — Validity Not Raised in Pleadings: The Supreme Court reversed the District Court award of $3,768.66 in damages related to freight adjustment, which the District Court had mistakenly labeled as invalid trailer charges. The award was improper because under the contract, plaintiff was responsible for the adjustments and because the validity of the charges was not properly raised in the initial or amended pleadings. Koontz v. Sky Country, Inc., 244 M 192, 795 P2d 980, 47 St. Rep. 1490 (1990).

28-1-301. Types of obligations involving several persons.

Compiler's Comments

1997 Amendment: Chapter 429 in exception clause inserted "and 27-1-705". Amendment effective on occurrence of contingency.

Preamble: The preamble attached to Ch. 429, L. 1997, provided: "WHEREAS, efforts of the Legislature to amend the comparative negligence statute, which is premised on a modified joint and several liability scheme, have repeatedly been struck down by the Montana Supreme Court; and

WHEREAS, the Montana Supreme Court rulings prohibiting the consideration of fault attributable to nonparties impair the effectiveness of the current modified joint and several liability system in Montana; and

WHEREAS, the Legislature intends that the policy of the state should be a system of comparative fault in which persons are held responsible only to the extent to which they cause or contribute to the harm; and

WHEREAS, the current system of joint and several liability, which apportions all liability only among parties to the action, fails to apportion liability among all tortfeasors according to their equitable share of fault; and

WHEREAS, the Legislature recognizes that public policy favors fair settlements that accurately reflect the liability of settled or released parties; and

WHEREAS, the Legislature is concerned with the present inequitable results of solvent defendants having to pay for the liability of insolvent, immune, or settled parties; and

WHEREAS, the present system of joint and several liability for all tort actions does not reflect the state's policy of liability in proportion to fault; and

WHEREAS, the Legislature recognizes that joint and several liability should be retained for certain situations; and

WHEREAS, at least ten other states have abrogated the doctrine of joint and several liability, except for specific situations; and

WHEREAS, the Legislature has the power to alter tort causes of action to promote legitimate state interests.

THEREFORE, the Legislature declares that the doctrine of joint and several liability is abolished, except for specific causes of action, and is replaced with a comparative fault system utilizing the principles of several liability."

Severability: Section 9, Ch. 429, L. 1997, was a severability clause.

1987 Amendment: At beginning inserted exception clause.

Case Notes

Insurers of Uninsured Motorist Not Treated as Joint Tortfeasors for Purposes of Liability: When accident and injury are caused by uninsured motorist, insurance companies providing uninsured motorist coverage to parties involved cannot be held jointly and severally liable because an insurer's relationship to the uninsured motorist is based on contract, not tort. Guiberson v. Hartford Cas. Ins. Co., 217 M 279, 704 P2d 68, 42 St. Rep. 1196 (1985).

Enforcement of Parties' Rights: Although under 28-1-302 the common-law distinctions between joint, joint and several, and several liabilities are abolished, under this section the rights which may be enforced by several persons are left undisturbed; they may be enforced jointly, severally, or jointly and severally, as the facts may warrant. Hand v. Heslet, 81 M 68, 261 P 609 (1927). See also Morgen & Oswood Constr. Co., Inc. v. USF&G Co., 167 M 64, 535 P2d 170 (1975).

28-1-302. Joint obligations and covenants to be taken as joint and several.

Compiler's Comments

1987 Amendment: At beginning inserted exception clause.

Case Notes

On Remand for Calculation of Damages Caused by Breach: The defendants were employed by the plaintiff's accounting firm under an employment agreement containing a covenant restricting competition. When the defendants established a competing accounting firm and solicited the plaintiff's clients, the plaintiff filed a complaint against the defendants to declare the covenant enforceable and to recover damages. After the Supreme Court remanded the issue of damages caused by the breach back to the District Court in Junkermier v. Alborn, 2016 MT 218, 384 Mont. 464, 380 P.3d 747, the District Court determined that the covenant was reasonable, that the defendants were jointly and severally liable for damages arising out of the covenant's breach pursuant to the contractual calculation of 1 year's billings to the plaintiff's clients, and that the plaintiff was entitled to prejudgment interest. The Supreme Court affirmed on all issues with the exception of the date interest began accruing based on the language in the covenant, which was described as de minimus. Junkermier v. Alborn, 2020 MT 179, 400 Mont. 408, 469 P.3d 111.

Materialman Not Bound by Owners' Agreement to Share Costs: In an action to foreclose a mechanics' lien (now construction lien), an agreement between the lessors and lessees of the liened property on sharing improvement costs is a matter to be settled only between the lessors and lessees. The contractor was not a party to that contract and is not bound by its terms. Price Bldg. Serv., Inc. v. Holms, 214 M 456, 693 P2d 553, 42 St. Rep. 84 (1985).

Successive Judgments Against Co-obligors: Entry of default judgment against codefendant does not bar entry of subsequent judgment against co-obligor on same obligation where obligation was joint and several, thereby permitting successive judgments against each in amount of total obligation of both. Common-law rule that judgment on joint obligation against one of two joint obligors forecloses later judgment against other was abrogated by statute. White v. Nollmeyer, 151 M 387, 443 P2d 873 (1968).

Enforcement of Parties' Rights: Although under this section the common-law distinctions between joint, joint and several, and several liabilities are abolished, under 28-1-301 the rights which may be enforced by several persons are left undisturbed; they may be enforced jointly, severally, or jointly and severally, as the facts may warrant. Hand v. Heslet, 81 M 68, 261 P 609 (1927).

28-1-303. Right to contribution from joint debtors.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

1987 Amendment: At beginning inserted exception clause.

Case Notes

Guarantor Owes Pro Rata Share: Appellant and four other shareholders in company executed continuing guaranties for promissory notes on behalf of their shared business. Appellant subsequently signed away his share in company and left the business. Although the court considered appellant's equitable defense that he was not liable for his pro rata share of the notes because the other four guarantors personally profited from the sale of the business after appellant departed, he remains liable for his pro rata share. He signed the guaranty knowing the lender could sue him directly on the notes. All five shareholders shared equal liability on the promissory notes, and appellant is required to contribute his one-fifth pro rata share. Citizens St. Bank v. Bossard, 226 M 75, 733 P2d 1296, 44 St. Rep. 468 (1987).

Accommodation Endorsers — Parol Evidence: While it is general rule that where a number of persons successively sign a note, they are prima facie liable in the order in which their names appear even though they are in fact accommodation endorsers, their intention that there should be a joint rather than a successive liability may be inferred from the circumstances, and parol evidence is admissible to show that there was an agreement to that effect. Anderson v. Border, 75 M 516, 244 P 494 (1926).

Relation of Parties: Where the relation of parties is merely that of joint or joint and several obligors, an action at law can be maintained by one party against any one of the others, upon the theory that each of them upon assuming the relation impliedly agreed to contribute to every other such sum as the other should be compelled to pay in his behalf. Croft v. Bain, 49 M 484, 143 P 960 (1914).

Part 4
Conditional Obligations

28-1-401. What obligations are conditional.

Case Notes

Form of Bid Deposit Accepted by Seller's Agent — No Failure to Satisfy Condition Precedent — Specific Performance to Enforce Transfer of Real Property — Summary Judgment Proper: The defendants auctioned off two parcels of land. To qualify to bid on the parcels, a bidder had to make a bid deposit in certified funds or other acceptable funds. The plaintiffs each made a bid deposit accepted by the seller's agent, were the highest bidders on the respective parcels, and afterward executed a buy-sell agreement. However, the defendant sellers later notified the plaintiffs that they would not convey the property to them because the plaintiffs had failed to satisfy the condition precedent to entering into the buy-sell agreement since their bid deposits were not certified funds. The plaintiffs then filed suit seeking specific performance of the agreement. The District Court granted the plaintiffs' summary judgment. On appeal, the Supreme Court agreed that the form of the bid deposit did not effect a failure of a condition precedent to formation of the contract and affirmed the grant of summary judgment. Davidson v. Barstad, 2019 MT 48, 395 Mont. 1, 435 P.3d 640.

28-1-403. Condition precedent defined.

Case Notes

Condition Precedent — Sick Leave Payout Upon 25 Years of Service — No Compensation Prior to 25 Years of Service: A hospital discontinued a policy whereby it paid employees for their sick leave after 25 years of service. Employees with less than 25 years of service sued the hospital alleging violations of Title 39, ch. 3. The District Court granted the hospital summary judgment, concluding that the policy did not constitute deferred compensation or wages under Montana law. The plaintiffs appealed. The Supreme Court affirmed, agreeing that the completion of 25 years of service was a condition precedent and therefore the benefit did not accrue until the employee had actually completed 25 years of service. Chipman v. NW. Healthcare Corp., 2014 MT 15, 373 Mont. 360, 317 P.3d 182.

Settlement Agreement — Clearing of Title Not Condition Precedent Under Plain Meaning of Language: The parties entered into a settlement agreement to resolve a dispute over two oil wells. The agreement provided that Summer Night Oil would make payments to Miocene and Miocene would clear its liens against Summer Night's property. Summer Night filed a motion to compel Miocene to clear the liens even though it had not made any payments to Miocene, claiming that the payments to Miocene were conditioned upon Miocene first clearing the liens. Miocene argued that clearing the title was not a condition precedent to Summer Night's payment under the settlement agreement. The District Court agreed with Miocene, as did the Supreme Court on appeal, that under the plain language of the settlement agreement, Summer Night's payments were not conditioned upon Miocene first clearing the liens. Summer Night Oil Co., LLC v. Munoz, 2011 MT 202, 361 Mont. 424, 259 P.3d 778.

Negligence During House Moving — Breach of House Moving Agreement — Remand for Determination of Causation and Damages: Kelly entered an agreement with Hall to move four of Kelly's housing units. Hall agreed to obtain cargo insurance on each unit but did not do so. During the move, two units were damaged, and Kelly filed a claim against Hall's insurer for remuneration. The claim was denied, and the insurer sought a declaratory judgment against both Hall and Kelly. Kelly filed negligence and breach of contract claims against Hall, and Hall counterclaimed for breach of contract against Kelly. The District Court concluded that Kelly failed to establish negligence, that both parties breached the contract, and that neither party could recover against the other. On appeal, the Supreme Court affirmed the finding that Hall breached the contract by failing to obtain cargo insurance and that, based on the presumption against conditions precedent and inconclusive evidence, Kelly also breached the contract and thus could not recover breach of contract damages. However, there was no evidence to rebut Kelly's negligence claim, nor did the District Court address the damages that Hall conceded occurred during the move. Because it was error to find that Kelly failed to establish negligence, the case was remanded for trial on causation and damages. Scottsdale Ins. Co. v. Hall, 2003 MT 188, 316 M 460, 73 P3d 819 (2003).

Five Agreements Constituting Integrated Sales Agreement With Condition Precedent — Overriding Previous Partnership Agreements and Providing for Attorney Fees: Daines argued that of the five agreements executed by the parties, the option agreement should have been read separately and interpreted as an option to buy conferring a privilege but not imposing an obligation and that on that basis, he could not be liable for not completing a purchase agreement. The Supreme Court held that the lower court had properly looked at the five agreements as a whole in interpreting the parties' intent and had correctly concluded that the agreements constituted an integrated sales agreement subject to conditions precedent. The Supreme Court further held that since the five agreements constituted a sales agreement, they superseded the previous partnership agreements. The respondents were not liable for capital contributions as partners, and the default provision in the option agreement providing for attorney fees did apply to the agreement created by all five of the documents executed by the parties. Daines v. Knight, 269 M 320, 888 P2d 904, 52 St. Rep. 8 (1995).

Completion of Survey Not Condition Precedent: Buyer breached buy-sell agreement, claiming he is entitled to rescission because of sellers' refusal to permit a survey of the real property prior to closing of the sale. The court properly held that there is no language in the contract indicating completion of a survey to be a condition precedent to closing. Because the sellers had performed all material conditions precedent, they are entitled to specific performance. Hillstrom v. O'Neil, 226 M 452, 736 P2d 126, 44 St. Rep. 795 (1987).

Default Excused by Failure to Convey Good Title: Defendants were successors in interest by assignment of contract for deed granted by plaintiff to defendants' assignor. The question addressed by the court was whether plaintiff's failure to convey good title excused defendants' default in not tendering a balloon payment, thereby entitling defendants to keep proceeds of defendants' fire insurance policy when the residence was destroyed by fire. The court held that plaintiff's duty to convey title free and clear of a Federal Land Bank mortgage constituted a condition precedent to defendants' balloon payment obligation. It also constituted a concurrent condition unfulfilled by plaintiff. Additionally, under the doctrine of equitable conversion, plaintiff would bear the risk of loss since she could not convey good title. Sharbono v. Darden, 220 M 320, 715 P2d 433, 43 St. Rep. 400 (1986), followed in Stark v. Borner, 226 M 356, 735 P2d 314, 44 St. Rep. 717 (1987) (affirmed in Stark v. Borner, 234 M 254, 762 P2d 857, 45 St. Rep. 1885 (1988)).

Real Estate Sale Conditioned on Approval of Shareholders — No Commission Due: District Court correctly reasoned that buy-sell agreement was a conditional contract containing the condition precedent of full shareholder approval of seller corporation. The condition precedent was never performed, and therefore the payment of broker's commission never became enforceable on the uncompleted sale. ERA Real Estate Home & Ranch Properties v. Big Horn Game Ranch, Inc., 213 M 47, 692 P2d 1218, 41 St. Rep. 1937 (1984).

Sufficiency of Default Notice — Mandatory Finding: Michunovich purchased a tract of land under contract for deed from the Brangers. Michunovich entered a contract for deed to sell a portion of that tract to Owen. Owen fulfilled his part of the contract. Michunovich defaulted on the Branger contract. Brangers filed a breach of contract suit against Michunovich. Michunovich served Owen a notice of termination since he was unable to secure a deed release from Brangers. Michunovich did not refund Owen's downpayment as required by the contract. Owen refused to vacate the property. Michunovich assigned all his interest in the Branger contract to Stevenson with the Brangers' consent. Since Stevenson was able to bring the Branger contract current, the

Brangers stipulated to the dismissal of their suit against Michunovich. Owen filed a purchaser's lien on the property under his contract from Michunovich. Stevenson then filed a quiet title action. The trial court found for Stevenson, finding that the notice from Michunovich to Owen terminated that contract so that Owen had no interest in the land. The Supreme Court remanded because according to the terms of the contract the refund of Owen's downpayment was a condition precedent to the contract being declared void. The trial court was instructed to determine whether Stevenson's default notice terminated the Owen contract and to resolve issues regarding rental value and improvements. Stevenson v. Owen, 212 M 287, 687 P2d 1010, 41 St. Rep. 1743 (1984).

Condition of Payment in Commission Contract — "Unless" Condition Held Valid: Where the plaintiff and defendant entered into a commission contract providing that the defendant would not pay any commission to the plaintiff "unless and until" the purchaser of the defendant's property fulfilled its duties under a contract for deed, the District Court did not err in holding that this language created a valid condition precedent for payment of the commission. By using the term "unless", the defendant reserved the right to withhold payment of the commission, and the time contingency, created by the use of the term "until", does not come into play until the condition precedent occurs. Martin v. Community Gas & Oil Co., 205 M 394, 668 P2d 243, 40 St. Rep. 1385 (1983).

Condition as Triggering Contract: A condition precedent is to be performed before the agreement becomes effective. It calls for the happening of an event upon the performance of an act after the parties have agreed to terms. It causes the contract to be binding on the parties. Westmont Tractor Co. v. Viking Exploration, Inc., 543 F. Supp. 1314, 39 St. Rep. 1398 (D.C. Mont. 1982).

Documents Incorporated as Contract — Waiver of Condition Precedent: Plaintiff negotiated to sell two-wheel loaders to defendant. The terms of the sale were contained on the purchase order and included a 30-day warranty. Later, a lease agreement covering the same equipment was executed with plaintiff as lessor and defendant as lessee. One of the loaders broke down and required repair. Plaintiff contended the date of the warranty was from the date the purchase order was executed. Defendant refused to pay for the repair, contending the warranty began on the date of the lease agreement. Plaintiff claimed breach and took possession of the loaders. By its own admission, plaintiff conceded that the initial agreement was transformed into the lease agreement. This in effect was a modification of the contract. The terms contained in the purchase order were incorporated into and became part of the lease agreement. The two writings together constituted the final written expression of the agreement. The terms were unambiguous and could not be contradicted by evidence of any prior agreement. Plaintiff was responsible for repair under the warranty provision. Defendant contended refusal to honor this warranty constituted breach of the agreement, while plaintiff contended that a provision for advance payment, not rendered by defendant, was a condition precedent to the formation of the lease contract. The only logical interpretation of the events which transpired was that plaintiff waived the advance payment by delivering the loaders prior to receipt of the payment. Plaintiff could not rely on failure to receive the advance payment in claiming breach of contract under 30-2-706. Defendant was entitled to summary judgment. Westmont Tractor Co. v. Viking Exploration, Inc., 543 F. Supp. 1314, 39 St. Rep. 1398 (D.C. Mont. 1982).

Waiver:

A buy-sell agreement contained a clause making the agreement contingent upon the buyer's obtaining a contract for deed for that part of the seller's interest subject to a previous contract for deed. The buyer proceeded to obtain such a contract for deed but upon different terms from those specified in the buy-sell agreement. Assuming that contingency clause created a condition precedent, the buyer's acceptance of different terms resulted in a waiver of any right to rely on the contingency clause. Wendy's of Mont. v. Larsen, 196 M 525, 640 P2d 464, 39 St. Rep. 299 (1982).

A clause in a water well drilling contract providing that the contract was not valid unless approved by the FHA made approval a condition precedent. However, the condition was waived by drilling and payment. Hein v. Fox, 126 M 514, 254 P2d 1076 (1953).

Buy-Sell Agreement: A buy-sell agreement contained a clause stating that the agreement was contingent upon the buyer's obtaining a contract for deed for that part of the seller's interest subject to a previous contract for deed. This clause may have been a necessary prerequisite to closing the transaction but was not a condition precedent whose lack of performance required the return of earnest money. Wendy's of Mont. v. Larsen, 196 M 525, 640 P2d 464, 39 St. Rep. 299 (1982).

Specified Time of Performance — Nonperformance of Condition Precedent: Contract farmer and landowner orally agreed that farmer would seed landowner's land between August 25 and September 20, with the condition that landowner would help farmer with the downpayment on drills needed for seeding. The help with the downpayment was a condition precedent that had to be performed by landowner before farmer was bound to the time frame in the contract. When landowner did not help with the downpayment, farmer was relieved of his obligation to meet the contract performance dates and the contract was to be performed within a reasonable time. Weyler v. Kaufman, 196 M 132, 638 P2d 393, 38 St. Rep. 2197 (1981).

Condition Precedent — Fulfillment Required: Before any party to an obligation can require another party to perform any act under it, he must fulfill all conditions precedent thereto imposed upon himself and must be able and offer to fulfill all conditions concurrent so imposed upon him of the like fulfillment by the other party except as provided by 28-1-407. Management, Inc. v. Mastersons, Inc., 189 M 435, 616 P2d 356, 37 St. Rep. 1601 (1980).

Offer Subject to Financing — Condition Precedent: The District Court properly found that the failure to obtain the necessary financing for the purchase from Empire Federal Savings and Loan in Livingston rendered the contract a nullity. The provision is specific that the offer is subject to such financing and, as such, a condition precedent. Under the circumstances, the efforts to obtain financing were reasonable. Management, Inc. v. Mastersons, Inc., 189 M 435, 616 P2d 356, 37 St. Rep. 1601 (1980).

Franchise Agreement: The court decided that duties of a franchisor by necessary implication were conditions precedent if construing them as covenants or concurrent duties would leave a franchisee without an adequate remedy for a breach of those obligations by franchisor. United Campgrounds, U.S.A. v. Stevenson, 175 M 17, 571 P2d 1161 (1977).

Lease Agreement: Lease terminable by either party upon 10 days' notice does not impose a condition precedent, performance of which must be alleged in plaintiff's complaint, but a condition subsequent which terminates the obligations of the parties to the lease. McEwen v. Big Sky of Mont., Inc., 169 M 141, 545 P2d 665 (1976).

Condition Precedent to Be Alleged and Proved:

In an action for an accounting based on a lease and management agreement by which defendant turned over his sheep ranch, farm machinery, and sheep to plaintiffs, who were required to build fences, plant hay and grain crops, care for the sheep, and perform other similar duties before they would become entitled to their share of the revenue from the sale of lambs and wool, the requirements were conditions precedent, and to state a cause of action on a contract of this nature, plaintiffs were required to allege performance under this contract or set forth facts excusing failure to perform. First Nat'l Bank of White Sulphur Springs v. Stoyanoff, 137 M 20, 349 P2d 1016 (1960).

Where the right of recovery is dependent upon happening of a condition precedent or of a future event, the happening of the condition or contingency must be alleged and proved; otherwise, the conditions agreed to between the parties would be nullified, a new contract would be made for them by the court, and the defendant's obligation and plaintiff's right would have accrued without reference to the express terms of the agreement. Binzel v. Viehmann, 111 M 6, 106 P2d 187 (1940).

Where right of recovery is dependent upon happening of the condition precedent, the happening of the condition must be alleged. Broat Lumber Co. v. Van Houten, 66 M 478, 213 P 1116 (1923).

Abandonment of Contract: Where written contract was clear and explicit and neither party performed his part of the contract but acted contrary to terms of contract pursuant to a subsequent oral agreement, there was an abandonment of the original contract. Eggers v. Gen. Refrigerating Co., 123 M 205, 210 P2d 636 (1949).

Condition Performed Before Agreement Becomes Effective: A "condition precedent" is one that is to be performed before the agreement becomes effective, and which calls for the happening of some event or the performance of an act after the terms thereof have been agreed upon, before the contract shall be binding on the parties. Atlantic-Pacific Oil Co. of Mont. v. Gas Dev. Co., 105 M 1, 69 P2d 750 (1937).

Performance Precedent to Payment: Under a building contract providing that final payment should be made only upon the production of satisfactory proof that there were no claims or liens against the building, the performance of the condition is precedent to the right of payment. Franklin v. Schultz, 23 M 165, 57 P 1037 (1899).

28-1-404. Condition concurrent defined.

Case Notes

Agreement to Sign Land Development Plan After Sale of Land Not Mutually Dependent Concurrent Obligation With Agreement for Sale of Land: Paragraph 4 of a buy/sell agreement provided that defendant would buy land from plaintiffs. Paragraph 5 provided that "[w]ithin 30 days of the closing of this sale", plaintiffs and defendant would enter into an agreement to develop the land. The two paragraphs were not mutually dependent concurrent obligations. Paragraph 4 had to be complied with before paragraph 5 had to be complied with, paragraph 5 was dependent upon the performance of paragraph 4, and paragraph 5 was void if paragraph 4 was not complied with. Defendant failed to make the downpayment and to sign the contract for deed required by paragraph 4, which were material breaches permitting plaintiffs to suspend performance under paragraph 5. The lower court erred by ruling that the parties mutually breached the two paragraphs when plaintiffs refused to perform under paragraph 5 because defendant had not yet performed under paragraph 4. King Resources, Inc. v. Oliver, 2002 MT 301, 313 M 17, 59 P3d 1172 (2002), followed, with regard to performance under a construction contract, in James Talcott Constr., Inc. v. P&D Land Enterprises, 2006 MT 188, 333 M 107, 141 P3d 1200 (2006).

Default Excused by Failure to Convey Good Title: Defendants were successors in interest by assignment of contract for deed granted by plaintiff to defendants' assignor. The question addressed by the court was whether plaintiff's failure to convey good title excused defendants' default in not tendering a balloon payment, thereby entitling defendants to keep proceeds of defendants' fire insurance policy when the residence was destroyed by fire. The court held that plaintiff's duty to convey title free and clear of a Federal Land Bank mortgage constituted a condition precedent to defendants' balloon payment obligation. It also constituted a concurrent condition unfulfilled by plaintiff. Additionally, under the doctrine of equitable conversion, plaintiff would bear the risk of loss since she could not convey good title. Sharbono v. Darden, 220 M 320, 715 P2d 433, 43 St. Rep. 400 (1986), followed in Stark v. Borner, 226 M 356, 735 P2d 314, 44 St. Rep. 717 (1987) (affirmed in Stark v. Borner, 234 M 254, 762 P2d 857, 45 St. Rep. 1885 (1988)).

Delivery and Payment for Chattels: Where delivery of chattels and payment for them were to be concurrent, plaintiff in his action for breach of contract was required to show an offer and ability to pay for and receive them at the place of delivery before he could put defendant in default. Weatherman v. Reid, 62 M 522, 205 P 251 (1922).

Sale of Land: One who has agreed to convey land when he has acquired title to it cannot terminate the contract without tendering a conveyance, or at least accompanying the demand for payment with an offer to convey. The obligation to convey being concurrent with the obligation to pay, the right to terminate the contract does not arise until the vendor has acquired title and tendered or offered a conveyance. Milwaukee Land Co. v. Ruesink, 50 M 489, 148 P 396 (1915).

28-1-405. Condition subsequent defined.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

Case Notes

Engagement Ring Given in Contemplation of Marriage Not Considered Gift — Conditional Gift Analysis: Albinger gave Harris a $29,000 diamond engagement ring when the two promised to marry. The relationship was strained, resulting in breakups and the return of the ring to Albinger several times, but each time the couple reconciled, and the ring was returned to Harris. Following their final separation, Albinger told Harris to "take the car, the horse, the dog, and the ring", so Harris moved to Kentucky, marriage plans evaporated, and Harris refused to return the ring. Albinger filed in District Court to settle ownership of the ring. The District Court found the ring to be a gift in contemplation of marriage, implying that the existence of a condition attached to the gift, and held that Albinger was entitled to return of the ring upon failure of the condition of marriage. Harris appealed, and the Supreme Court reversed. The rights and duties of parties regarding property exchanges in contemplation of marriage are determined by existing law and common-law principles. A gift is a transfer of personal property made voluntarily and without consideration, and the essential elements of an inter vivos gift are donative intent, voluntary delivery, and acceptance by the recipient. Delivery, which manifests the intent of the giver, must turn over dominion and control of the property to the recipient, and when made without condition, such a gift becomes irrevocable upon acceptance, so the Supreme Court will not void the transfer when the giver experiences a change of heart. The only revocable gift recognized under Montana law is a gift in view of death, and a gift causa mortis may be revoked by the giver at any time and is revoked by the giver's recovery from the illness or escape from the peril under which the gift was made. However, the Supreme Court declined to analogize gifts in contemplation of marriage with a gift in contemplation of death. Further, a purported gift that is part of the inducement for an agreement to do or not do a certain thing becomes the consideration essential to contract formation. An exchange of promises creates a contract to marry, albeit an unenforceable one, so when an engagement ring is given as consideration for the promise to marry, a contract is formed and legal action to recover the ring is barred by the abolition of breach of promise actions in 27-1-602. Here, the engagement ring was an unconditional, completed gift upon acceptance, and a completed gift is not revocable. Thus, the ring remained in Harris's ownership and control. Albinger v. Harris, 2002 MT 118, 310 M 27, 48 P3d 711 (2002).

Lease Agreement: Lease terminable by either party upon 10 days' notice does not impose a condition precedent performance of which must be alleged in plaintiff's complaint, but a condition subsequent which terminates the obligations of the parties to the lease. McEwen v. Big Sky of Mont., Inc., 169 M 141, 545 P2d 665 (1976).

Operation of Condition Subsequent Upon Estate: A "condition subsequent" operates upon the estate already created and vested, rendering it liable to be defeated if the condition is broken. Atlantic-Pacific Oil Co. of Mont. v. Gas Dev. Co., 105 M 1, 69 P2d 750 (1937).

28-1-406. What conditions must be performed before requiring performance by another.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Failure to Give Notice of Deficient Performance — Summary Judgment Burdens: Plaintiff alleged it had performed and was entitled to payment under a contract. Defendant answered that plaintiff had performed deficiently and that defendant had not breached the contract and owed no money under it. Since the contract required defendant to notify plaintiff of deficient performance, whether notice was given was crucial to each party's case. Defendant's answer raised the genuine issue of material fact as to whether defendant gave notice of deficiency, so that when plaintiff moved for summary judgment, plaintiff had the initial burden of offering evidence establishing the absence of notice. Statements of plaintiff's attorney that no notice had been given did not meet this burden; therefore, the burden to show that notice had been given did not shift to defendant and the court committed reversible error when it: (1) placed that burden on defendant; (2) granted plaintiff summary judgment for failure of defendant to carry the burden; and (3) refused defendant's motion for alteration or amendment of the judgment. However, defendant could have avoided an unnecessary appeal by filing affidavits or other evidence showing that defendant had given notice and that a genuine issue of material fact thus existed. Brinkman & Lenon v. P&D Land Enterprises, 263 M 238, 867 P2d 1112, 51 St. Rep. 36 (1994).

Suspension of Performance Upon Material Breach of Contract: As part of a contract for sale of real property, seller agreed to obtain release of mortgage within 1 year, and failure to do so constituted a material breach entitling buyer to suspend performance. Sjoberg v. Kravik, 233 M 33, 759 P2d 966, 45 St. Rep. 1270 (1988).

Prior Breach by Plaintiff as Bar to Enforcement of Contract: The general rule is that a party committing a substantial breach of a contract cannot maintain an action against the other contracting party or his predecessor in interest for a subsequent failure to perform if the promises are dependent. A substantial or material breach is one which touches the fundamental purposes of the contract and defeats the object of the parties in making the contract. Malloy v. Judge's Foster Home Program, Inc., 229 M 317, 746 P2d 1073, 44 St. Rep. 1996 (1987); Rogers v. Relyea, 184 M 1, 601 P2d 37 (1979).

Sufficiency of Default Notice — Mandatory Finding: Michunovich purchased a tract of land under contract for deed from the Brangers. Michunovich entered a contract for deed to sell a portion of that tract to Owen. Owen fulfilled his part of the contract. Michunovich defaulted on the Branger contract. Brangers filed a breach of contract suit against Michunovich. Michunovich served Owen a notice of termination since he was unable to secure a deed release from Brangers. Michunovich did not refund Owen's downpayment as required by the contract. Owen refused to vacate the property. Michunovich assigned all his interest in the Branger contract to Stevenson with the Brangers' consent. Since Stevenson was able to bring the Branger contract current, the Brangers stipulated to the dismissal of their suit against Michunovich. Owen filed a purchaser's lien on the property under his contract from Michunovich. Stevenson then filed a quiet title action. The trial court found for Stevenson, finding that the notice from Michunovich to Owen terminated that contract so that Owen had no interest in the land. The Supreme Court remanded because according to the terms of the contract the refund of Owen's downpayment was a condition precedent to the contract being declared void. The trial court was instructed to determine whether Stevenson's default notice terminated the Owen contract and to resolve issues regarding rental value and improvements. Stevenson v. Owen, 212 M 287, 687 P2d 1010, 41 St. Rep. 1743 (1984).

Real Estate Listing — Time Limits Binding: Defendant entered a real estate listing agreement with plaintiff. The agreement was entered June 25, 1979, and was to expire June 25, 1980, with a 180-day grace period for a buyer put in contact with the seller by the realtor. This period ended December 22, 1980. On October 23, 1979, defendant entered a buy-sell agreement with the Gerhardts, who were shown the ranch by a realtor affiliated with the defendant. The agreement was contingent on the Gerhardts' selling their ranch. The Gerhardts occupied defendant's ranch as tenants. Gerhardts were not able to sell their ranch until December 31, 1980, and on January 29, 1981, they bought defendant's ranch. Defendant refused to pay the real estate commission, and this suit followed. It is a generally accepted rule that a buyer is financially "able" only when he can command the necessary funds to complete the purchase within the time allowed by the offer. Here, the buyers were not able to purchase until they sold their ranch. Courts have generally strictly followed the time limits in listing agreements. An exception may occur if surrounding circumstances indicate the time provisions were waived by the parties or if the seller interfered with the sale. Nothing in this case suggests either, and judgment for the defendant was affirmed. Property Brokers, Inc. v. Loyning, 201 M 309, 654 P2d 521, 39 St. Rep. 2128 (1982). See also WRB-West Associates, Inc. v. Madison Addition Inv. Ltd. Partnership, 270 M 498, 893 P2d 340, 52 St. Rep. 329 (1995), distinguishing Snyder v. Schram, 547 P2d 102 (Oreg. 1976).

Specific Performance — Failure to Tender Purchase Price — Excuse: Plaintiff and defendants entered into a buy-sell agreement for a parcel of land. The agreement was prepared by defendants' real estate agent. The agreement failed to note a 60-foot roadway and utility easement. Defendants in the meantime sold an adjoining parcel of land, including an interest in the 60-foot easement. Plaintiff sued for specific performance of the buy-sell agreement. Plaintiff was excused from tendering the purchase price because defendants by selling the adjoining parcel subject to the easement indicated their refusal and inability to perform the agreement. Plaintiff is entitled to specific performance of that part of the agreement defendants are now able to convey, notwithstanding that it is the very same title plaintiff refused to accept in the first instance. Chadwick v. Giberson, 190 M 88, 618 P2d 1213, 37 St. Rep. 1723 (1980).

Performance of Conditions Precedent to Be Alleged: In an action for an accounting based on a lease and management agreement by which defendant turned over his sheep ranch, farm machinery, and sheep to plaintiffs, who were required to build fences, plant hay and grain crops, care for the sheep, and perform other similar duties before they would become entitled to their share of the revenue from the sale of lambs and wool, the requirements were conditions precedent, and to state a cause of action on a contract of this nature, plaintiffs were required to allege performance under this contract or set forth facts excusing failure to perform. First Nat'l Bank of White Sulphur Springs v. Stoyanoff, 137 M 20, 349 P2d 1016 (1960).

Abandonment of Contract: Where written contract was clear and explicit and neither party performed his part of the contract but acted contrary to terms of contract pursuant to a subsequent oral agreement, there was an abandonment of the original contract. Eggers v. Gen. Refrigerating Co., 123 M 205, 210 P2d 636 (1949).

Sale of Corporate Stock:

If agreement relating to sale of corporate stock gave purchaser an option to return it on becoming dissatisfied with his bargain, return of it was a condition precedent to his right to maintain an action to recover the purchase price paid, and defendant in such an action could invoke the doctrine of waiver and estoppel because of plaintiff's retention of dividends paid on the stock after the accrual of his right to return it. Peterson v. Nelson, 77 M 539, 252 P 368 (1926).

Complaint in action to recover purchase price of corporate stock based on contract for its redelivery and payment of the price paid within a specified time is insufficient where the concurrent condition of redelivery is not alleged. Porter v. Plymouth Gold Min. Co., 29 M 347, 74 P 938 (1904).

Pleading: Where the right of recovery is dependent upon happening of condition precedent, the happening of the condition must be alleged. Broat Lumber Co. v. Van Houten, 66 M 478, 213 P 1116 (1923).

Sale of Real Property: In an action to cancel contract for sale of real estate and forfeit the downpayment, the condition that plaintiffs should secure authority from probate court to execute the deed and make delivery of it to the defendant within a reasonable time, was a condition precedent to putting defendant in default. Henderson v. Daniels, 62 M 363, 205 P 964 (1922), overruled on another point by Thelen v. Vogel, 86 M 33, 281 P 753 (1929).

Valid Defense: A right dependent on a condition precedent does not accrue unless or until the condition is performed. It is a valid defense in a contract action to show that the obligation to perform was based on a condition which was not complied with. White v. Hulls, 59 M 98, 195 P 850 (1921).

Delivery of Grain: Where delivery of a carload of oats and payment therefor were to be concurrent at shipping point, the buyer was required, in his action for breach of the contract of sale, to show an offer and ability to pay at that point. Jenderson v. Hansen, 50 M 216, 146 P 473 (1915).

28-1-407. When prior performance of conditions excused.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Specific Performance — Failure to Tender Purchase Price — Excuse: Plaintiff and defendants entered into a buy-sell agreement for a parcel of land. The agreement was prepared by defendants' real estate agent. The agreement failed to note a 60-foot roadway and utility easement. Defendants in the meantime sold an adjoining parcel of land, including an interest in the 60-foot easement. Plaintiff sued for specific performance of the buy-sell agreement. Plaintiff was excused from tendering the purchase price because defendants by selling the adjoining parcel subject to the easement indicated their refusal and inability to perform the agreement. Plaintiff is entitled to specific performance of that part of the agreement defendants are now able to convey, notwithstanding that it is the very same title plaintiff refused to accept in the first instance. Chadwick v. Giberson, 190 M 88, 618 P2d 1213, 37 St. Rep. 1723 (1980).

Condition Precedent: Before any party to an obligation can require another party to perform any act under it, he must fulfill all conditions precedent thereto imposed upon himself and must be able and offer to fulfill all conditions concurrent imposed upon him by their fulfillment by the other party except as provided by this section. Management, Inc. v. Mastersons, Inc., 189 M 435, 616 P2d 356, 37 St. Rep. 1601 (1980).

Obligation to Make Payments Under Mining Agreement When Escrow Not Established: In a mining agreement with an option to purchase, the covenant to establish escrow was a material part of the contract and a condition precedent to the plaintiff's obligation to make payments. Although the plaintiff knew escrow had not been established, he did not waive the requirement, and the defendant defaulted first when he refused to establish escrow. Therefore, the defendant could not enforce the making of payments. Rogers v. Relyea, 184 M 1, 601 P2d 37 (1979).

Waiver: A party entitled to performance of a condition precedent may waive the condition either expressly or by his actions. Fed. Sur. Co. v. Basin Constr. Co., 91 M 114, 5 P2d 775 (1931). See also Reilly v. Maw, 146 M 145, 405 P2d 440 (1965).

28-1-408. Condition involving forfeiture to be strictly construed.

Case Notes

Show of Prejudice From Untimely Notice Required to Deny Coverage: The plaintiff filed an action for a declaratory judgment that it was not required to defend under a commercial general liability policy its insured that had entered into an agreement with a third party. The plaintiff argued that the policy required the insured to provide timely notice of a claim, which the insured did not. The federal District Court held that the plaintiff was excused from defending because of the insured's failure to provide timely notice of a claim. The case was appealed to the Ninth Circuit Court of Appeals, which certified the question of whether an insurer must show prejudice from the lack of notice in order to deny a claim. The Supreme Court held that an insurer must prove that it suffered prejudice in order to deny coverage. Atlantic Casualty Ins. Co. v. Greytak, 2015 MT 149, 379 Mont. 332, 350 P.3d 63.

Waiver of Contract Rights — Late Payments Not Considered Breach Based on Prior Acceptance: The uninsured employers' fund (UEF) sought indemnity from an employer that did not have workers' compensation insurance using a monthly payment arrangement that was agreed to by the parties. The UEF accepted four late payments before turning the employer over to collections, at which point the employer sued UEF for breach of contract. The Supreme Court held that UEF waived its right to terminate the contract based on late payment when it accepted late payments without objection. Consequently, it was a breach of contract for the UEF to turn the employer over to collections and the employer was entitled to damages. Elk Mtn. Motor Sports, Inc. v. Dept. of Labor and Industry, 2012 MT 261, 367 Mont. 36, 289 P.3d 165.

Coordination of Habendum and Pugh Clauses in Oil and Gas Lease — Shut-In Gas Well Considered Producing Well for Lease Purposes — Lease Extended on Section With Producing Well, Terminated on Undeveloped Sections for Lack of Timely Rental Payments: Plaintiff's oil and gas leases had habendum clauses, which provided that the primary leases would be extended as long as oil or gas was produced or drilling operations continued on any of the leased property, and Pugh clauses, which provided that production would not serve to extend the primary term of a lease unless the lessee paid an annual per-acre rental fee prior to the end of the primary term. By the end of the primary term, plaintiff had only one shut-in well developed on the leasehold. Depending on the habendum clauses, plaintiff concluded that there was not a producing well on the leasehold, so the Pugh clauses did not take effect and rental payments were not required. Depending on the Pugh clauses, defendants concluded that because there were no producing wells on the leasehold and because the rental fee on the shut-in well was 2 days late, all of plaintiff's leases were canceled. In reconciling the clauses, the District Court correctly found that: (1) the Pugh clauses required that rental payments be paid on or before the expiration of the primary term in order to extend leases on undeveloped sections; and (2) because time is of the essence in oil and gas leases and plaintiff did not pay timely rental, the leases expired by their own terms on all sections except the section containing the shut-in well, which was considered a producing well, and that lease would continue under the habendum clause as long as plaintiff used reasonable diligence in marketing the gas. Sandtana, Inc. v. Wallin Ranch Co., 2003 MT 329, 318 M 369, 80 P3d 1224 (2003).

Forfeiture — Affirmative Defense: Forfeiture is an affirmative defense and must be pleaded in the defendant's answer to a complaint. It will not be considered for the first time on appeal. Massar Cattle Co. v. Reese, 216 M 22, 699 P2d 87, 42 St. Rep. 609 (1985).

Gross Negligence in Failure to Perform — No Relief From Forfeiture: The seller of real property is entitled to cancellation of a contract for deed. The purchasers are not entitled to any equitable relief from forfeiture because they were grossly negligent in failing to perform in accordance with the terms and provisions of the contract. Redinger v. French, 216 M 16, 699 P2d 94, 42 St. Rep. 604 (1985).

Buy-Sell Agreement: A buy-sell agreement contained an earnest money forfeiture clause and a clause making the agreement contingent upon the buyer's obtaining a contract for deed for that part of the seller's interest subject to a previous contract for deed. As the latter clause was not a condition precedent whose lack of performance required the return of the earnest money, the forfeiture clause was upheld. Wendy's of Mont. v. Larsen, 196 M 525, 640 P2d 464, 39 St. Rep. 299 (1982).

Waiver of Default — Limit of Scope: Though after a default by purchaser, vendor accepted sums due and performed according to the contract, such action does not constitute a total waiver of default provisions. Following Suburban Homes Co. v. North, 50 M 108, 145 P 5 (1914), such a waiver does not compel vendor to keep contract open indefinitely; on the contrary, the vendor waives the right to forfeit only for the time being and may terminate the contract after purchaser is given suitable notice and a reasonable time to pay. Mont. Williams Double Diamond v. Royal Village, Inc., 186 M 359, 607 P2d 1120 (1980).

Interest in Insurance Proceeds — Issue of Law — Implied Waiver of Default Provision: Summary judgment was improperly granted when the record disclosed, as a matter of law, that plaintiff had a possessory interest in a building on the property in dispute at time of destruction by fire, giving plaintiff a corresponding right to the insurance proceeds less the unpaid balance of the purchase price. This result was based on an implied waiver of a contract default provision by defendant county's failure to timely repossess. Hansen v. Transamerica Ins. Co., 175 M 273, 573 P2d 663 (1978).

Forfeiture Improper: Interpreting the forfeiture clause of a mine sale contract against plaintiffs, the parties for whose benefit the provision was created, it can hardly be said that the contract requires forfeiture for failure to produce 300 yards of material each working day. The appropriate remedy is an award of damages for breach of contract, even though not requested in the pleadings. Smith v. Zepp, 173 M 358, 567 P2d 923 (1977).

Assignment of Lease: Under lease providing that lessee would not assign lease without consent of lessor, and that sale of more than 50% of the stock would be considered an assignment, no violation of lease occurred where lessor had consented to sale of stock in one instance, and such stock was then pledged as security for a loan, which security was then surrendered for the payment of the loan. Such surrender was by operation of law, and provision restraining assignment of lease includes only voluntary assignments and is not operative against an assignment effected by law. Lipsker v. Billings Boot Shop, 129 M 420, 288 P2d 660 (1955).

Strict Interpretation Against Benefited Party: This section requires a condition involving a forfeiture to be strictly interpreted against the party for whose benefit it is created, and trial court erred in declaring a forfeiture of the drilling agreement between a lessee of oil and gas and an operator, for failure to find a market for plaintiff's share of the gas produced by defendant operator. Cedar Oil & Gas Co. v. Archer, 112 M 477, 117 P2d 265 (1941).

Sufficiency of Allegations to Sustain Action on Forfeiture: Where purchaser of farm land, under contract which made time of the essence and provided that in case of default in payment the purchaser should forfeit his right to possession and all payments made as liquidated damages, remained in possession for 10 years without any complaint, and then finding himself unable by reason of conditions beyond his control to meet the final payment, notified vendor of his inability to make payment and of his desire to surrender the land, whereupon the contract was declared forfeited, his complaint in his action to be relieved of the forfeiture, asking recovery of difference between payments made by him under the contract, with taxes, insurance, cost of improvements made by him, etc., and rental value of property, was held insufficient to state facts which appeal to the conscience of a court of equity and therefore insufficient to state a cause of action under 28-1-104. Estabrook v. Sonstelie, 86 M 435, 284 P 147 (1930).

Forfeiture Favored in Oil and Gas Leases: While generally speaking forfeitures are not favored in the law, in the case of an oil and gas lease, forfeiture is favored rather than frowned upon because of injury that may result to lessor from delay, where it clearly appears that lessee has failed to commence operations within the time stipulated or thereafter neglected to prosecute such operations with diligence. Solberg v. Sunburst Oil & Gas Co., 76 M 254, 246 P 168 (1926).

Intention of Parties: In order to provide for a forfeiture there must be a plainly expressed intention by parties that the language employed is to have that effect. Finley v. School District, 51 M 411, 153 P 1010 (1915).

Part 5
Alternative Obligations

28-1-501. Who may select between alternative performances.

Case Notes

Time of Payment: Where one offered to purchase lands at a certain price, part to be paid in cash and balance in 2 or 3 years, and the vendor agreed to these terms, the vendee had the option to elect whether to make the deferred payment either in 2 or 3 years. Long v. Needham, 37 M 408, 96 P 731 (1908).

28-1-502. How right of selection lost.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Part 10
Transfer of Rights and Duties Under Obligation

Part Law Review Articles

Is a Promise to Perform That Which Is Due a Third Party Sufficient Consideration to Support a Promise?, Babbitt, 8 Mont. L. Rev. 86 (1947).

28-1-1001. Rights arising out of obligation transferable.

Compiler's Comments

2005 Amendment: Chapter 392 inserted second sentence providing that unless otherwise provided by law, a transfer by written, oral, electronic, or other means creates a valid assignment upon the transfer; and made minor changes in style. Amendment effective October 1, 2005.

Case Notes

Enforcement of Agricultural Lien Following Sale or Transfer of Farm Products — Assignment of Inchoate or Unperfected Lien Interests Allowed: A crop of sugar beets was sold, and a pesticide sprayer that held an agricultural lien sought to enforce the lien after the sale. Plaintiff bank also held a secured interest on the proceeds of the crop. The buyer issued checks made payable jointly to the bank and the sprayer, honoring the agricultural lien, and the lienholder's unconditioned negotiation of the check acknowledged satisfaction and release of its lien. The bank asserted that, not being an agricultural supplier, the sprayer had no right to file the lien and further contended that because inchoate or unperfected liens are not assignable, any argument that the supplier had assigned its lien right to the sprayer must fail as a matter of law. The sprayer argued that the supplier was clearly eligible to file an agricultural lien and that all actions taken by the sprayer were taken in an agency capacity for the supplier, as indicated in the lien filing, so the payment was not an assignment. Alternatively, the sprayer contended that the transaction was a pass-through between related entities constituting a limited assignment for collection purposes only and that even if the bank's evidence was sufficient to demonstrate that the transaction was a full assignment supported by consideration, inchoate lien interests are nonetheless assignable. The Supreme Court concluded that the dispute was best resolved on the issue of the assignability of inchoate lien interests, noting that generally property of any kind may be transferred, that a right arising out of an obligation is the property of the person to whom it is due and may be transferred, and that Montana's general policy supports the free assignability of rights and obligations stemming from contractual obligations. An agricultural lien is a security and ought to follow the debt or contract to which it pertains, and the free assignability of the right to perfect an agricultural lien comports with lien statutes as well as modern business practices. Thus, even though the supplier's lien was not yet perfected when transferred to the sprayer, it was assignable, and the sprayer validly proceeded to perfect and enforce the lien and was entitled to funds in the amount stipulated by the parties as payment for the chemicals sold by the supplier to the farm and applied by the sprayer and was entitled to the interest on the funds to be credited on that sum. Stockman Bank of Mont. v. Mon-Kota, Inc., 2008 MT 74, 342 M 115, 180 P3d 1125 (2008).

Assignment Not Prohibited by Contract — Mineral Development Contract Not So Personal or Unique as to Preclude Assignment: A contract for the development of a mineral interest did not prohibit assignment or delegation. Despite this fact, appellants pointed out that an exception to the general rule (that rights arising under a contract are generally assignable unless prohibited by the contract) exists when the contract is personal in nature and an assignment would deprive a party of the benefit of his bargain. The Supreme Court acknowledged this exception but found that the duties imposed by the agreement were not so unique in the industry as to involve a degree of trust and confidence singularly personal to the contracting parties. Somont Oil, Inc. v. Nutter, 228 M 467, 743 P2d 1016, 44 St. Rep. 1685 (1987).

Ambiguous Assignment — Construction of Document as a Whole: Peterson sold property to the Blairs under a contract for deed that reserved one-half the mineral rights in Peterson. Peterson then assigned her rights under the contract to Hopkins. The Blairs paid Hopkins and recorded. Peterson sued Hopkins to quiet title when the lessee of Peterson's one-half mineral rights claimed Peterson had assigned them to Hopkins by mistake. Hopkins was granted summary judgment because the assignment conveyed all of Peterson's right, title, and interest in the property, together with the contract for deed. The judgment was reversed, and judgment was granted Peterson. The assignment stated that it was subject to the contract for deed, thus creating an ambiguity. Taken as a whole, it appeared that the assignment was of the contract for deed and was not itself a deed of the entire surface and mineral interests to Hopkins. This was supported by the conduct of the parties, for Peterson leased her reserved interest for the 22 years following the assignment until lessee raised the alleged mistake, and at no time up to his death in the 17th year of the 22 years did Hopkins claim all the mineral rights or demand Peterson's one-half interest. Peterson v. Hopkins, 210 M 429, 684 P2d 1061, 41 St. Rep. 1140 (1984).

Ambiguous Assignment — Explanatory Evidence Admissible: A contract for deed reserved one-half the mineral rights in seller. Seller's subsequent assignment was ambiguous where it assigned all of seller's right, title, and interest in the property, together with the contract for deed, yet also stated that it was subject to the contract for deed. Therefore, the evidence was admissible to explain the ambiguity and the intent of seller and assignee of seller's rights under the contract for deed. Peterson v. Hopkins, 210 M 429, 684 P2d 1061, 41 St. Rep. 1140 (1984).

28-1-1002. When burden of obligation may be transferred.

Case Notes

Transfer of Obligation — Transfer of Performance of Duty Not Prohibited: A health care provider issued refunds for overpayment to a patient on two occasions by mailing prepaid debit cards issued through a bank in the amount of the refund due. The patient activated the first card but did not use either card to pay for goods, withdraw money at an ATM, or exchange the cards for cash at a bank. The patient sued the health care provider, alleging, among other claims, a violation of 28-1-1002 for unlawfully transferring the health care provider's obligation to the bank without the patient's consent. The District Court found for the health care provider, holding that 28-1-1002 prohibits the nonconsensual transfer of the obligation itself but does not prohibit the transfer of the performance of the obligation. The health care provider could lawfully delegate the performance of its duty to refund the patient without wholly delegating its duty to refund the payment. The Supreme Court affirmed the District Court's holding. Bratton v. Sisters of Charity of Leavenworth Health Sys., 2020 MT 86, 399 Mont. 490, 461 P.3d 127.

Assignor Not Liable for Breach by Debtor: Plaintiffs, tribal members, obtained a loan from the Blackfeet Tribe. Plaintiffs defaulted, and the tribe obtained a judgment in tribal court. The tribe filed notice with the Clerk and Recorder and the District Court. Plaintiffs agreed to sell their ranch to Robertson and to provide title insurance. A portion of the purchase price was placed in escrow to cover the amount owing the tribe. The escrow agreement contained a provision assigning pasturage fees to which plaintiffs were entitled to Robertson. Plaintiffs later filed suit against the tribe and Robertson. On appeal, the Supreme Court held that it is an established rule of contract law that the assignor does not guarantee that the obligor will pay and that the assignor is not liable to the assignee for breaches of the assignment by the debtor. Robertson could not recover pasturage fees from the plaintiffs, because plaintiffs did not owe them. Wippert v. Blackfeet Tribe, 201 M 299, 654 P2d 512, 39 St. Rep. 2117 (1982), overruled in part on other grounds by Green v. Gerber, 2013 MT 35, 369 Mont. 20, 303 P.3d 729.

Part 11
Extinction of Obligation by Performance

28-1-1101. Extinction of obligation by full performance.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

Case Notes

Surrogacy Contract Terminated by Its Own Terms on Surrogate's Relinquishment of Child. Sayler v. Yan Sun, 2023 MT 175, 413 Mont. 303, 536 P.3d 399.

Option Agreement — Sufficiency of Consent and Consideration: The defendant appealed from a judgment granting specific performance of an option agreement to the plaintiff and ordering the property involved conveyed to the plaintiff. On appeal, the Supreme Court rejected the defendant's contention that the writing involved was not an option agreement because it failed to meet the essential requirements for the validity of a contract. In particular, he contended that there was a lack of consent and that the consideration was legally insufficient. The Supreme Court found the actual payment of $1 and actual participation in a family corporate dissolution sufficient consideration for the agreement. A memorandum here acted as an offer, and a binding agreement resulted from action on that offer by the offeree. The trial court was affirmed. Van Atta v. Schillinger, 191 M 472, 625 P2d 73, 38 St. Rep. 426 (1981).

28-1-1102. Performance by one of several joint debtors.

Case Notes

Guarantor Owes Pro Rata Share: Appellant and four other shareholders in company executed continuing guaranties for promissory notes on behalf of their shared business. Appellant subsequently signed away his share in company and left the business. Although the court considered appellant's equitable defense that he was not liable for his pro rata share of the notes because the other four guarantors personally profited from the sale of the business after appellant departed, he remains liable for his pro rata share. He signed the guaranty knowing the lender could sue him directly on the notes. All five shareholders shared equal liability on the promissory notes, and appellant is required to contribute his one-fifth pro rata share. Citizens St. Bank v. Bossard, 226 M 75, 733 P2d 1296, 44 St. Rep. 468 (1987).

Joint and Several Note: Where note sued upon is joint and several the complaint must, in order to show a breach of condition, allege that payment has not been made by any of the parties liable, since payment by one of the makers extinguishes the liability of all. First Nat'l Bank of Butte v. Silver, 45 M 231, 122 P 584 (1912).

28-1-1104. Extinction when directions of creditor followed.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Extinguishment of Debt: Where a creditor directed his debtor (his niece) to transfer property to her daughters in payment of the debt without consideration moving from them to him and the transfer was made, a finding that it was based on the consideration of natural love and affection only was erroneous, the consideration having been the extinguishment of the debt due from the grantor to her creditor. Hale v. Belgrade Co., 75 M 99, 242 P 425 (1925).

28-1-1105. When partial performance extinguishes part of obligation.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Cattle Feeding and Sale — Complete Breach of Nonseverable Contract: A joint venture was formed, the contract contemplating the feeding of cattle by one party until 80% graded "choice", followed by sale and splitting of the proceeds with the supplier of the cattle, who was the second party. When cattle prices dropped, the feeder lost his financing and defaulted on the contract. The agreement was entire and nonseverable. Having failed in the complete performance of the contract, the feeder could not recover under it. Restitution to the feeder of his expenses before default would have to be based on implied contract theory. In order for a claim of restitution to lie, there must be no willful or intentional departure from the contract, and the defects in performance must not pervade the whole or be so essential that the object which the parties intended to accomplish is not accomplished. The feeder could not recover his prior expenses because a party who has completely breached an entire, nonseverable contract, without justification or excuse, may not recover for any performance rendered prior to the breach. On the contrary, a counterclaim against the feeder for damages was upheld. Roundup Cattle Feeders v. Horpestad, 184 M 480, 603 P2d 1044 (1979), distinguishing Murphy v. Redland, 178 M 296, 583 P2d 1049 (1978).

Defaulting Party's Right to Accounting — Contract Entire or Divisible: To determine whether or not a party defaulting on a contract is entitled to an accounting (either contractually or equitably), it must be determined first whether the contract was entire or severable. This depends very largely on contractual terms and on the intention of the parties disclosed by those terms. As a general rule, a contract is entire when by its terms, nature, and purpose it contemplates and intends that each and all of its parts are interdependent and common to one another and to the consideration. A contract contemplating the feeding of cattle by one party until 80% graded "choice", followed by sale and splitting of the proceeds with the supplier of the cattle, was held clearly intended to be entire and nonseverable. The feeder's default and abandonment completely frustrated the purpose, intent, and terms of the joint venture agreement. The feeder thereby forfeited any right it may have had to an accounting under the contract. When the joint venture was destroyed by abandonment by one of the joint venturers, equity would not compel an accounting because a wrongdoer may not take advantage of his own wrong. Roundup Cattle Feeders v. Horpestad, 184 M 480, 603 P2d 1044 (1979), distinguishing Murphy v. Redland, 178 M 296, 583 P2d 1049 (1978).

Election of Remedies:

A contractor may, on breach of contract by other party by refusal to make payment due during progress of work, discontinue work and elect either to sue upon contract to recover damages for its breach, or ignore the contract and bring action on quantum meruit. When he pursues the former remedy he is entitled to recover the entire amount due at time of default, including percentages reserved on previous estimates, with interest, from date on which contract was breached. Clifton-Applegate-Toole v. Big Lake Drain District, 82 M 312, 267 P 207 (1928).

One charging wrongful interference with contract by other party thereto can treat wrongful act as a breach and sue for damages (difference between contract price and cost to him of doing work) or treat contract as ended and sue on quantum meruit for work already done. McFarland v. Welch, 48 M 196, 136 P 394 (1913).

Retention of Benefits From Work Done: Where defendant's retention of benefits from work done under the partial performance of a contract to plow and sow land with wheat was not voluntary, he was not liable for the work done. Waite v. Shoemaker & Co., 50 M 264, 146 P 736 (1915).

28-1-1106. Application of performance when there are several obligations.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Defendant Not Allowed to Characterize Damages: Shilhaneks were injured in a vehicle accident, and defendants were ordered to pay more than $3 million in damages, including punitive damages. Defendants requested that the $750,000 tendered to Shilhaneks to date be allocated toward payment of the punitive award and that Shilhaneks be required to file a corresponding satisfaction of judgment with respect to the punitive damages award, in essence asserting that a defendant has the power to specifically designate payment toward a particular award. Defendants cited 25-9-311 for the rule that a satisfaction of judgment must be provided by the party in whose favor judgment is entered and contended that under 28-1-1225 and this section, the power lies with the debtor, not the creditor, when it comes to designating to which particular obligation a payment should be credited. The District Court denied the request, noting that Title 28 applies only to contractual obligations and that Title 25 governs obligations arising from judgments. The District Court did not abuse its discretion, given defendants' failure to provide a legal basis that would allow them to dictate how damages owed are characterized, the fact that defendants owed more than double the available insurance coverage and were obligated to pay the policy limits to satisfy the verdict, and that allocating 22% of the available insurance proceeds to the punitive damage award would have harsh tax consequences on Shilhaneks. Shilhanek v. D-2 Trucking, Inc., 2000 MT 16, 298 M 101, 994 P2d 1105, 57 St. Rep. 89 (2000).

Failure to Direct Application of Payment:

Absent instructions from the debtor as to which note to apply rents to, it was not a breach of the duty of good faith and fair dealing for a savings and loan to apply the rents to satisfy an August note prior to satisfying a July note in light of the fact that the debtor was notified of the action but failed to object. Am. Fed. S&L Ass'n v. Buckland, 238 M 364, 777 P2d 1289, 46 St. Rep. 1339 (1989).

When a debtor owes more than one debt and on making a general payment fails to direct the creditor as to which debt should receive the credit, the creditor may apply it on any one of the debts, secured or unsecured, and a surety on the secured debt is in no position to complain if made on one unsecured. Nat'l Bank of Mont. v. Bingham, 91 M 62, 5 P2d 554 (1932).

Under this section a debtor owing more than one debt or a debt consisting of more than one item (as principal and interest) has the right to direct application of a payment voluntarily made by him, and if the creditor accepts the payment and retains it, the law will treat it as having been applied as directed. Monidah Trust v. Hruze, 62 M 444, 205 P 232 (1922).

Second Lease Canceling First Lease — Subsequent Payments: The parties entered into a second lease that canceled the first lease, with neither party reserving any rights. The lower court's ruling that subsequent payments could not be applied to rents owed under the first lease due to lessor's not reserving its rights was affirmed on appeal. The Supreme Court held, however, that lessor could apply the payments to other accounts existing between the parties since lessee had not specified to which account the payments applied. Empire Dev. Co. v. Johnson, 236 M 433, 770 P2d 525, 46 St. Rep. 487 (1989).

Application of Debtor's Payment to Past Due Account With Creditor — Debtor's Instructions — Creditor's Lien Despite Payment: Defendant contracted for a new building. The contractor purchased materials from the plaintiff through a subcontractor who had an account with the plaintiff. When the subcontractor was paid by the defendant, he in turn paid the plaintiff. The plaintiff applied the payment to the subcontractor's past due account, then later filed a lien against the defendant. The defendant appealed from a judgment upholding the lien. Because a creditor is bound by the instructions given to him by his debtor as to the application of a payment, the issue on appeal was the instructions the subcontractor gave to the plaintiff. With no trial court finding of a duty of the plaintiff to apply the funds paid to it by the subcontractor to the bill for materials used by the defendant, the Supreme Court followed the clear mandate from the Legislature and held that the defendant was liable to the plaintiff on the lien judgment against him, while recommending that the Legislature review the statute. Gen. Elec. Supply v. Mont. Auto. Ass'n, 189 M 553, 617 P2d 136, 37 St. Rep. 1715 (1980), distinguished in Witbart v. Witbart, 204 M 446, 666 P2d 1217, 40 St. Rep. 995 (1983).

Liquor License Sale Proceeds: Where debtor's liquor license had been purchased with advances from bank under security agreement, proceeds from the sale of such license were to be applied first to notes secured by such security agreement, then to note secured by an attachment, and finally to other obligations since sale contract provided that all proceeds were to be placed in escrow with bank to whom all debts were owed. Gallatin Trust & Sav. Bank v. Darrah, 152 M 256, 448 P2d 734 (1968).

No Presumption That Payments Made on Last Accruing Obligation: It is incumbent upon defendant, in order for him to sustain the burden of proof that an action to recover wages due under a contract of employment was barred because most of the items accrued more than 5 years prior to commencement of the action, to show that the partial payments were applied on the items last accruing rather than the oldest, the record failing to show any direction for application thereof by either party. There is no presumption that payments were made on an obligation last accruing. Girson v. Girson, 112 M 183, 114 P2d 274 (1941).

Statute of Limitations: In an action to recover balance due on contract for the purchase of water stock and to foreclose mortgages on land securing contracts, where company constructed its water distribution system under contract with the Carey Land Act Board, payment of an installment of the purchase price made 8 years before suit and credited first to interest on the entire unpaid balance prevented the 8-year Statute of Limitations from running against any of the installments remaining unpaid. Valier-Montana Land & Water Co. v. Ries, 109 M 508, 97 P2d 584 (1940).

When Consent Necessary for Application: Where defendant in action to recover balance due for goods, wares, and merchandise claimed he turned the property over to a corporation which agreed to discharge his personal debts incurred in working the mine, and that the plaintiff had so applied certain payments made by it, it was held that in absence of showing that the corporation had consented to having payments made by it so applied, neither plaintiff nor defendant could rely on the doctrine of application of payments declared by this section. Ingman v. Hewitt, 107 M 267, 86 P2d 653 (1938).

Agreement as to Application of Payment: Where several written instruments relating to the same indebtedness contained no provision for the order of payment, parol evidence was competent to show what application of a payment was agreed on. Grogan v. Valley Trading Co., 30 M 229, 76 P 211 (1904).

28-1-1112. Objections to tender — waiver.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Waiver of Contract Rights — Late Payments Not Considered Breach Based on Prior Acceptance: The uninsured employers' fund (UEF) sought indemnity from an employer that did not have workers' compensation insurance using a monthly payment arrangement that was agreed to by the parties. The UEF accepted four late payments before turning the employer over to collections, at which point the employer sued UEF for breach of contract. The Supreme Court held that UEF waived its right to terminate the contract based on late payment when it accepted late payments without objection. Consequently, it was a breach of contract for the UEF to turn the employer over to collections and the employer was entitled to damages. Elk Mtn. Motor Sports, Inc. v. Dept. of Labor and Industry, 2012 MT 261, 367 Mont. 36, 289 P.3d 165.

Failure to Timely Enforce Contract Provision Insufficient of Itself to Constitute Waiver — Proof of Waiver — Reasonable Diligence Required of Rescinding Party: Mere failure to take steps to enforce a legal right under a contract in a timely manner is not, by itself, sufficient to constitute proof of waiver. Rather, a party claiming waiver must prove that the language or conduct by the other party showed unequivocally that the party voluntarily and intentionally relinquished the right to receive the full benefit of the contract. (See Pipe Indus. Ins. Fund Trust v. Consol. Pipe Trades Trust, 233 M 162, 760 P2d 711, 45 St. Rep. 1392 (1988).) Even though a party may be entitled to rescind a contract because of failure of consideration, the rescinding party must take action within a reasonable time upon discovering the facts that enable the rescission. Here, the District Court erred in concluding, without first determining whether the provisions of 28-2-1713 were complied with, that purchasers under a contract could rescind for failure of consideration. Norwood v. Serv. Distrib., Inc., 2000 MT 4, 297 M 473, 994 P2d 25, 57 St. Rep. 8 (2000), following Liddle v. Petty, 249 M 442, 816 P2d 1066, 48 St. Rep. 779 (1991).

Acceptance of Payment — Waiver of Right to Demand Acceleration: Bailey sold Lilly real property under a contract. Six years later Lilly sold the property to Hiramoto subject to Bailey's interest. Bailey refused to consent to the sale unless Lilly paid off the original contract in full. After the sale by Lilly to Hiramoto, Bailey filed suit alleging default. Prior to trial, Bailey continued to accept the payments from the escrow account for Lilly's obligation under the contract. District Court held that Lilly did not breach his agreement with Bailey and that any right of Bailey to demand acceleration of the balance due was waived as Bailey accepted Lilly's payments under the terms of the contract up until the date of trial. Bailey v. Lilly, 205 M 35, 667 P2d 933, 40 St. Rep. 1079 (1983).

Acts Constituting Waiver: Party who was obligated to sell shares of stock under repurchase agreement waived objections to tender by failing to object to terms of tender, conduct evidencing his willingness to sell and requesting a change in payment terms. State ex rel. Howeth v. D. A. Davidson & Co., 163 M 355, 517 P2d 722 (1973), overruled, with regard to elements of collateral estoppel, in Dagel v. Great Falls, 250 M 224, 819 P2d 186, 48 St. Rep. 919 (1991).

Check as Tender: Ordinarily a check is not a tender, but it may be as effective as a tender of currency if there is no timely objection to the form of tender, or if the objection is waived. Schultz v. Campbell, 147 M 439, 413 P2d 879 (1966).

Insufficiency of Tender:

Where the makers of a renewal note tendered an amount in payment which did not include a disputed attorney's fee, failure to include the fee in the tender rendered it ineffective to discharge the mortgage lien. Jensen v. Franklin, 135 M 341, 340 P2d 832 (1959).

Insufficiency of the tender of delinquent taxes by a mortgagee seeking to redeem from the county was immaterial because, first, objections to a tender are waived unless specified at the time and, second, they are waived where the tenderee's attitude would make the tender a vain and idle ceremony. Blackford v. Judith Basin County, 109 M 578, 98 P2d 872 (1940).

Specific Performance on Option to Purchase Real Property: In action for specific performance by lessee having option to purchase real property, tender could not be objected to where it was evident that defendants would not have conveyed property no matter what was done in the way of a tender and no objection was made to the tender at the time it was made. Fiers v. Jacobson, 123 M 242, 211 P2d 968 (1949), distinguished in Dalakow v. Geery, 132 M 457, 318 P2d 253 (1957).

Tender Unnecessary: In an action for damages for breach of a contract of sale of real property, where defendant vendor conveyed the property to another when his contract with vendee was still valid, tender was not necessary for recovery, hence unnecessary to plead. Thompson v. Lincoln Nat'l Life Ins. Co., 110 M 521, 105 P2d 683 (1940).

Rescission of Contract for the Sale of Goods: Where one seeking to rescind a contract relating to the furnishing of a furnace requests the one furnishing it to remove it because it is unsatisfactory, the latter, on refusing, must point out his objection to the offer to return it at the time it is made, and if he does not do so he will be deemed to have waived all objections thereto and is precluded from later objecting to the sufficiency of the tender. O'Keefe v. Routledge, 110 M 138, 103 P2d 307 (1940).

28-1-1113. Creditor's retention of thing that creditor refuses to accept.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Part 12

Extinction of Obligation by Offer of Performance

28-1-1201. When obligation extinguished by offer of performance.

Case Notes

Unconditional Offer and Ability to Perform: An unconditional offer in good faith to perform made by the party upon whom the obligation rests, coupled with the ability to perform, is equivalent to full performance and extinguishes the obligation as to the party making the offer, and a wrongful refusal to accept it disables the other party from claiming any benefit. Lehrkind v. McDonnell, 51 M 343, 153 P 1012 (1915), distinguished in Audit Serv., Inc. v. Frontier-West, Inc., 252 M 142, 827 P2d 1242, 49 St. Rep. 186 (1992). See also Hanlon v. Manger, 85 M 31, 277 P 433 (1929).

28-1-1202. Effect of offer.

Case Notes

Failure to Timely Enforce Contract Provision Insufficient of Itself to Constitute Waiver — Proof of Waiver — Reasonable Diligence Required of Rescinding Party: Mere failure to take steps to enforce a legal right under a contract in a timely manner is not, by itself, sufficient to constitute proof of waiver. Rather, a party claiming waiver must prove that the language or conduct by the other party showed unequivocally that the party voluntarily and intentionally relinquished the right to receive the full benefit of the contract. (See Pipe Indus. Ins. Fund Trust v. Consol. Pipe Trades Trust, 233 M 162, 760 P2d 711, 45 St. Rep. 1392 (1988).) Even though a party may be entitled to rescind a contract because of failure of consideration, the rescinding party must take action within a reasonable time upon discovering the facts that enable the rescission. Here, the District Court erred in concluding, without first determining whether the provisions of 28-2-1713 were complied with, that purchasers under a contract could rescind for failure of consideration. Norwood v. Serv. Distrib., Inc., 2000 MT 4, 297 M 473, 994 P2d 25, 57 St. Rep. 8 (2000), following Liddle v. Petty, 249 M 442, 816 P2d 1066, 48 St. Rep. 779 (1991).

What Constitutes Valid Tender: In order to constitute a valid tender, the party making the tender must offer a specific amount that covers all that the other party is entitled to, including interest, costs, and attorney fees. Audit Serv., Inc. v. Frontier-West, Inc., 252 M 142, 827 P2d 1242, 49 St. Rep. 186 (1992), distinguishing Lehrkind v. McDonnell, 51 M 343, 153 P 1012 (1915).

Promise of Performance Not Equivalent to Unconditional Tender of Performance: Obligor gave written notice of the intention to prepay the balance of a contract for deed but never made the payment. The statement of what the obligor intended to do in the future never rose to the level required to make an unconditional tender of performance that would trigger the *Lehrkind* rule or to the level required to constitute an offer to pay under this section; therefore, the obligation was never extinguished. Keller v. Dooling, 248 M 535, 813 P2d 437, 48 St. Rep. 554 (1991).

Contention of Error in Award of Prejudgment Interest — Faulty Waiver Argument: Defendant argued that plaintiff's waiver of payments availed defendant of a defense to interest on the difference between the contract amount due and the amount actually paid. However, the Supreme Court discounted the waiver argument and noted that defendant did not pay the whole principal; therefore, interest was proper under 27-1-211. Pipe Indus. Ins. Fund Trust v. Consol. Pipe Trades Trust, 233 M 162, 760 P2d 711, 45 St. Rep. 1392 (1988).

Mode of Tender: Ordinarily a check is not a tender, but it may be as effective as a tender of currency if there is no timely objection to the form of tender, or if objection is waived. Schultz v. Campbell, 147 M 439, 413 P2d 879 (1966).

Contract for Purchase of Ranch: A ranch was sold on an installment plan with the contract providing for a downpayment, 10 annual payments at 5% interest, and possession on April 1, 1954. The sellers retained possession of the ranch and operated it until April 1960. The purchaser did not tender the various amounts due except as to the "binder" payment, in effect borrowing the deferred payments at 5%. Since the purchaser received a reasonable rental value for the property, he was required to stand a reduction of the amount of interest due under the contract on all payments over the downpayment of 29% for the time they were due. Hughes v. Melby, 139 M 308, 362 P2d 1014 (1961).

Effect of Dispute as to Consideration: Where there was a bona fide dispute between the makers and payees of a renewal note as to whether there was a partial failure of consideration, an offer to pay an amount not including the disputed item did not bar the payees' right to hold mortgage security. Jensen v. Franklin, 135 M 341, 340 P2d 832 (1959).

Satisfaction of Debt: It is payment, not tender, that is required to discharge or satisfy the debt. Mahoney v. Lester, 118 M 551, 168 P2d 339 (1946).

Right of Redemption: Where one entitled to redeem from execution sale fully complies with the statutory requirements, such compliance results in a completed redemption and a Sheriff's deed to the property issued thereafter to purchaser is void since redemption operated to transfer to redemptioner all right, title, and interest acquired by purchaser. Leonard v. Western, 74 M 513, 241 P 523 (1925).

Release of Lien: Since tender has same effect upon all incidents of obligation as actual payment, if debt is secured by lien upon property or by sureties, tender operates as release of lien or sureties, the creditor being left to his personal claim against debtor. Hamilton v. Hamilton, 51 M 509, 154 P 717 (1916).

28-1-1203. Offer of partial performance ineffective.

Case Notes

What Constitutes Valid Tender: In order to constitute a valid tender, the party making the tender must offer a specific amount that covers all that the other party is entitled to, including interest, costs, and attorney fees. Audit Serv., Inc. v. Frontier-West, Inc., 252 M 142, 827 P2d 1242, 49 St. Rep. 186 (1992), distinguishing Lehrkind v. McDonnell, 51 M 343, 153 P 1012 (1915).

28-1-1204. Who must make offer of performance.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

28-1-1205. To whom offer must be made.

Case Notes

When Payment Does Not Constitute Performance: Performance of a contract is the doing of the things promised to be done. While the obligation may be for the delivery of money only, in which event performance is called "payment", if the contract calls for the doing of various things, payment alone would not constitute performance. Hardenburgh v. Hardenburgh, 115 M 469, 146 P2d 151 (1944).

28-1-1206. Where offer may be made.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Option Agreement — "Indefinite" Terms: The defendant appealed from a judgment granting specific performance of an option agreement to the plaintiff and ordering the property involved conveyed to the plaintiff. The defendant contended that the terms of the option agreement were so indefinite that specific performance could not be granted as a remedy. When the contract is silent, the place of payment is wherever the seller can be found. The option agreement here provided for the manner and the amount of payment. Although the interest to be conveyed was not mentioned, 70-20-301 provides that when the contract or terms of the grant are silent, a fee simple is presumed to be intended to pass. The Supreme Court concluded that the defendant surely did not intend that any less interest should pass and if he so intended, he did not prove it. Specific performance was affirmed. Van Atta v. Schillinger, 191 M 472, 625 P2d 73, 38 St. Rep. 426 (1981).

When Payment Does Not Constitute Performance: Performance of a contract is the doing of the things promised to be done. While the obligation may be for the delivery of money only, in which event performance is called "payment", if the contract calls for the doing of various things, payment alone would not constitute performance. Hardenburgh v. Hardenburgh, 115 M 469, 146 P2d 151 (1944).

Alternative or Unstated Conditions: Where the place of performance of a contract is in the alternative, ordinarily the promisor may elect what act he will perform, the obligation being discharged by the performance of either of the enumerated acts; if one contracts to do one of two things by a given date and allows the day to lapse without performing either, his right of election is lost; if a given date is not stated, the expiration of a reasonable time has the same effect. Thomas v. Cloyd, 110 M 343, 100 P2d 938 (1940).

28-1-1208. Offer of late performance with compensation.

Case Notes

Sale of Sheep: Where time was not of the essence of contract for sale of sheep, buyers could not claim violation of contract or rescind for nondelivery on the day specified, without giving seller an opportunity to tender performance, with compensation for delay. Seller was obliged, within a reasonable time, to tender performance coupled with an offer to compensate for delay. Curtis v. Parham, 49 M 140, 140 P 511 (1914).

Sale of Real Property: Time was held not to be of the essence of an oral contract to sell realty. Stevens v. Trafton, 36 M 520, 93 P 810 (1908).

28-1-1211. When offer may be conditional.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Tender of Payment of Attorney Fees Conditioned on Release of Files Upheld — Right of Patent Assignee to Files Upheld — Construction of Agreement as Assignment and Not License of Patent: Millhollin invented a device to align conveyor belts, which he called a "belt trapper". Millhollin also entered into an agreement with The Conveyor Company (TCC), in which Millhollin gave TCC the exclusive right to make, use, and sell the belt trapper in the United States and foreign countries and in which, in return, TCC agreed to pay Millhollin royalties and other amounts. After deciding that the fees charged by Conover, Millhollin's lawyer, for certain work in connection with the patents were too high, TCC tendered Conover the balance of his fees, conditioned upon Conover turning over his files in the matter to TCC. Millhollin then sent TCC a notice of its default on the contract. After no action was taken by TCC to cure the default, Millhollin declared the agreement terminated and filed a declaratory judgment action. The District Court held that TCC had the right to tender payment conditioned upon receipt of the files. Citing Advance-Rumely Thresher Co., Inc. v. Hess, 85 M 293, 279 P 236 (1929), and this section, the Supreme Court held that a tender of payment may be conditional as long as the condition is one that the tenderer has a right to insist upon. The Supreme Court then analyzed the relationship between TCC and Millhollin as set forth in the written agreement between them and found that the agreement transferred by assignment all of Millhollin's rights in the belt trapper to TCC. Consequently, the Supreme Court held that the files in the hands of Conover were property belonging to TCC and that TCC could therefore withhold payment to Conover conditioned upon release of those files without breaching its agreement with Millhollin. Millhollin v. The Conveyor Co., 1998 MT 41, 287 M 377, 954 P2d 1163, 55 St. Rep. 136 (1998).

Sale of Livestock: An offer to perform by obligee must be unconditional and made in good faith, coupled with the ability to perform; hence where the seller of sheep, sued for damages for failure to make delivery, offered to deliver the animals provided a certain person could select them, the offer was conditional and of no avail to him as a defense. Hanlon v. Manger, 85 M 31, 277 P 433 (1929).

Debtor Not Excused From Paying Delay Money: Lessee of land for oil and gas exploration under a contract which, inter alia, provided that money to be paid by him should be paid to lessor or deposited in bank for his credit was not excused from making payment of delay money by refusal of lessor to execute an indemnity bond assuring proper apportionment of the money among grantees of portions of the lands sold after execution of lease, the transferees having taken subject to its provisions. Lessee, by making payment as provided, would have been released from all claims by the transferees and was therefore in no position to insist upon acceptance of the condition prior to making payment. Thomas v. Standard Dev. Co., 70 M 156, 224 P 870 (1924).

28-1-1212. Objections to mode of offer — waiver.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

No Implied Waiver Contract Provision Subject to Waiver or Modification: In an action involving several complex business transactions, the District Court allowed the plaintiffs to present evidence regarding contract formation and waiver to the jury. On appeal, the defendant bank argued that the no waiver provision of the contract applied. The Supreme Court disagreed, holding that antiwaiver clauses are like any other clause in a contract, subject to waiver or modification by performance. Masters Group Int'l, Inc. v. Comerica Bank, 2015 MT 192, 380 Mont. 1, 352 P.3d 1101.

Blank Security Agreement Signed by Borrower and Filled Out by Bank: Borrower signed a blank security agreement that bank then filled out and mailed to her. The record shows that she had the agreement in her possession in December 1985; thus, she had the means to discover the fraud that she alleged bank committed in setting the agreement's terms. Because she did not file a claim until December 1988, her claim was barred by the 2-year statute of limitations. Richland Nat'l Bank & Trust v. Swenson, 249 M 410, 816 P2d 1045, 48 St. Rep. 730 (1991).

Acts Constituting Waiver: Party who was obligated to sell shares of stock under repurchase agreement waived objections to tender by failing to object to terms of tender, conduct evidencing his willingness to sell and requesting a change in payment terms. State ex rel. Howeth v. D. A. Davidson & Co., 163 M 355, 517 P2d 722 (1973), overruled, with regard to elements of collateral estoppel, in Dagel v. Great Falls, 250 M 224, 819 P2d 186, 48 St. Rep. 919 (1991).

28-1-1221. Title to thing offered.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

28-1-1224. Custody of thing other than money.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

28-1-1225. Deposit of money offered in payment.

Case Notes

Defendant Not Allowed to Characterize Damages: Shilhaneks were injured in a vehicle accident, and defendants were ordered to pay more than $3 million in damages, including punitive damages. Defendants requested that the $750,000 tendered to Shilhaneks to date be allocated toward payment of the punitive award and that Shilhaneks be required to file a corresponding satisfaction of judgment with respect to the punitive damages award, in essence asserting that a defendant has the power to specifically designate payment toward a particular award. Defendants cited 25-9-311 for the rule that a satisfaction of judgment must be provided by the party in whose favor judgment is entered and contended that under 28-1-1106 and this section, the power lies with the debtor, not the creditor, when it comes to designating to which particular obligation a payment should be credited. The District Court denied the request, noting that Title 28 applies only to contractual obligations and that Title 25 governs obligations arising from judgments. The District Court did not abuse its discretion, given defendants' failure to provide a legal basis that would allow them to dictate how damages owed are characterized, the fact that defendants owed more than double the available insurance coverage and were obligated to pay the policy limits to satisfy the verdict, and that allocating 22% of the available insurance proceeds to the punitive damage award would have harsh tax consequences on Shilhaneks. Shilhanek v. D-2 Trucking, Inc., 2000 MT 16, 298 M 101, 994 P2d 1105, 57 St. Rep. 89 (2000).

Substantial Compliance: Judgment debtor's deposit in a savings account in judgment creditor's name of amount of trial court's recomputed award extinguished its obligation so that interest did not continue to run even though deposit did not include interest already accrued and original, higher award was reinstated on appeal. Resner v. N. Pac. Ry., 161 M 177, 505 P2d 86 (1973), overruled on other grounds in Woods v. Burlington N. Ry., 2004 MT 384, 325 M 106, 104 P3d 1045 (2004).

Lease Option Renewal — Tender to Lessor's Daughter Ineffective: Tender of check to lessor's daughter-in-law at lessor's residence did not renew lease option since there was no tender to lessor himself and no written offer of payment or deposit of funds was made, notwithstanding that daughter-in-law refused to allow lessee to see lessor because of latter's illness. Keller v. Martin, 153 M 9, 452 P2d 422 (1969).

Method of Payment: Where payment of judgment was tendered and refused, payment should be made under the provisions of this section and not by deposit in court. Galbreath v. Armstrong, 121 M 387, 193 P2d 630 (1948).

Conditional Tender: A tender is not valid when accompanied with conditions which the tenderer has no right to make, and in order for a tender to operate as payment of an obligation it must be for the full amount thereof. Advance-Rumely Thresher Co., Inc. v. Hess, 85 M 293, 279 P 236 (1929).

Tender in Redemption: After a tender in redemption had been made and refused, plaintiff was not required, in order to keep it good, to deposit the money in court and keep it there. Hamilton v. Hamilton, 51 M 509, 154 P 717 (1916).

Part 13
Prevention of Performance

Part Case Notes

$250,000 Nonrefundable Option Payment — Plaintiffs Allowed to Keep Payment Despite Developers' Inability to Develop Land: The plaintiffs entered into a real estate contract to sell property near Whitefish Lake to the defendants. The contract provided for a $250,000 nonrefundable option due within 30 days, which the defendants paid to the plaintiffs. Subsequently, the defendants were unable to get the approval necessary to develop the property and sought the return of the $250,000, claiming that the contract was null and void. Following a bench trial, the District Court ordered the plaintiffs to return the money to the defendants and the plaintiffs appealed. The Supreme Court reversed, holding that the real estate contract was a binding agreement because it included all the essential material terms, regardless of the later opposition of neighbors to the development of the property. Consequently, the plaintiffs were

entitled to keep the nonrefundable option as provided for in the contract. Hurly v. Lake Cabin Dev., LLC, 2012 MT 77, 364 Mont. 425, 276 P.3d 854.

Unenforceability of Buy-Sell Agreement on Grounds of Impossibility or Impracticality of Performance — Requiring Performance of Contract With Potential for Environmental Degradation Unconstitutional: Cape-France Enterprises (Cape-France) entered a buy-sell agreement with Peed (now deceased) and Moore to purchase some property near Bozeman for a subdivision. Before the subdivision could be completed, water needed to be procured for the site. According to the agreement, as buyers, Peed and Moore were responsible to bring water to the property, but because city water was not available, a well needed to be drilled. However, the presence of a pollution plume was discovered near the land. After the subdivision process was commenced, the Department of Environmental Quality notified Cape-France that: (1) the plume may have advanced under the property; (2) a subdivision would not be approved unless a well was drilled and tested; (3) a well could be drilled, but if testing showed pollution in the water, treatment would be extensive; and (4) if drilling or pumping of the water caused expansion of the pollution, then Cape-France, as owner of the property, would be held liable for cleanup costs. On cross-motions for summary judgment, the District Court held that the buy-sell agreement could be rescinded on the basis of mutual mistake of fact and impossibility or impracticality of performance and that specific performance would not be granted. The Supreme Court affirmed. A court may determine that an act is impossible in legal contemplation when it is not practicable, when the act can be done only at an excessive, unreasonable, and unbargained-for cost. The doctrine of impossibility or impracticability is applied when, aside from the object of a contract being unlawful, the public policy underlying the strict performance of the contract is outweighed by the senselessness of requiring performance. The doctrine is not limited to cases of literal impossibility but may also be applied in cases that present a potential for substantial and unbargained-for damages. In this case, requiring Cape-France to go forward with the performance of the contract when there was a very real possibility of substantial environmental degradation and resultant financial liability for cleanup was not in the public interest or in the interests of the contracting parties and was not in accord with the guarantee of a clean and healthful environment in Art. II, sec. 3, Mont. Const., or the mandate to maintain and improve a clean and healthful environment for present and future generations in Art. IX, sec. 1, Mont. Const. Thus, rescission of the contract was proper. Cape-France Enterprises v. Estate of Peed, 2001 MT 139, 305 M 513, 29 P3d 1011 (2001). See also Smith v. Zepp, 173 M 358, 567 P2d 923 (1977), and Mont. Envtl. Information Center v. Dept. of Environmental Quality, 1999 MT 248, 296 M 207, 988 P2d 1236 (1999).

What Constitutes Excuse of Performance: On appeal in a breach of contract action, the seller argued that the evidence showed he intended to deliver the calves to the buyer by the extended delivery date of December 15 but was excused from performance because of bad weather. The trial court, however, chose to believe that the seller did not so intend, which belief was supported by the facts. The findings were not clearly erroneous. Therefore, the trial court was upheld. Miller v. Titeca, 192 M 357, 628 P2d 670, 38 St. Rep. 853 (1981).

What Constitutes Excuse of Performance by Reason of Rejection: On appeal in a breach of contract action, the seller argued that the buyer had wrongfully rejected delivery after January 1. (The contract called for delivery in mid-November, but an extended delivery date of December 15 had been discussed.) The rejection allegedly made performance impossible due to the buyer's hindrance. The trial court found that the seller had never delivered any calves and concluded that the failure of the seller to make even partial performance amounted to a complete breach of the contract. The court's finding was supported by the evidence that the seller failed to tender delivery after January 1; that all he did was state on several occasions that he would be unable to deliver until January 1; and that the buyer always had demanded delivery by the (earlier) agreed date. After January 1, the seller took the calves to Billings and sold them at a price higher than the contract price without offering them to the buyer. Accordingly, the trial court's findings were held not clearly erroneous. Miller v. Titeca, 192 M 357, 628 P2d 670, 38 St. Rep. 853 (1981).

Impossibility of Performance of Contract: A joint venture was formed, the contract contemplating the feeding of cattle by one party until 80% graded "choice", followed by sale and splitting of the proceeds with the supplier of the cattle, who was the second party. A drop in cattle prices which caused the feeder to lose his financing was not a case of commercial impossibility for two reasons. First, in order for commercial impossibility to excuse performance of a contract, the parties thereto must have had no reason to foresee the impossibility at the time they contracted prior to the breach. On the contrary, a contract against the feeder for damages was upheld. Fluctuation in cattle prices is foreseeable. Second, in order for commercial impossibility to excuse performance, the contractual duties must be impossible for anyone to perform. Subjective (personal) impossibility does not inhere to the nature of the act to be performed and does not excuse nonperformance. A loss of financing is personal impossibility. Roundup Cattle Feeders v. Horpestad, 184 M 480, 603 P2d 1044 (1979), distinguishing Murphy v. Redland, 178 M 296, 583 P2d 1049 (1978).

28-1-1301. When delay or failure to perform or offer to perform excused.

Case Notes

No Delay Attributable to Performance of Obligation — Interest Owing From Date of Mistaken Mortgage Payment: The Ophuses sold their farm and ranch to the Fritzes pursuant to a contract for deed, which included annual mortgage payments payable by the Fritzes to a federal land bank. After the Fritzes defaulted, the parties entered another contract for deed wherein the Ophuses agreed to sell the same property back to the Fritzes at a reduced price. The second contract contained provisions for dividing any profits that the Fritzes received from their sale of the property, but a dispute arose concerning the profits after the Fritzes sold the property to another party. In the course of discovery, it was found that pursuant to the new contract, the Fritzes had made a payment to the land bank that should have been paid by the Ophuses. The District Court held that the Ophuses owed the payment amount to the Fritzes, plus 7% interest from the date on which the payment was made. On appeal, the Ophuses did not dispute their obligation to repay the Fritzes, but did contest the interest calculation. The Supreme Court found that under this section, the Ophuses could not be excused from their interest obligation unless the Fritzes caused the Ophuses to delay repaying, which was not the case because the Fritzes were not even aware that they had mistakenly made the payment until 8 years later. The District Court's calculation of the interest was affirmed. Ophus v. Fritz, 2000 MT 251, 301 M 447, 11 P3d 1192, 57 St. Rep. 1037 (2000).

Inability to Pay Insufficient Defense to Obligations Due on Promissory Note: Plaintiffs claimed that a bank's exercise of a setoff made it impossible to pay off promissory notes. The Supreme Court affirmed a finding that inability to pay is the common problem of any maker of a promissory note who defaults and that inability is not in itself a sufficient defense to obligations due on the note. Bottrell v. Am. Bank, 237 M 1, 773 P2d 694, 46 St. Rep. 561 (1989).

Contract for Purchase of Ranch: A contract for the sale of a ranch on an installment plan provided for a down payment and then 10 annual payments at 5% interest, possession April 1, 1954. Sellers remained in possession and operated the ranch until April 1960. The purchaser did not tender the various amounts due except as to the "binder" payment. He was in effect borrowing the deferred payments at 5% interest. Having received the reasonable rental value of the property the purchaser must stand a reduction of the amount of interest due under the contract on all payments over the down payment of 29% for the time they were due. Hughes v. Melby, 139 M 308, 362 P2d 1014 (1961).

Nonperformance Excused — Failure to Pay Caused by Seller: Notwithstanding provision in contract that seller was to be wholly discharged of liability under warranty in case buyer failed to pay for goods ordered, if the failure to pay was caused by action of seller, as where price was to be paid out of advances on government contract and government contract was lost because of defective condition of goods, nonperformance was excused. Pioneer Eng'r Works, Inc. v. McConnell, 123 M 171, 212 P2d 641 (1949).

Applicable in Action for Negligence — Act of God: An act of God such as to excuse performance under this section is an unusual or unprecedented happening or event arising within the realm of natural law, but beyond and outside of the observations and experience of the average person. Wibaux Realty Co. v. N. Pac. Ry., 101 M 126, 54 P2d 1175 (1935).

28-1-1302. Effect when performance prevented by creditor.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Demand for Performance of Term Not Contained in Contract — Statement That Party Will Not Perform Unless Demand Met — Anticipatory Breach of Contract: "A party acts at his peril if, insisting on what he mistakenly believes to be his rights, he refuses to perform his duty." Therefore, a demand for performance of a term not contained in the parties' contract, accompanied by an unequivocal statement that the demanding party will not perform unless the additional term is met, constitutes an anticipatory breach of the contract, excusing performance by the other party. In determining whether an anticipatory breach was committed, the concern is whether the promisor communicated an unequivocal indication of an intent not to perform rather than the promisor's uncommunicated subjective intent in repudiating its contractual obligations. A promisee need not jeopardize its own interests by speculating about the promisor's clear refusal to perform or by waiting until the time set for performance to ascertain whether the promisor's unequivocal repudiation was serious. Chamberlin v. Puckett Constr., 277 M 198, 921 P2d 1237, 53 St. Rep. 593 (1996), following United Calif. Bank v. Prudential Ins. Co, 681 P2d 390 (Ariz. Ct. App. 1983), and followed in Eschenbacher v. Anderson, 2001 MT 206, 306 M 321, 34 P3d 87 (2001). See also Boyne USA, Inc. v. Spanish Peaks Dev., LLC, 2013 MT 1, 368 Mont. 143, 292 P.3d 432. See also Comment d, Restatement (Second) of Contracts 250 (1981).

Inability to Pay Insufficient Defense to Obligations Due on Promissory Note: Plaintiffs claimed that a bank's exercise of a setoff made it impossible to pay off promissory notes. The Supreme Court affirmed a finding that inability to pay is the common problem of any maker of a promissory note who defaults and that inability is not in itself a sufficient defense to obligations due on the note. Bottrell v. Am. Bank, 237 M 1, 773 P2d 694, 46 St. Rep. 561 (1989).

Case of First Impression — Breach of Contract by Anticipatory Repudiation: Combining two maxims of jurisprudence, "The law neither does nor requires idle acts" and "For every wrong there is a remedy", court found no reason in policy or in law for denying an immediate action for damages based on breach of contract by anticipatory repudiation. However, court held for defendant as language asserted by plaintiff as a repudiation was subject to different interpretations and since breach of contract by anticipatory repudiation works harsh results; for its application, there must be a positive unequivocal statement to the promisee indicating that the promisor will not or cannot substantially perform his contractual duties before his time for performance has arrived. STC, Inc. v. Billings, 168 M 364, 543 P2d 374 (1975).

Prevention Caused by Changes in Building Plans: A building contractor agreed to complete the remodeling of a residence within a given time and not to receive any payment until completion. During such time the owner made frequent changes in plans occasioning considerable delay and necessitating additional work. The owner thereby prevented the performance of the condition precedent upon which his liability under the contract depended, but he could not avail himself of its nonperformance which he himself had occasioned. Smith v. Gunniss, 115 M 362, 144 P2d 186 (1943).

Rejection of Offer of Performance: An unconditional offer in good faith to perform by the party on whom the obligation rests, coupled with the ability to perform, is, if rejected by the other party, equivalent to full performance and extinguishes such obligation; the offerer is then entitled to all the benefits he would have been entitled to if performance had been complete on both sides. Lehrkind v. McDonnell, 51 M 343, 153 P 1012 (1915).

28-1-1303. Effect when performance prevented by other causes.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

No Tortious Interference With Business When Sublease Terminated Prior to Alleged Interference: Lessee Anderson filed a counterclaim against lessor Grenfell for tortiously interfering with Anderson's sublease of a portion of the leased property. However, the District Court correctly found that Anderson terminated the sublease prior to Grenfell's actions, so Grenfell could not be found to have interfered with a sublease that was no longer in effect. Grenfell v. Anderson, 2002 MT 225, 311 M 385, 56 P3d 326 (2002).

Mortgage Against Party's Interest in Property Granted Pursuant to Dissolution — No Tortious Interference With Business, Prima Facie Tort, or Intentional Infliction of Emotional Distress: When George and Joyce were divorced, the District Court granted George exclusive possession of the ranch until it could be sold and the proceeds divided between the parties. During the course of the dissolution proceedings, Joyce took out several loans for living expenses. After the dissolution, Joyce consolidated the $150,000 in loans, and the bank executed a mortgage on Joyce's interest in the ranch to secure the loan. When George found out about the mortgage and security interest, he became distraught because he believed that he would not be able to obtain loans on the property to enable him to conduct ranch obligations and meet his operations. George subsequently filed suit against Joyce, the bank, and the bank president, who was Joyce's son-in-law, alleging tortious interference with business relationships, prima facie tort, and intentional infliction of emotional distress. The District Court granted the defendants' motion for summary judgment, and George appealed. The Supreme Court affirmed. Applying Farrington v. Buttrey Food & Drug Stores Co., 272 M 140, 900 P2d 277 (1995), the court concluded that the acts of Joyce and the bank were legal and that, standing alone, the acts did not give rise to any presumption or inference that the acts were done to harm George. The court also declined to recognize a separate cause of action for prima facie tort under the facts of this case. Applying Sacco v. High Country Independent Press, Inc., 271 M 209, 896 P2d 411 (1995), the court further concluded that because the defendants' acts were legal, no claim for emotional distress could arise from those acts. Absent material facts evidencing malicious intent or damages, summary judgment was proper. Pospisil v. First Nat'l Bank of Lewistown, 2001 MT 286, 307 M 392, 37 37 P3d 704 (2001).

Instruction Necessary — Interference With Contract: An instruction on interference with contract must address the element of unjustifiability or impropriety of the alleged tortious actions and provide that the act is "without right or justifiable cause on the part of the actor". NW. Nat'l Bank of Great Falls v. Weaver-Maxwell, Inc., 224 M 33, 729 P2d 1258, 43 St. Rep. 1995 (1986), distinguished in Weinberg v. Farmers St. Bank of Worden, 231 M 10, 752 P2d 719, 45 St. Rep. 391 (1988).

Breach of Contract — Interference With Business: Defendant breached a contract to sell business property to plaintiff and not to compete and subsequently interfered with the conduct of plaintiff's business. Defendant is liable not only for breach of the contract between himself and plaintiff but also for the tort of intentional interference with a contractual or business relationship between plaintiff and his potential customers. Bolz v. Myers, 200 M 286, 651 P2d 606, 39 St. Rep. 1747 (1982), followed in Farrington v. Buttrey Food & Drug Stores Co., 272 M 140, 900 P2d 277, 52 St. Rep. 667 (1995).

Interference With Contractual Relationship: In order to establish a prima facie case of interference with contractual or business relations, it must be shown that: (1) the acts were intentional and willful; (2) the acts were calculated to cause damage to the plaintiff in his business; (3) the acts were done with the unlawful purpose of causing damage or loss, without right or justifiable cause on the part of the actor; and (4) actual damages and loss resulted. Bolz v. Myers, 200 M 286, 651 P2d 606, 39 St. Rep. 1747 (1982), followed in Randolf V. Peterson, Inc. v. J.R. Simplot Co., 239 M 1, 778 P2d 879, 46 St. Rep. 1463 (1989), Grenfell v. Anderson, 2002 MT 225, 311 M 385, 56 P3d 326 (2002), and Emmerson v. Walker, 2010 MT 167, 357 Mont. 166, 236 P.3d 598.

Prevention of Performance by Stranger: An action against a stranger to a contract for damages caused by his unlawful interference with its performance is one for a tort, and not one upon the contract, and therefore plaintiff was not required to plead in his complaint that he had performed all conditions precedent to be performed by him under it, to entitle him to recover. Burden v. Elling St. Bank, 76 M 24, 245 P 958 (1926), followed in Bolz v. Meyers, 200 M 286, 651 P2d 606, 39 St. Rep. 1747 (1982).

28-1-1304. Effect of refusal to accept performance before offer.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Demand for Performance of Term Not Contained in Contract — Statement That Party Will Not Perform Unless Demand Met — Anticipatory Breach of Contract: "A party acts at his peril if, insisting on what he mistakenly believes to be his rights, he refuses to perform his duty." Therefore, a demand for performance of a term not contained in the parties' contract, accompanied by an unequivocal statement that the demanding party will not perform unless the additional term is met, constitutes an anticipatory breach of the contract, excusing performance by the other party. In determining whether an anticipatory breach was committed, the concern is whether the promisor communicated an unequivocal indication of an intent not to perform rather than the promisor's uncommunicated subjective intent in repudiating its contractual obligations. A promisee need not jeopardize its own interests by speculating about the promisor's clear refusal to perform or by waiting until the time set for performance to ascertain whether the promisor's unequivocal repudiation was serious. Chamberlin v. Puckett Constr., 277 M 198, 921 P2d 1237, 53 St. Rep. 593 (1996), following United Calif. Bank v. Prudential Ins. Co, 681 P2d 390 (Ariz. Ct. App. 1983), and followed in Eschenbacher v. Anderson, 2001 MT 206, 306 M 321, 34 P3d 87 (2001). See also Boyne USA, Inc. v. Spanish Peaks Dev., LLC, 2013 MT 1, 368 Mont. 143, 292 P.3d 432. See also Comment d, Restatement (Second) of Contracts 250 (1981).

Case of First Impression — Breach of Contract by Anticipatory Repudiation: Combining two maxims of jurisprudence, "The law neither does nor requires idle acts" and "For every wrong there is a remedy", court found no reason in policy or in law for denying an immediate action for damages based on breach of contract by anticipatory repudiation. However, court held for defendant as language asserted by plaintiff as a repudiation was subject to different interpretations and since breach of contract by anticipatory repudiation works harsh results, for its application, there must be a positive unequivocal statement to the promisee indicating that the promisor will not or cannot substantially perform his contractual duties before his time for performance has arrived. STC, Inc. v. Billings, 168 M 364, 543 P2d 374 (1975).

Anticipatory Breach: Where the plaintiff in an action for breach of contract of sale communicated to the defendant in advance his refusal to be longer bound thereby, the defendant was excused from further performance on his part, and was justified in treating the contract as repudiated, and was under no obligation to give notice of his intention to consider the agreement at an end and resell. McCaull-Dinsmore Co. v. Jackson, 57 M 555, 189 P 771 (1920).

Part 14
Accord and Satisfaction

Part Law Review Articles

A Primer on Accord and Satisfaction, Burnham, 47 Mont. L. Rev. 1 (1986).

28-1-1401. Accord — definition and effect.

Case Notes

Amendment of Judgment Proper Based on Impermissible Double Recovery Yet Jury's Determination of Breach Supported by Substantial Evidence — Accord and Satisfaction Not Argued and Not Supported by Facts: The plaintiff filed a motion for a new trial or amendment of judgment, arguing that there was insufficient evidence to justify the jury's damages award of $25,000 for the plaintiff's breach of the implied covenant of good faith and fair dealing. The trial court found that this argument had merit because the award would be an impermissible double recovery for the defendant and, accordingly, granted the plaintiff's request that the award be vacated. However, the plaintiff never asserted that there was not substantial evidence supporting the jury's determination that the plaintiff breached the second agreement, nor did the plaintiff argue waiver or accord and satisfaction as defenses. Thus, though the parties disputed its terms, there was sufficient evidence for the jury to find that all the elements of a contract existed, that the plaintiff breached a second agreement, and that the defendant was damaged. Moreover, the Supreme Court determined that the evidence was substantive enough for the jury to have found in favor of the defendant and to have rejected the waiver and accord and satisfaction arguments the plaintiff presented on appeal. Ryffel Family Partnership v. Alpine Country Constr., Inc., 2016 MT 350, 386 Mont. 165, 386 P.3d 971.

Absence of Evidence of Rescission, Release, Waiver, or Accord and Satisfaction of Contract — Reversal Warranted: Plaintiffs owned shares in defendant's corporation and sought to sell the shares back to the corporation. The corporation sent a letter offering to purchase the shares for $64,933.60, and plaintiffs were instructed that to accept the offer, they were to sign the back of the stock certificate and mail it to the corporation. Plaintiffs did so, but included with the certificate a letter stating that by accepting the offer, plaintiffs reserved their rights under federal and state law. The corporation found the language unacceptable and declined to purchase the shares, instead returning the certificate to plaintiffs. Concerned about possessing a signed stock certificate, plaintiffs ultimately visited the corporation and surrendered the endorsed certificate in exchange for a new one. Plaintiffs then brought a breach of contract suit claiming $64,933.60 in damages, asserting that the corporation had breached its offer to repurchase the stock. The corporation denied that a contract offer existed, arguing that plaintiffs' reply was not an acceptance but rather a counteroffer, and asserted that even if a contract did exist, plaintiffs had waived their rights under it by forfeiting the endorsed certificate in favor of a new one and by failing to immediately assert their rights under the contract. A jury found that the corporation had breached its contract, causing damages in the amount of $64,933.60, but then entered a verdict for the corporation on grounds that the corporation had proved at least one of its affirmative defenses of rescission, release, waiver, or accord and satisfaction. On appeal, the Supreme Court noted that only in rare cases should a jury verdict be set aside but reversed the verdict nevertheless on grounds that, even drawing all legitimate inferences in favor of the corporation, there was a complete absence of probative evidence supporting any of the corporation's affirmative defenses. The case was remanded for entry of judgment of $64,933.60 in favor of plaintiffs. Benson v. Diverse Computer Corp., 2004 MT 114, 321 M 140, 89 P3d 981 (2004), followed in Harland v. Anderson Ranch Co., 2004 MT 132, 321 M 338, 92 P3d 1160 (2004).

Insurer Required to Pay Undisputed Medical Coverage Without Settlement Agreement When Liability Reasonably Clear — No Bad Faith Claim for Pre-Watters Conditioned Settlement Offer: Defendant insurer offered to pay plaintiffs the policy limit of $1 million in exchange for a full release of claims against the insureds. Plaintiffs refused to provide a release, the case went to trial, and plaintiffs were awarded more than $3 million. Plaintiffs then counterclaimed against the insurer, claiming that refusal to pay the undisputed medical claims without a release violated 33-18-201(6) and (13). The Supreme Court noted that the purpose of 33-18-201 is to ensure prompt payment of damages for which an insurer is clearly obligated. Thus, pursuant to Ridley v. Guar. Nat'l Ins. Co., 286 M 325, 951 P2d 987 (1997), and Watters v. Guar. Nat'l Ins. Co., 2000 MT 150, 300 M 91, 3 P3d 626 (2000), the insurer had a duty to pay plaintiffs' undisputed medical expenses up to the limits of its coverage and without the benefit of a settlement agreement. Nevertheless, because the insurer made its settlement offer in 1998, more than 2 years prior to the Watters decision, the insurer had an arguably reasonable basis under 33-18-242 for asserting that it was entitled to condition payment of policy limits on plaintiffs' provision of a release of claims, so the insurer was not liable for acting in bad faith in violation of 33-18-201. Shilhanek v. D-2 Trucking, Inc., 2003 MT 122, 315 M 519, 70 P3d 721 (2003), overruling Juedeman v. Nat'l Farmers Union Property & Cas. Co., 253 M 278, 833 P2d 191 (1992), and overruling Watters to the extent that Watters implies that an insurer's obligation under Ridley is limited to the minimum coverage required by the Motor Vehicle Safety-Responsibility Act. See also High Country Paving, Inc. v. United Fire & Cas. Co., 2019 MT 297, 398 Mont. 191, 454 P.3d 1210.

Validity and Enforceability of Memorandum of Understanding — Findings of Facts and Conclusions of Law Not Required: The District Court ruled that the parties had entered into a valid and enforceable memorandum of understanding (MOU) regarding the parties' obligations applicable to an agricultural lease. The defendants argued that the MOU was simply an agreement to agree, that only a formal settlement agreement would bind the parties, and that the District Court erred in finding the MOU to be binding without setting out its findings of fact and conclusions of law. The plaintiff maintained that the MOU was an unconditional settlement agreement, that a more formal settlement document was not necessary to finalize or carry out the MOU, and that the court had no duty to set out its findings and conclusions. The Supreme Court found no error in the District Court's ruling and affirmed. All interested parties were present at the settlement conference and participated in negotiations, which ended with all the parties signing the MOU, memorializing the agreement among the signatories. Clearly there was a meeting of the minds during negotiations, and all the parties anticipated being bound by the MOU. The MOU was not conditioned upon the execution of a formal settlement agreement, so one was not necessary. The Supreme Court has recognized the validity of similar MOUs in Hetherington v. Ford Motor Co., 257 M 395, 849 P2d 1039 (1993), and Marta Corp. v. Thoft, 271 M 109, 894 P2d 333 (1995), and concluded that the agreement memorialized in the MOU here was a valid unconditional resolution of the parties' claims that effectively released any claims of the signatories. Further, under former Rule 52(a), M.R.Civ.P. (now superseded), findings and conclusions are unnecessary on decisions of motions except for judgments at trial, which did not apply in this case. The District Court did not abuse its discretion in denying a defendant's motion to file an amended answer and counterclaim addressed to the original complaint, because those claims were also resolved by the MOU. Bar OK Ranch, Co. v. Ehlert, 2002 MT 12, 308 M 140, 40 P3d 378 (2002).

Unfair Trade Practice to Require Full and Final Release of Liability Before Claim Paid Within Policy Limits — "Settlement" Distinguished From "Release": Guaranty National Insurance Co. (Guaranty) provided a minimum motor vehicle liability policy for Moore, who was clearly liable for injuring the Watterses' in a car accident. Guaranty offered to settle the Watterses' claim to the extent of the policy coverage, but not without an absolute release of all liability. The Watterses declined the offer, eventually bringing an unfair trade action against Guaranty for failing to promptly pay damages for which Moore was liable. Guaranty argued that the full release from liability was necessary to effectuate a settlement, citing Thompson v. St. Farm Mut. Auto. Ins. Co., 161 M 207, 505 P2d 423 (1973), and Juedeman v. Nat'l Farmers Union Property & Cas. Co., 253 M 278, 833 P2d 191 (1992), and contended that because no settlement was proffered from the Watterses, Guaranty could not, as a matter of law, have violated 33-18-201. The Supreme Court instead applied Ridley v. Guar. Nat'l Ins. Co., 286 M 325, 951 P2d 987 (1997). The court clarified the relevant terms, noting that in accord with the general governing principles of contract law from which the law of settlements is derived, in the context of the Unfair Trade Practices Act, a settlement is synonymous with an enforceable bilateral contract that discharges a future or existing obligation, while a release, as a matter of law, is nothing more than an accord and satisfaction or one of several ways in which an obligation may contractually be discharged or settled for less than or for something different than from what is owed. The court concluded that a settlement between Guaranty and the Watterses was legally possible without the Watterses executing a full and final release of all liability, as evidenced by Guaranty's settlement of the Watterses' property damage claims within the limits of Moore's policy without a release. Thus, when liability resulting from an automobile accident is reasonably clear and a third-party claimant's damages undisputedly exceed mandatory minimum policy limits pursuant to 61-6-103, it is an unfair trade practice per se under 33-18-201 for an insurer to condition the payment of the owed mandatory minimum policy limits on the third party's agreement to provide a full and final release of all liability in favor of an insured. An insurer who pays mandatory minimum policy limits under these circumstances does not act in bad faith per se against its insured by not obtaining a full and final liability release on the insured's behalf. Unfortunately for the Watterses, under the case law in effect at the time, Guaranty had a reasonable basis under Juedeman upon which to deny payment of policy limits, so Guaranty's cross-motion for summary judgment was granted. Watters v. Guar. Nat'l Ins. Co., 2000 MT 150, 300 M 91, 3 P3d 626, 57 St. Rep. 588 (2000), overruling Thompson v. St. Farm Mut. Auto. Ins. Co., 161 M 207, 505 P2d 423 (1973), and Juedeman v. Nat'l Farmers Union Property & Cas. Co., 253 M 278, 833 P2d 191 (1992). See also High Country Paving, Inc. v. United Fire & Cas. Co., 2019 MT 297, 398 Mont. 191, 454 P.3d 1210.

Accord and Satisfaction Applicable Only Between Parties to Agreement: Berlin entered into agreements with Boedecker and his brother Brooks to purchase interests in certain oil well properties. Later, Brooks and Berlin renegotiated their agreement twice. Still later, Berlin sued Boedecker upon discovery that Boedecker had committed fraud in the transaction. Boedecker argued that the action against him by Berlin should be dismissed on the basis of accord and satisfaction. The Supreme Court held that accord and satisfaction extinguishes only the obligation between the parties to the agreement (Berlin and Brooks) and that it had no effect upon Boedecker's liability to Berlin. Berlin v. Boedecker, 268 M 444, 887 P2d 1180, 51 St. Rep. 569 (1994).

No Accord When Payment Stopped on Check — Evidence of Agreement Properly Excluded: In a dispute over the charges for the care and training of horses, the parties agreed that Watkins would accept $5,000 for his services. The Williamses gave Watkins two checks for $2,500, but they stopped payment on the second check and refused to tender the rest of the money on the basis that one of the horses had been mistreated. The jury returned a verdict in favor of Watkins for $20,191 for services. The Williamses argued that the lower court erred in initially excluding the accord and satisfaction affirmative defense. The Supreme Court ruled that there was no accord because of the Williamses' failure to pay the agreed-upon sum and that the District Court had been correct in excluding testimony concerning the agreement. Watkins v. Williams, 265 M 306, 877 P2d 19, 51 St. Rep. 489 (1994).

Breach of Release Agreement by Heirs — Specific Performance Proper: The heirs of a woman, who died from injuries sustained after being run over by her own automobile, authorized their attorney to accept a settlement agreement that required Ford Motor Company (Ford) and a local body shop to pay a total of $185,000 in exchange for a full and final release of all claims. Four days after authorizing acceptance of the settlement offer, the heirs retained different counsel and filed an action against Ford, claiming that the right to bring a claim was not lost until the agreement was formally executed. Ford subsequently counterclaimed for summary judgment, seeking specific performance based on the settlement agreement. The District Court denied Ford's motion, ruling that there was no "meeting of the minds" on the release provision in the agreement. On appeal, the Supreme Court reversed, holding that the interim agreement was an executory accord and Ford, upon the heirs' breach, had the option of suing for damages or asking for specific performance of the contract. Hetherington v. Ford Motor Co., 257 M 395, 849 P2d 1039, 50 St. Rep. 325 (1993), followed in Marta Corp. v. Thoft, 271 M 109, 894 P2d 333, 52 St. Rep. 374 (1995), and distinguished in Murphy v. The Home Depot, 2012 MT 23, 364 Mont. 27, 270 P.3d 72.

Accord and Satisfaction as Extinction of Debt — Further Claims Barred: Bohnsacks agreed to assign a $20,000 promissory note to Hi-Noon Petroleum, Inc. as payment for a $23,729 debt owed Hi-Noon for gasoline delivered to a third party, Charles, for which Bohnsacks acted as guarantor. Bohnsacks then sought to proceed against Hi-Noon for wrongfully delivering gasoline to Charles despite Charles' failure to pay for loads previously delivered. However, Hi-Noon had agreed to accept less than that to which it was entitled in extinction of Bohnsack's debt. Once Hi-Noon accepted payment, the debt was extinguished by accord and satisfaction, barring Bohnsack's further claims. Bohnsack v. Hi-Noon Petroleum, Inc., 243 M 190, 793 P2d 815, 47 St. Rep. 1125 (1990).

Cashing of Check Evidence of Full Satisfaction of Claim: In settlement of a personal injury claim, plaintiff cashed defendant's check, which action constituted a full satisfaction of the claim. Despite plaintiff's subsequent contention that he did not intend to fully and finally release the claim, the trial court found that the check was tendered to plaintiff under such circumstances that he was bound to know it was offered in full settlement of the claim, resulting in an accord and satisfaction between the parties and a discharge of plaintiff's whole claim. A disputed, unliquidated obligation may be extinguished if the obligated party offers to exchange an amount different from or less than the obligation in full settlement of the obligation and if the party owed the obligation agrees to accept and does accept the amount offered in full settlement of the obligation. Boyer v. Ettelman, 235 M 323, 767 P2d 324, 46 St. Rep. 21 (1989), followed in Eatinger v. Johnson, 269 M 99, 887 P2d 231, 51 St. Rep. 1484 (1994).

No Accord and Satisfaction When Right to Recover Deficiency Reserved: Defendant's conveyance of interest in real property as consideration for an antecedent debt does not constitute accord and satisfaction when defendant agreed that if there was a deficiency after sale of the property, he remained responsible for the deficiency. Hunt v. Hunt, 219 M 118, 710 P2d 1352, 42 St. Rep. 1887 (1985), distinguishing Hale v. Belgrade Co., 75 M 99, 242 P 425 (1925).

Unsatisfied Accord: Where buyer of ranch agreed to take over seller's debt on mortgaged sheep on the property, but agreement and promise of settlement of debt were never completed, there was no satisfaction and seller was still liable for the debt. Goggins v. Bookout, 141 M 449, 378 P2d 212 (1963).

Evidence of Accord: In action against landlord where tenant alleged that he had given verbal notice, accepted by the landlord, of his intention to renew lease and had paid consideration therefor, and landlord alleged that consideration was for subsequent accord and satisfaction which allowed tenant time to remove property from premises, there was ample evidence from which the jury could determine that landlord had breached the accord. Flint v. Mincoff, 137 M 549, 353 P2d 340 (1960).

What Does Not Constitute Accord and Satisfaction: To constitute acceptance by a creditor of a smaller amount than that claimed by him to be due on an accord and satisfaction, there must be a bona fide dispute between the parties with respect to the amount due. If plaintiff accepted weekly pay for an amount less than he claimed to be due, laboring under the impression that eventually his employer would make up the difference as he promised, and continued to work until he learned the promise would not be kept, the jury could not logically find that he was bound to know that his acceptance of the pay constituted an accord and satisfaction. Jensen v. Cloud, 107 M 593, 88 P2d 36 (1939).

Accord and Satisfaction — Suit on Quantum Meruit: Where plaintiff agreed to accept stock in lieu of wages if defendant desired, if stock was not delivered and agreement breached, he is not restricted to remedy of specific performance on breach of the agreement, or to an action for damages for the breach, but may treat agreement as ended and sue upon quantum meruit. Davis v. Sullivan Gold Min. Co., 103 M 452, 62 P2d 1292 (1936).

Obligation Not Extinguished: Under this section and 28-1-1402, an accord does not extinguish the obligation sought to be extinguished until the agreement between the parties is fully executed, i.e., in case of a tort, until the injured party has accepted the consideration for the accord; until then the original obligation remains. Barbarich v. Chicago, Milwaukee, St. Paul & Pac. Ry., 92 M 1, 9 P2d 797 (1932).

Distinction Between "Compromise and Settlement" and "Accord and Satisfaction": Distinctions drawn between "compromise and settlement" and "accord and satisfaction"—terms in many cases used interchangeably—seem to be of little practical importance, the intention of the parties in making the agreement in either instance and the effect given by statute to it being the controlling factors. Barbarich v. Chicago, Milwaukee, St. Paul & Pac. Ry., 92 M 1, 9 P2d 797 (1932).

"Obligation" Defined: An "obligation" within the meaning of this section includes a liability for actionable tortious conduct. Barbarich v. Chicago, Milwaukee, St. Paul & Pac. Ry., 92 M 1, 9 P2d 797 (1932).

Defense of Accord and Satisfaction: Defense of accord and satisfaction must be pleaded, and to constitute acceptance by mortgagee of check for less amount than was actually due from mortgagor on accord, there must have been an agreement on part of mortgagee to accept less in satisfaction in full of the mortgage. Nett v. Stockgrowers' Fin. Corp., 84 M 116, 274 P 497 (1929).

"Accord and Satisfaction" Defined: "Accord and satisfaction" means the substitution of a new agreement in satisfaction of an obligation different from the original rights existing under an antecedent liability, and to be available in defense must be specially pleaded. Nelson v. Young, 70 M 112, 224 P 237 (1924).

28-1-1402. Satisfaction — definition and effect.

Case Notes

Amendment of Judgment Proper Based on Impermissible Double Recovery Yet Jury's Determination of Breach Supported by Substantial Evidence — Accord and Satisfaction Not Argued and Not Supported by Facts: The plaintiff filed a motion for a new trial or amendment of judgment, arguing that there was insufficient evidence to justify the jury's damages award of $25,000 for the plaintiff's breach of the implied covenant of good faith and fair dealing. The trial court found that this argument had merit because the award would be an impermissible double recovery for the defendant and, accordingly, granted the plaintiff's request that the award be vacated. However, the plaintiff never asserted that there was not substantial evidence supporting the jury's determination that the plaintiff breached the second agreement, nor did the plaintiff argue waiver or accord and satisfaction as defenses. Thus, though the parties disputed its terms, there was sufficient evidence for the jury to find that all the elements of a contract existed, that the plaintiff breached a second agreement, and that the defendant was damaged. Moreover, the Supreme Court determined that the evidence was substantive enough for the jury to have found in favor of the defendant and to have rejected the waiver and accord and satisfaction arguments the plaintiff presented on appeal. Ryffel Family Partnership v. Alpine Country Constr., Inc., 2016 MT 350, 386 Mont. 165, 386 P.3d 971.

Absence of Evidence of Rescission, Release, Waiver, or Accord and Satisfaction of Contract — Reversal Warranted: Plaintiffs owned shares in defendant's corporation and sought to sell the shares back to the corporation. The corporation sent a letter offering to purchase the shares for $64,933.60, and plaintiffs were instructed that to accept the offer, they were to sign the back of the stock certificate and mail it to the corporation. Plaintiffs did so, but included with the certificate a letter stating that by accepting the offer, plaintiffs reserved their rights under federal and state law. The corporation found the language unacceptable and declined to purchase the shares, instead returning the certificate to plaintiffs. Concerned about possessing a signed stock certificate, plaintiffs ultimately visited the corporation and surrendered the endorsed certificate in exchange for a new one. Plaintiffs then brought a breach of contract suit claiming $64,933.60 in damages, asserting that the corporation had breached its offer to repurchase the stock. The corporation denied that a contract offer existed, arguing that plaintiffs' reply was not an acceptance but rather a counteroffer, and asserted that even if a contract did exist, plaintiffs had waived their rights under it by forfeiting the endorsed certificate in favor of a new one and by failing to immediately assert their rights under the contract. A jury found that the corporation had breached its contract, causing damages in the amount of $64,933.60, but then entered a verdict for the corporation on grounds that the corporation had proved at least one of its affirmative defenses of rescission, release, waiver, or accord and satisfaction. On appeal, the Supreme Court noted that only in rare cases should a jury verdict be set aside but reversed the verdict nevertheless on grounds that, even drawing all legitimate inferences in favor of the corporation, there was a complete absence of probative evidence supporting any of the corporation's affirmative defenses. The case was remanded for entry of judgment of $64,933.60 in favor of plaintiffs. Benson v. Diverse Computer Corp., 2004 MT 114, 321 M 140, 89 P3d 981 (2004), followed in Harland v. Anderson Ranch Co., 2004 MT 132, 321 M 338, 92 P3d 1160 (2004).

Accord and Satisfaction Applicable Only Between Parties to Agreement: Berlin entered into agreements with Boedecker and his brother Brooks to purchase interests in certain oil well properties. Later, Brooks and Berlin renegotiated their agreement twice. Still later, Berlin sued Boedecker upon discovery that Boedecker had committed fraud in the transaction. Boedecker argued that the action against him by Berlin should be dismissed on the basis of accord and satisfaction. The Supreme Court held that accord and satisfaction extinguishes only the obligation between the parties to the agreement (Berlin and Brooks) and that it had no effect upon Boedecker's liability to Berlin. Berlin v. Boedecker, 268 M 444, 887 P2d 1180, 51 St. Rep. 569 (1994).

No Accord When Payment Stopped on Check — Evidence of Agreement Properly Excluded: In a dispute over the charges for the care and training of horses, the parties agreed that Watkins would accept $5,000 for his services. The Williamses gave Watkins two checks for $2,500, but they stopped payment on the second check and refused to tender the rest of the money on the basis that one of the horses had been mistreated. The jury returned a verdict in favor of Watkins for $20,191 for services. The Williamses argued that the lower court erred in initially excluding the accord and satisfaction affirmative defense. The Supreme Court ruled that there was no accord because of the Williamses' failure to pay the agreed-upon sum and that the District Court had been correct in excluding testimony concerning the agreement. Watkins v. Williams, 265 M 306, 877 P2d 19, 51 St. Rep. 489 (1994).

28-1-1403. When part performance extinguishes obligation.

Case Notes

Signing of Separation Agreements and Acceptance of Payments Precluding Obligation for Further Payments: Several physicians signed separation agreements when terminating employment with a medical clinic. The agreements provided that the physicians expressly accepted payments representing a reduced amount of profits, stock, and partnership interest and that the payments called for by the agreements constituted the full amount payable by the clinic. The physicians later asserted that the provision in the agreement reducing payments was void or unreasonable. The Supreme Court disagreed. Pursuant to 28-1-1403, any obligation of the clinic to pay more was extinguished when the physicians accepted the terms of the separation agreement. Mungas v. Great Falls Clinic, LLP, 2009 MT 426, 354 M 50, 221 P3d 1230 (2009).

Partial Payment Accompanied by Letter Indicating Payment as Full Settlement — Accord and Satisfaction Created: Where the Department of Revenue sought back child support of $14,240 and the father's attorney sent a $1,000 check to the Department along with a letter clearly indicating that the check was offered as full settlement and that negotiation of the check would represent consent to full compromise of the Department's claim, the District Court properly held that the claim was a disputed and unliquidated claim and that acceptance of the check created an accord and satisfaction. St. v. Frank, 226 M 283, 735 P2d 290, 44 St. Rep. 657 (1987).

Endorsement of Check: Where a claim is liquidated, it can be discharged only by payment in full or by acceptance in writing of a lesser amount. Endorsement of a check for purpose of cashing it is not the writing contemplated by this section as evidence of acceptance of a lesser amount for that claimed to be due. Sawyer v. Somers Lumber Co., 86 M 169, 282 P 852 (1929). See also Geissler v. Nelson, 222 M 409, 722 P2d 632, 43 St. Rep. 1372 (1986), and Interstate Prod. Credit Ass'n v. Abbott, 223 M 405, 726 P2d 824, 43 St. Rep. 1829 (1986).

Part 15
Novation

Part Case Notes

Statute of Frauds: Where promise is made to pay antecedent obligation of another upon condition that party receiving it will cancel the obligation, accepting the new promise in substitution therefor, it is an original undertaking or agreement and not a mere promise to answer for debt of another within meaning of Statute of Frauds, and need not be in writing. Tannhauser v. Shea, 88 M 562, 295 P 268 (1930).

What Are Subjects of Novation: Judgments are as much the subjects of novation as simple contract debts. Tannhauser v. Shea, 88 M 562, 295 P 268 (1930).

Assignment of Lease: Plaintiffs leased business property to one who covenanted to pay rent for the full term of 6½ years but thereafter assigned the lease to another who in turn subleased it to a third person, all with the consent of the lessors. Contention of defendant (the original lessee), in an action for rent, that novation resulted from his assignment of lease with consent of lessors, their acceptance of rent from assignee, and their recognition of latter's right to sublease was unavailing, where it was not apparent that acts of plaintiffs were inconsistent with their intention to continue to look to defendant for rent in case of default of his assignee. Harrison v. Fregger, 88 M 448, 294 P 372 (1930).

Affirmative Defense:

Novation is an affirmative defense. It constitutes new matter which must be specially pleaded. It is made by contract and is subject to all the rules concerning contracts in general. It must be supported by consideration. Bose v. Sullivan, 87 M 476, 288 P 614 (1930).

In action on notes the defense to which was novation, defendant had burden of proving that payee bank agreed to release him from all liability on the notes and to accept alleged new debtor as its debtor instead of defendant, that alleged new debtor agreed to pay notes, and that defendant to whom the new debtor was indebted released the latter from payment of an amount equal to total due on notes. First St. Bank v. Larsen, 65 M 404, 211 P 214 (1922).

Novation as a Cause of Action: When plaintiff failed to allege either that defendant company agreed that the contract claimed to have been made with its promoters should be its own, with the understanding that the original obligor should be released, or that it adopted or agreed to carry out the terms and conditions of the contract in substitution of the original obligor agreed to by the parties to the original contract, the complaint did not state a cause of action in novation. Kirkup v. Anaconda Amusement Co., 59 M 469, 197 P 1005, 17 ALR 441 (1921).

Renewal of Note: Renewal of a note will not be treated as payment or discharge of an original obligation unless there is an affirmative showing that its execution constituted a novation. First Nat'l Bank v. Cottonwood Land Co., 51 M 544, 154 P 582 (1916).

Agreements Not Constituting a Novation: Where automobile buyer gave a chattel mortgage to secure unpaid purchase money but afterward made a new agreement whereby he was to run the machine for hire, the seller paying expenses and the buyer to turn over to the seller all money received until the balance due on the machine was paid, the agreement did not effect a novation or extinguish the debt. Kinsman v. Stanhope, 50 M 41, 144 P 1083 (1914).

28-1-1501. Novation defined.

Case Notes

Novation Not Found: Defendant Mastersons was the original obligee in a contract with plaintiff and simply wanted his money for the building and property, not a substitute contract with another person when plaintiff defaulted by nonpayment. Plaintiff attempted to secure additional buyers for the property when he was in default and induced Mastersons to allow plaintiff to enter a buy-sell agreement as a seller with third parties. However, the buy-sell failed to effectuate a binding contract. There was no substituted contract and, therefore, no novation. Management, Inc. v. Mastersons, Inc., 189 M 435, 616 P2d 356, 37 St. Rep. 1601 (1980).

Pleading Novation: In pleading a novation a plaintiff must allege the following essential elements: a previous valid obligation, an agreement of all the parties to the new contract, extinguishment of the old contract, and validity of the new contract. The question of whether the facts alleged constitute a novation is one of law. Tannhauser v. Shea, 88 M 562, 295 P 268 (1930); Kirkup v. Anaconda Amusement Co., 59 M 469, 197 P 1005 (1921).

Novation and Assignment Distinguished: In novation, an obligation between original parties is completely extinguished and new obligation between transferee and obligator is substituted for the previous one; while in case of assignment of contract, obligation of original debtor continues to rest upon him and he may be compelled to respond to obligee upon default of assignee. Harrison v. Fregger, 88 M 448, 294 P 372 (1930).

Modification of Former Agreement Not a Novation: Where one is already legally bound by his contract (a note) to perform an obligation, a later agreement (a new note) for same consideration, modifying the former one, does not effect a novation. Bose v. Sullivan, 87 M 476, 288 P 614 (1930).

Essentials:

To constitute a novation by substitution of new debtor for old one with intent to release latter, there must be a mutual agreement between the three parties and creditor must have consented to discharge of original debtor and accepted promise of new one; such acceptance need not be shown by express words to that effect but may be implied from attendant facts and circumstances and subsequent conduct of parties. Kenison v. Anderson, 83 M 430, 272 P 679 (1928).

Novation, like any other valid contract, must be supported by consideration which may be the discharge of the original debt or the release of the original debtor, and may be proved by parol. Kenison v. Anderson, 83 M 430, 272 P 679 (1928).

Partial Novation: Where subcontractor assigned a portion of money to become due under his contract with defendant, and defendant accepted the assignment, the transaction constituted a novation to extent of money assigned. The assignee became creditor of defendant, and the rights and remedies of the parties were determinable under the contract of novation. Silver v. Morin, 74 M 398, 240 P 825 (1925).

28-1-1502. Kinds of novation.

Case Notes

Summary Judgment on Breach of Contract Affirmed — Wrongful Discharge Claim Reversed for Determination of Whether Claimant Was Employee or Independent Contractor: Tvedt brought a claim for breach of contract, wrongful termination, and indemnification of expenses, alleging that defendant group had breached the covenant of good faith and fair dealing, waived the at-will clauses in their employment agreement, and mischaracterized Tvedt as an independent contractor, rather than an employee. Defendant group moved for summary judgment and filed a contingent counterclaim stating that in the event that Tvedt was found to be defendant group's employee, then defendant group's obligation to pay Tvedt the contract value should cease and all payments made to Tvedt should be returned. The District Court determined that Tvedt was not an employee and granted summary judgment to defendant group on all claims, and Tvedt appealed. The Supreme Court affirmed summary judgment on the breach of covenant issue because Tvedt was given adequate notice of termination, defendant group was exercising the specific language of the at-will termination provision of the contract, and Tvedt did not demonstrate that defendant group had waived the right to enforce that provision. However, the court reversed summary judgment on the wrongful discharge claim because the District Court incorrectly applied defendant group's novation argument and because genuine issues of fact remained whether Tvedt was an employee or independent contractor and whether a manager's agreement that recognized Tvedt individually was in effect at the time of termination. Remand was ordered because the District Court never considered whether Tvedt was entitled to relief for wrongful discharge as a matter of law and, if so, whether the claim for indemnification was appropriate. Tvedt v. Farmers Ins. Group of Co., 2004 MT 125, 321 M 263, 91 P3d 1 (2004).

Subordination Agreement — Novation Not Found: A subordination agreement signed by the parties did not constitute a novation of the original promissory note. When the borrowers defaulted, the creditor could still sue on the original promissory note. There was no new consideration for a novation, and the subordination agreement did not disclose any intent by the parties to extinguish the old obligation. Waite v. Andreassi, 249 M 149, 813 P2d 987, 48 St. Rep. 647 (1991), followed in O'Brien v. O'Brien, 2022 MT 246, 411 Mont. 101, 532 P.3d 831.

Consent to Contractual Assignment Refused — Breach of Contract: A contract for sale of real property provided that assignment could be accomplished only with written consent of the seller and that such consent could not be unreasonably withheld. The District Court properly found that the contract was breached by the seller's failure to provide a sufficient reason for refusing to consent to an assignment and that seller was therefore responsible for damages. Erban v. Monforton, 227 M 531, 740 P2d 677, 44 St. Rep. 1290 (1987).

Novation of Lease — New Lessee's Obligation Not Affected by His Ownership Rights: Franchisor took possession of franchise after franchisee indicated a desire to sell the franchise. To make the franchise more attractive to prospective purchasers, franchisor agreed with Godwin, who had leased equipment to the franchise, to make the rental payments on the equipment if Godwin would forgo repossession of the equipment. In a proceeding involving right to possession of the equipment and recovery of rental payments, although franchisor claimed a right under the Uniform Commercial Code to possession of the equipment under its security agreement with franchisee, the lower court correctly found franchisor liable for rent. That franchisor may have been entitled to possession did not preclude it from making a binding agreement with Godwin to take over franchisee's rental payments. Taylor Rental Corp. v. Ted Godwin Leasing, Inc., 209 M 124, 681 P2d 691, 41 St. Rep. 594 (1984).

Novation Not Found: Defendant Mastersons was the original obligee in a contract with plaintiff and simply wanted his money for the building and property, not a substitute contract with another person when plaintiff defaulted by nonpayment. Plaintiff attempted to secure additional buyers for the property when he was in default and induced Mastersons to allow plaintiff to enter a buy-sell agreement as a seller with third parties. However, the buy-sell failed to effectuate a binding contract. There was no substituted contract and, therefore, no novation. Management, Inc. v. Mastersons, Inc., 189 M 435, 616 P2d 356, 37 St. Rep. 1601 (1980).

Assignment of Contract: Novation resulted where remodeling contract was assigned to contracting company's manager, who was superintending the work and paid all bills presented even though charged to the company. The owner consented to the substitution and was in no position, in a mechanics' and materialmen's lien (now construction lien) foreclosure action, to question assignee's right to include in his claim money expended for labor and materials on the property before the assignment, but was estopped from denying that the assignee was the original contractor. Smith v. Gunniss, 115 M 362, 144 P2d 186 (1943).

Substitution of New Debtor for Old:

In determining whether substitution of new debtor for old one constituted a novation, intent to release original debtor is of vital importance. There must have been a clear and definite intention on the part of all concerned in that behalf, since novation is never to be presumed. Harrison v. Fregger, 88 M 448, 294 P 372 (1930).

To constitute novation by substitution of new debtor for old one with intent to release the latter, there must be a mutual agreement between the three parties and creditor must have consented to discharge of original debtor and accepted promise of new one; such consent and acceptance need not necessarily be shown by express words to that effect but may be implied from attendant facts and circumstances and subsequent conduct of parties. Kenison v. Anderson, 83 M 430, 272 P 679 (1928); McAllister v. McDonald, 40 M 375, 106 P 882 (1910).

Acceptance of new note from defendants for one executed by their father resulted in novation which barred plaintiff payee from thereafter enforcing the trust which he might otherwise have relied upon to secure payment of the original note. Larsen v. Marcy, 61 M 1, 201 P 685 (1921).

Agreements Not Constituting Novation:

In action for rent, it was held that where plaintiffs leased business property to one who covenanted to pay rent for full term of 6½ years and thereafter assigned lease to another, he in turn subleasing to a third, all with the consent of the lessors, contention of defendant (original lessee) that novation resulted from his assignment of lease with consent of lessors, their acceptance of rent from assignee, and their recognition of the latter's right to sublease was not upheld, nothing appearing from acts of plaintiffs enumerated inconsistent with their intention to continue to look to defendant for rent in case of default of his assignee. Harrison v. Fregger, 88 M 448, 294 P 372 (1930).

No cause of action in novation was stated where complaint failed to allege either that defendant company agreed that contract claimed to have been made with its promoters should be its own, with the understanding that original obligor be released, or that it agreed to carry out terms of contract in place of original obligor, agreed to by the parties to the original contract. Kirkup v. Anaconda Amusement Co., 59 M 469, 197 P 1005, 17 ALR 441 (1921).

General Essentials: In action on notes the defense to which was novation, defendant had burden of proving that payee bank agreed to release him from all liability on the notes and to accept alleged new debtor as its debtor instead of defendant, that alleged new debtor agreed to pay notes, and that defendant to whom the new debtor was indebted released the latter from payment of an amount equal to total due on notes. First St. Bank v. Larsen, 65 M 404, 211 P 214 (1922).

Agreements Constituting a Novation: Where purchaser of building had agreed with seller immediately upon completion of sale, and with plaintiff, that he would assume a debt due the latter from seller for a lighting plant installed by him in the building prior to the sale, the transaction amounted to a "novation" within meaning of subsection (2) of this section and rendered purchaser liable on obligation assumed by him. Sullivan v. Marshall, 56 M 568, 187 P 1013 (1919).

28-1-1503. How novation accomplished.

Case Notes

Consideration Essential: A novation, like other valid contracts, must be supported by consideration, which may be discharge of original debt or release of original debtor. Proof of novation may be by parol. Kenison v. Anderson, 83 M 430, 272 P 679 (1928). See also Bose v. Sullivan, 87 M 476, 288 P 614 (1930).

Mutual Agreement Between Parties: To constitute a novation by substitution of debtors, there must be a mutual agreement between the three (or more) parties involved and "the creditor must have consented to the discharge of the original debtor and have accepted the promise of the new debtor. It is not essential that the assent to and acceptance of the terms of novation be shown by express words to that effect, but the same may be implied from the facts and circumstances attending the transaction and the conduct of the parties thereafter." Kenison v. Anderson, 83 M 430, 272 P 679 (1928); Silver v. Morin, 74 M 398, 240 P 825 (1925); First St. Bank v. Larsen, 65 M 404, 211 P 214 (1922); McAllister v. McDonald, 40 M 375, 106 P 882 (1910).

28-1-1504. When acceptance of novation may be rescinded.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Part 16
Release of Debtor by Creditor

Part Case Notes

Release Procured Through Fraud: Where plaintiff, in his reply, alleged that release pleaded by defendant's answer was procured through fraud, whether there was sufficient fraud to avoid the release was question for jury. Westfall v. Motors Ins. Corp., 140 M 564, 374 P2d 96 (1962).

28-1-1601. Extinction of obligation by a release.

Case Notes

Debtor Signed Release Provided by Creditor — Creditor Did Not Refund Surplus — Debtor Sought Surplus — Release Did Not End Article 9 Protections for Creditor: The District Court erred in granting summary judgment to the defendant creditor and in determining that a release agreement the plaintiff debtor signed terminated any further application of the Uniform Commercial Code. The plaintiff entered into an installment sale contract and security agreement to purchase a mobile home with a company that assigned the contract to the defendant. Six years later, the plaintiff voluntarily vacated the mobile home and allowed the defendant to take possession of it. When the plaintiff returned the mobile home to the defendant, she owed $39,791.80. The plaintiff signed a full release of contract, under which she released all rights to the mobile home. The defendant resold the mobile home 1 month later, without notice to the plaintiff, for $53,500, which the plaintiff alleged was $13,708.20 more than the principal she owed when she returned the mobile home. The defendant did not refund any surplus to the plaintiff and disputed that a surplus was in fact realized. The plaintiff argued that the execution of the release did not terminate the defendant's duty under 30-9A-608 to pay her the surplus proceeds from the resale of the mobile home. The Supreme Court determined that despite the release, Article 9 of the U.C.C. (Title 30, ch. 9A) may still require the creditor to account for a surplus realized from the collection of an account or from the disposition of the collateral. The plaintiff's relationship to the defendant was one of debtor to creditor through a secured transaction governed by Article 9. When the plaintiff defaulted on her obligations under the contract, the defendant's rights and responsibilities as a creditor also were governed by Article 9. The defendant's argument that Article 9 no longer governed the parties' relationship following execution of the release was based on its representation that it agreed in the release to absolve the plaintiff from any further contractual obligation she owed to the defendant. The release did not, by its express terms, lift the parties' relationship from that of debtor and creditor under Article 9 or render obsolete the protections afforded a debtor under 30-9A-608 and 30-9A-615. Kapor v. RJC Inv., Inc., 2019 MT 41, 394 Mont. 311, 434 P.3d 869.

Successor in Interest Bound Only to Extent of Underlying Interests: The Leonards granted 36% of the interest in a log home to the Johnstons. After certain defects with the log home were found, the Leonards signed a general release of liability in favor of the log cabin construction company. Subsequently, more extensive structural defects were found in the cabin. In addition, both the Johnstons and the Leonards sold their interest in the property to a third party, the Johnston Trust. The District Court found that the release applied to the entire interest owned by the Johnston Trust. The Supreme Court reversed with respect to the Johnstons, finding that although the Johnston Trust was the successor to both interests, the release was binding only on the interests owned by the Leonards at the time that they signed it. Johnston v. Centennial Log Homes & Furnishings, Inc., 2013 MT 179, 370 Mont. 529, 305 P.3d 781.

Insurance Release Voided by Rescission — Insurer Not Entitled to Rely on Effect of Release Prior to Rescission: Six days after an auto accident, plaintiff signed a release and settled with defendant insurer for $3,500. About 1 month later, plaintiff asked defendant to rescind the release because plaintiff experienced additional pain, but defendant refused to rescind the release. Plaintiff then retained counsel, and defendant rescinded the release and settled the claim for about $200,000. Plaintiff then filed a Montana Unfair Trade Practices Act common-law bad faith claim. At trial the District Court granted plaintiff's motion to exclude evidence of the legal effect of the release and refused defendant's proposed jury instruction regarding the release. Defendant appealed, but the Supreme Court affirmed. Because defendant's rescission of the release effectively voided the release from the beginning, defendant was not, as a matter of law, entitled to rely on the legal effect of the release prior to rescission. Jacobsen v. Allstate Ins. Co., 2009 MT 248, 351 M 464, 215 P3d 649 (2009). See also Westfall v. Motors Ins. Corp., 140 M 564, 374 P2d 96 (1962).

Absence of Evidence of Rescission, Release, Waiver, or Accord and Satisfaction of Contract — Reversal Warranted: Plaintiffs owned shares in defendant's corporation and sought to sell the shares back to the corporation. The corporation sent a letter offering to purchase the shares for $64,933.60, and plaintiffs were instructed that to accept the offer, they were to sign the back of the stock certificate and mail it to the corporation. Plaintiffs did so, but included with the certificate a letter stating that by accepting the offer, plaintiffs reserved their rights under federal and state law. The corporation found the language unacceptable and declined to purchase the shares, instead returning the certificate to plaintiffs. Concerned about possessing a signed stock certificate, plaintiffs ultimately visited the corporation and surrendered the endorsed certificate in exchange for a new one. Plaintiffs then brought a breach of contract suit claiming

$64,933.60 in damages, asserting that the corporation had breached its offer to repurchase the stock. The corporation denied that a contract offer existed, arguing that plaintiffs' reply was not an acceptance but rather a counteroffer, and asserted that even if a contract did exist, plaintiffs had waived their rights under it by forfeiting the endorsed certificate in favor of a new one and by failing to immediately assert their rights under the contract. A jury found that the corporation had breached its contract, causing damages in the amount of $64,933.60, but then entered a verdict for the corporation on grounds that the corporation had proved at least one of its affirmative defenses of rescission, release, waiver, or accord and satisfaction. On appeal, the Supreme Court noted that only in rare cases should a jury verdict be set aside but reversed the verdict nevertheless on grounds that, even drawing all legitimate inferences in favor of the corporation, there was a complete absence of probative evidence supporting any of the corporation's affirmative defenses. The case was remanded for entry of judgment of $64,933.60 in favor of plaintiffs. Benson v. Diverse Computer Corp., 2004 MT 114, 321 M 140, 89 P3d 981 (2004), followed in Harland v. Anderson Ranch Co., 2004 MT 132, 321 M 338, 92 P3d 1160 (2004).

Unfair Trade Practice to Require Full and Final Release of Liability Before Claim Paid Within Policy Limits — "Settlement" Distinguished From "Release": Guaranty National Insurance Co. (Guaranty) provided a minimum motor vehicle liability policy for Moore, who was clearly liable for injuring the Watterses' in a car accident. Guaranty offered to settle the Watterses' claim to the extent of the policy coverage, but not without an absolute release of all liability. The Watterses declined the offer, eventually bringing an unfair trade action against Guaranty for failing to promptly pay damages for which Moore was liable. Guaranty argued that the full release from liability was necessary to effectuate a settlement, citing Thompson v. St. Farm Mut. Auto. Ins. Co., 161 M 207, 505 P2d 423 (1973), and Juedeman v. Nat'l Farmers Union Property & Cas. Co., 253 M 278, 833 P2d 191 (1992), and contended that because no settlement was proffered from the Watterses, Guaranty could not, as a matter of law, have violated 33-18-201. The Supreme Court instead applied Ridley v. Guar. Nat'l Ins. Co., 286 M 325, 951 P2d 987 (1997). The court clarified the relevant terms, noting that in accord with the general governing principles of contract law from which the law of settlements is derived, in the context of the Unfair Trade Practices Act, a settlement is synonymous with an enforceable bilateral contract that discharges a future or existing obligation, while a release, as a matter of law, is nothing more than an accord and satisfaction or one of several ways in which an obligation may contractually be discharged or settled for less than or for something different than from what is owed. The court concluded that a settlement between Guaranty and the Watterses was legally possible without the Watterses executing a full and final release of all liability, as evidenced by Guaranty's settlement of the Watterses' property damage claims within the limits of Moore's policy without a release. Thus, when liability resulting from an automobile accident is reasonably clear and a third-party claimant's damages undisputedly exceed mandatory minimum policy limits pursuant to 61-6-103, it is an unfair trade practice per se under 33-18-201 for an insurer to condition the payment of the owed mandatory minimum policy limits on the third party's agreement to provide a full and final release of all liability in favor of an insured. An insurer who pays mandatory minimum policy limits under these circumstances does not act in bad faith per se against its insured by not obtaining a full and final liability release on the insured's behalf. Unfortunately for the Watterses, under the case law in effect at the time, Guaranty had a reasonable basis under Juedeman upon which to deny payment of policy limits, so Guaranty's cross-motion for summary judgment was granted. Watters v. Guar. Nat'l Ins. Co., 2000 MT 150, 300 M 91, 3 P3d 626, 57 St. Rep. 588 (2000), overruling Thompson v. St. Farm Mut. Auto. Ins. Co., 161 M 207, 505 P2d 423 (1973), and Juedeman v. Nat'l Farmers Union Property & Cas. Co., 253 M 278, 833 P2d 191 (1992), and overruled in Shilhanek v. D-2 Trucking, Inc., 2003 MT 122, 315 M 519, 70 P3d 721 (2003), to the extent that Watters implies that an insurer's obligation under Ridley is limited to the minimum coverage required by the Motor Vehicle Safety-Responsibility Act. See also High Country Paving, Inc. v. United Fire & Cas. Co., 2019 MT 297, 398 Mont. 191, 454 P.3d 1210.

Promise to Hold Hearing — Requirement of Independent Consideration: Plaintiff, a custodian at the Yellowstone County Courthouse for 18 years, was discharged. His employment was "at will". After discharge, he was told by the County Commissioners that he would be given a grievance hearing. A letter was later sent to plaintiff, informing him that no hearing would be held. The promise to hold a hearing was not supported by independent consideration. Therefore, it was not an enforceable promise under contract law. Section 39-2-503 (now repealed) was, in effect, a part of the employment contract between plaintiff and the county. A promise to hold a hearing, given at a later date, could not modify that part of the contract without independent consideration unless consented to by both parties in writing. Reiter v. Yellowstone County, 192

M 194, 627 P2d 845, 38 St. Rep. 686 (1981), distinguished in Boreen v. Christensen, 267 M 405, 884 P2d 761, 51 St. Rep. 1014 (1994).

Rescission of Release: A release, being a contract, is subject to rescission for same reasons as other contracts, including fraud or mistake of fact. Westfall v. Motors Ins. Corp., 140 M 564, 374 P2d 96 (1962).

28-1-1602. What claims survive general release.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

28-1-1603. Effect of release of some but not all joint debtors.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

Case Notes

Joint Obligors — Modern View of Release of Party: Plaintiff, defendant, and another individual entered a written agreement for co-ownership of an airplane. The agreement contained a provision for the costs of usage, repair, and maintenance to be divided among the parties. Defendant was in arrears in his contributions. In early 1980, the parties decided to sell the plane. Defendant executed a blank bill of sale and delivered it to plaintiff. The third-party owner transferred his interest to plaintiff on May 16, 1980, in satisfaction of the amount owed the co-ownership. The plane was sold to a party other than that originally contemplated on October 30, 1980. Defendant contended the sale of the plane and the release of the third-party owner had the effect of releasing him from any obligation to plaintiff. There was no evidence to support this contention. The parties agreed to sell the plane, and defendant delivered a blank bill of sale to be used in the sale. The modern view of release of joint obligors is that where two or more obligors are jointly liable for a breach of contract, a release of one does not necessarily release the other. The question of whether the other is released depends upon: (1) the intention of the parties to the release instrument; and (2) whether the injured party has in fact received full compensation. Nothing in the transaction between the other owners indicated an intent to release defendant. Sunbird Aviation, Inc. v. Anderson, 200 M 438, 651 P2d 622, 39 St. Rep. 1855 (1982).

Comparison With Rule on Joint Tortfeasors: Where plaintiff compromised an action against Sheriff for false arrest and imprisonment for $1,000 and executed a release captioned "Release in full of all claims", reciting that he accepted said sum as "complete compensation for all injuries sustained in connection with" the matters set forth in the complaint, the release barred subsequent action against County Attorney, and it was held that even if tort liability was governed by statutes on joint debtors, the release would operate the same. Beedle v. Carolan, 115 M 587, 148 P2d 559 (1944).

CHAPTER 2
CONTRACTS

Chapter Law Review Articles

Consumer Contracts in Action, Furth-Matzkin, 82 Mont. L. Rev. 97 (2021).

Morrow v. Bank of America, Further Developments in Consumer Law in Montana, and their Impact on Consumers in the Age of COVID-19, Wilson & McCulloch, 82 Mont. L. Rev. 193 (2021).

Women's Autonomy in Nondisclosure Agreements for Sexual Misconduct Cases, Wagner, 82 Mont. L. Rev. 409 (2021).

Premarital Agreements in Montana, Barrett, 49 Mont. L. Rev. 56 (1988).

Contract Damages in Montana Part II: Reliance and Restitution, Burnham, 45 Mont. L. Rev. 1 (1984).

Contract Damages in Montana Part I: Expectancy Damages, Burnham, 44 Mont. L. Rev. 1 (1983).

The Default Clause in the Installment Land Contract, Isham, 42 Mont. L. Rev. 110 (1981).

Punitive Damages on Ordinary Contracts, Lee, 42 Mont. L. Rev. 93 (1981).

Presumptions Concerning Contracts, Clarke, 37 Mont. L. Rev. 101 (1976).

Toward Abolishing Installment Land Sale Contracts, Lohn, 36 Mont. L. Rev. 110 (1975).

State Contracts, Awarded to Montana Bidders When, 1961 Legislation, Mason, 22 Mont. L. Rev. 125 (1960).

Article 2: Sales, Mason, 21 Mont. L. Rev. 4 (1959).

Corporations: Validity of a Contract to Issue Stock for Future Services, Mertz, 2 Mont. L. Rev. 91 (1941).

Chapter Collateral References

Corbin on Contracts, Desk Edition, Murray Jr. and Murray (2019).

Contracts, Sixth Edition, Calamari and Perillo (2009).

Grismore on Contracts, Desk Edition, Murray Jr. (2009).

Contracts, 4th Edition, Farnsworth (2004).

Part 1
General Provisions

Part Case Notes

Questions of Fact Regarding Ambiguous Contract and Damages — Summary Judgment Inappropriate: Upon remand of a breach of contract action in Bradley v. Crow Tribe of Indians, 2003 MT 82, 315 M 75, 67 P3d 306 (2003), the District Court granted Bradley's motion for summary judgment a second time without considering the merits of defendant's defense to the breach of contract. However, because questions of fact still existed regarding ambiguous language in the contract and potential damages, summary judgment was inappropriate, so the case was again reversed and remanded for further consideration. Bradley v. Crow Tribe of Indians, 2005 MT 309, 329 M 448, 124 P3d 1143 (2005).

Assumption of Risk Inapplicable to Contract Action — Harmless Error: Garrison sued Averill, a real estate broker, in contract for defrauding him by failing to disclose the true facts concerning an easement on real property purchased by Garrison. The District Court found that Garrison had "assumed the risk" of subsequent damages by failing to read the terms of the easement. The Supreme Court held that assumption of risk is ordinarily a tort term associated with personal injury actions, but held that because the District Court did not continue with any more analysis or conclusion after its reference to assumption of risk and because the District Court found that Averill did not breach his duty of care to Garrison, the reference by the District Court to assumption of risk was harmless error. Garrison v. Averill, 282 M 508, 938 P2d 702, 54 St. Rep. 454 (1997).

Survey Services Provided — No Breach of Contract — Judicial Determination of Survey Locations Not Warranted: Property developers contracted with professional surveyors to survey several parcels of property into 20-acre lots. A subsequent unofficial government survey concluded that the results of the contracted work may have been in error, resulting in a potential encroachment of adjacent property. The developers brought an action for breach of contract, contending that if the corners were located where the government survey located them, some lots would be less than the 20-acre units they contracted for. The District Court properly found no breach of contract because, taking into consideration the inexact nature of surveying generally and the fact that the surveyors relied on approved standards and the best available information, the developers in fact received the services they contracted for. Yellowstone Basin Properties, Inc. v. Burgess, 255 M 341, 843 P2d 341, 49 St. Rep. 1051 (1992).

Unambiguous Contract — No Interpretation Needed: When the words of a contract are clear, certain, and unambiguous, the language alone controls and there is nothing for the courts to interpret or construe. In the construction of contracts, the courts may look not only to the language employed but also to the subject matter and the surrounding circumstances and may avail themselves of the same light that the parties possessed when the contract was made. The District Court did not err when it found that the term "concrete" included, specifically, precast concrete panels. Morning Star Enterprises, Inc. v. R.H. Grover, Inc., 247 M 105, 805 P2d 553, 48 St. Rep. 112 (1991), followed in Nyquist v. Nyquist, 255 M 149, 841 P2d 515, 49 St. Rep. 927 (1992).

Existence of Contract Question for Trier of Fact: If the existence of an oral contract is contested and the evidence is conflicting, the existence of the contract is a question for the trier of fact. In re Marriage of Dalley, 237 M 287, 773 P2d 295, 46 St. Rep. 808 (1989).

No Unilateral Resumption of Contract Terms Following Breach of Contract: Once a contract has been breached, its terms may not be unilaterally resumed. The breaching party cannot claim entitlement to the contract benefits, and the nonbreaching party has no duty to perform under the contract terms. W. Media, Inc. v. Merrick, 232 M 480, 757 P2d 1308, 45 St. Rep. 1212 (1988), followed, with regard to performance under a construction contract, in James Talcott Constr., Inc. v. P&D Land Enterprises, 2006 MT 188, 333 M 107, 141 P3d 1200 (2006).

Use of Plats to Induce Purchasers: In order to sell lots, a subdivider prepared and recorded subdivision plat maps that designated common areas and roadways. The purchase and sale contracts did not state who would construct roads or common areas. The issue of whether purchasers of lots have any legally enforceable right to have roads constructed depends not on their designation in the plats but on the subdivider's use of the plats in inducing purchasers. The instruments in question do not comprise a promise, express or implied, to construct roads. The purchasers did acquire an easement for the designated use. The case was remanded to determine factual issues relating to the use of the plats in inducing purchasers. Majers v. Shining Mtns., 219 M 366, 711 P2d 1375, 43 St. Rep. 16 (1986).

Lease — Lessor to Renovate — Bilateral Contract: Plaintiff and defendant signed a lease under which plaintiff was to renovate the leased office space and the two were to confer on the renovation and mutually agree on the final plans. Disagreements as to the plans arose. Plaintiff claimed he had increasing difficulties in contacting defendant. Defendant rescinded the lease on the ground that it had continually invested more time and money than plaintiff and thus from a business standpoint the lease was no longer feasible. Plaintiff's attempt to contact defendant's president failed, and plaintiff sent a notice of default and sued. The lease was not an executory unilateral contract; it was a bilateral obligation under which defendant was required to work with plaintiff in designing and approving plans and act reasonably if defendant disapproved the plans. The verdict for plaintiff and denial of defendant's motions for a directed verdict and judgment notwithstanding the verdict were affirmed. Nicholson v. United Pac. Ins. Co., 219 M 32, 710 P2d 1342, 42 St. Rep. 1822 (1985).

Distributorship Contract — No Termination Date — When Terminable: In deciding an issue never before decided by the court, the Supreme Court, in action by distributor for breach of wine distributorship contract by wine broker who terminated the contract, which had no termination provision, adopted the "modern majority rule" that when a distributorship contract has no termination provision, it is terminable at will only after a reasonable amount of time and upon reasonable notice. The court held that the rule applied where, as in the case at hand, the distributor had made a substantial investment in establishing or furthering the distributorship. The court deferred to the trier of fact on the issue of what a reasonable amount of time is, stating that absent an abuse of discretion the Supreme Court would not interfere. In the present case, the court upheld the lower court's decision that 24 months was a reasonable amount of time. Bronken's Good Time Co. v. J. W. Brown & Associates, 203 M 427, 661 P2d 861, 40 St. Rep. 549 (1983), followed in Moats Trucking Co., Inc. v. Gallatin Dairies, Inc., 231 M 474, 753 P2d 883, 45 St. Rep. 772 (1988).

28-2-101. Contract defined.

Case Notes

Engagement Ring Given in Contemplation of Marriage Not Considered Gift — Conditional Gift Analysis: Albinger gave Harris a $29,000 diamond engagement ring when the two promised to marry. The relationship was strained, resulting in breakups and the return of the ring to Albinger several times, but each time the couple reconciled, and the ring was returned to Harris. Following their final separation, Albinger told Harris to "take the car, the horse, the dog, and the ring", so Harris moved to Kentucky, marriage plans evaporated, and Harris refused to return the ring. Albinger filed in District Court to settle ownership of the ring. The District Court found the ring to be a gift in contemplation of marriage, implying that the existence of a condition attached to the gift, and held that Albinger was entitled to return of the ring upon failure of the condition of marriage. Harris appealed, and the Supreme Court reversed. The rights and duties of parties regarding property exchanges in contemplation of marriage are determined by existing law and common-law principles. A gift is a transfer of personal property made voluntarily and without consideration, and the essential elements of an inter vivos gift are donative intent, voluntary delivery, and acceptance by the recipient. Delivery, which manifests the intent of the giver, must turn over dominion and control of the property to the recipient, and when made without condition, such a gift becomes irrevocable upon acceptance, so the Supreme Court will not void the transfer when the giver experiences a change of heart. The only revocable gift recognized under Montana law is a gift in view of death, and a gift causa mortis may be revoked by the giver at any time and is revoked by the giver's recovery from the illness or escape from the peril under which the gift was made. However, the Supreme Court declined to analogize gifts in contemplation of marriage with a gift in contemplation of death. Further, a purported gift that is part of the inducement for an agreement to do or not do a certain thing becomes the consideration essential to contract formation. An exchange of promises creates a contract to marry, albeit an unenforceable one, so when an engagement ring is given as consideration for the promise to marry, a contract is formed and legal action to recover the ring is barred by the abolition of breach of promise actions in 27-1-602. Here, the engagement ring was an unconditional, completed gift upon acceptance, and a completed gift is not revocable. Thus, the ring remained in Harris's ownership and control. Albinger v. Harris, 2002 MT 118, 310 M 27, 48 P3d 711 (2002).

Contract Principles Inapplicable to Lease: The Supreme Court rejected an argument that the lease in issue should have been treated as a contract rather than a conveyance of an interest in land, stating that the case involved a lease, not a contract to make a lease. Knight v. OMI Corp., 174 M 72, 568 P2d 552 (1977).

Letter as Contract: A letter signed by contractor and written to owner of property stating the maximum cost of the construction of a house for purpose of permitting the owner to obtain a G.I. loan constituted a contract. Higby v. Hooper, 124 M 331, 221 P2d 1043 (1950).

Allegation of Contract: Complaint alleging that defendants agreed to sell for a specified consideration and that plaintiffs agreed to purchase, together with other averments in the complaint, contained a sufficient allegation of a contract. Johnson v. Elliot, 123 M 597, 218 P2d 703 (1950).

A Contract as a Voluntary Obligation: The terms "contracts" and "engagements" have much the same meaning, the latter being sometimes defined as quasi contracts. Each denotes a voluntarily assumed obligation and does not include torts. Capital Nat'l Bank of St. Paul v. Bartley, 101 M 591, 56 P2d 728 (1936).

Quasi-Contract: Where one has received money which, though not bound to do so by express contract, he in equity and good conscience ought to turn over to him from whom he received it, the law implies a promise on his part to that effect, and the obligation thus created or implied by law is termed a "quasi-contract", as distinguished from a contract as defined in this section and 28-2-102. Schaeffer v. Miller, 41 M 417, 109 P 970 (1910), distinguished in Keith v. Kottas, 119 M 98, 172 P2d 306 (1946).

Common-Law Definition: This section contains nothing more than the common-law definition of the term contract, and is manifestly intended to apply only to those obligations which arise immediately out of dealings between the parties, and not to that sort of contract which arises remotely out of the compact of government. Oppenheimer v. Regan, 32 M 110, 79 P 695 (1905).

Attorney General's Opinions

Deed Not a Contract: A contract, as defined in this section, is "an agreement to do or not do a certain thing". A deed, on the other hand, is not a contract. A deed is a written conveyance of realty, signed by the grantor, whereby title to realty is transferred from one to another. 35 A.G. Op. 65 (1974).

28-2-102. Essential elements of a contract.

Case Notes

Parties 97
Consent 98
Object 102
Consideration 105
Miscellaneous 109

PARTIES

Persons Not Parties to Contract — Right to Attorney Fees Under Contract Granting Them: When suit is brought under a contract providing for attorney fees to the prevailing party, persons who are not parties to the contract are not entitled to attorney fees, either under the contract or a statutory attorney fees provision. Where persons who were not parties to a contract by which a business was sold guaranteed payment of the purchase price, a guarantee which they had no intention of honoring, it was error to award them attorney fees upon finding that they were not liable under the guarantee because they received no consideration from plaintiff seller of the business for their guarantee. Rudio v. Yellowstone Merchandising Corp., 200 M 537, 652 P2d 1163, 39 St. Rep. 1923 (1982).

Meeting of Minds: It is axiomatic that a person cannot contract with himself. There must be the meeting of two separate and independent minds, at least two parties to a contract, and each must be competent. Gordon Campbell Petroleum Co. v. Gordon Campbell-Kevin Synd., 75 M 261, 242 P 540 (1926).

CONSENT

Meeting of Minds Required: Parties to a quiet title action engaged in a settlement discussion that caused one party to believe they had reached a settlement agreement. The District Court enforced the agreement as a contract. The Supreme Court reversed, finding that there was not a meeting of the minds. Jarussi v. Sandra L. Farber Trust, 209 MT 181, 396 Mont. 488, 445 P.3d 1226.

Termination of Policy — Express Disclaimer in Manual and Handbook — Policy Not Part of Employment Contract: A hospital discontinued a policy whereby it paid employees for their sick leave after 25 years of service. Employees with less than 25 years of service sued the hospital for breach of their employment contract. The hospital moved for summary judgment, arguing that the policy was not a part of the employment contract. It emphasized that the hospital's policy and procedure manual, as well as its employee handbook, explicitly provided that its policies could be amended, modified, or terminated at any time. The District Court granted the hospital summary judgment and the plaintiffs appealed. The Supreme Court agreed, holding that the express disclaimers in the hospital's manual and handbook clearly expressed its intention not to be contractually bound to the policy. Chipman v. NW. Healthcare Corp., 2014 MT 15, 373 Mont. 360, 317 P.3d 182.

Letters of Offer and Acceptance on Real Property Sale Exchanged — Terms of Response Immaterial — Contract for Sale Enforced by Specific Performance: Two sisters owned 78 acres as tenants in common. The defendant sister, who held a majority interest, sent a letter to the plaintiff sister, offering to sell her the majority interest or to purchase the minority interest. The letter set a deadline for a response and requested it be sent to a specified third party. Before the deadline expired, the plaintiff sister wrote back directly to her sister and agreed to purchase the majority interest. However, the defendant sister claimed she had decided to sell the property to their brother. The plaintiff sister sued, seeking specific performance of the contract. The defendant sister argued that the plaintiff had not accepted the original offer because she had not responded to the third party as requested. The District Court concluded that, as phrased in the letter, the request to direct the response to the third party was not a condition precedent to acceptance. On appeal, the Supreme Court agreed that the letters exchanged by the sisters formed a contract and that the mode of acceptance was not a condition precedent. The court affirmed the District Court's grant of specific performance ordering the defendant sister to sell her majority interest to the plaintiff. Olsen v. Johnston, 2013 MT 25, 368 Mont. 347, 301 P.3d 791.

Question Whether Parties Consented to Contract — Material Fact Precluding Summary Judgment: The District Court determined that defendant did not consent to a title policy, so the contract was invalid and defendant was entitled to summary judgment. On appeal, the Supreme Court found that the issue of whether and when plaintiff instructed defendant to issue the title policy in plaintiff's name was a material fact that was disputed by the parties. The extent and nature of the parties' consents are questions of fact that must be first determined, so summary judgment was inappropriate and the case was reversed and remanded for further proceedings. Amerimont, Inc. v. Fidelity Nat'l Title Ins. Co., 2009 MT 212, 351 M 292, 210 P3d 691 (2009).

Change in Credit Agreement Via "Bill Stuffer" Insufficient Notice on Which Unilateral Change to Contract Acceptable — Enforcement of Arbitration Clause: Defendant issued plaintiff a credit card and subsequently sent a "bill stuffer" with plaintiff's monthly statement that significantly changed the terms of the credit agreement. The change provided for arbitration of all credit disputes and prohibited jury trials and class actions. When plaintiff later filed a claim against defendant for multiple fair debt collections, defendant attempted to compel arbitration, asserting that plaintiff agreed to the credit agreement change through plaintiff's continued use of the credit card. The District Court agreed with defendant, issued an order compelling arbitration, and dismissed plaintiff's action. Plaintiff appealed and the Supreme Court reversed. Making a change in the credit agreement through use of a "bill stuffer" did not provide sufficient consumer notice on which acceptance of a unilateral change to a contract of adhesion could expressly or implicitly be found, including plaintiff's waiver of the fundamental constitutional right to a jury trial. The case was reversed for further proceedings. Kortum-Managhan v. Herbergers NBGL, 2009 MT 79, 349 M 475, 204 P3d 693 (2009), followed in Riehl v. Cambridge Ct. GF, LLC, 2010 MT 28, 355 Mont. 161, 226 P.3d 581, and following Keesun Partners v. Ferdig Oil Co., Inc., 249 M 331, 816 P2d 417 (1991). See also Kloss v. Edward D. Jones & Co., 2002 MT 129, 310 M 123, 54 P3d 1 (2002).

No Entitlement to Severance Benefits Following Rejection of Severance Package: Patterson's job was eliminated through a corporate restructuring, and Patterson was offered a severance package that was conditioned upon the release of all claims against the employer. Patterson declined the severance package and instead filed an employment discrimination claim against the employer. When the claim failed about 1 year later, Patterson signed the severance agreement and mailed it to the employer, who refused to honor it. Patterson then sued, claiming entitlement to the severance benefits. Following discovery, the District Court granted summary judgment for the employer. On appeal, the Supreme Court affirmed. The severance contract offer could no longer be considered valid because there was no mutual consent between the parties and because Patterson sought to accept the severance contract after violating the release provision. An acceptance upon terms varying from those offered is a rejection of the offer. Unless the party who made the original offer renews it or assents to a modification, an offeree cannot later revive a contract through acceptance after rejecting the offer. Patterson's purported acceptance was at best a counteroffer that the employer did not accept, so no contract arose between the parties as to severance, and Patterson was not entitled to severance benefits. Patterson v. Verizon Wireless, 2005 MT 261, 329 M 79, 122 P3d 1193 (2005).

Contract to Arbitrate Not Formed by Employee Handbook and Employee's Acknowledgment — Ambiguous Arbitration Provisions: When Hubner began working for defendant communications company, she signed an acknowledgment in an employee handbook that contained an arbitration provision. The arbitration clause provided that all controversies would be subject to binding arbitration, but the clauses in the handbook specified that the handbook did not constitute a contract of employment or create any relationship other than an employment-at-will relationship. When Hubner's employment was subsequently terminated, she brought a state claim for wrongful discharge, and defendant moved for a summary disposition compelling arbitration pursuant to 27-5-115. The District Court agreed with Hubner that there was no agreement to arbitrate and denied the motion, so defendant appealed. Defendant argued that because the arbitration clause was separable, it could be independently enforced. A state contract law defense that goes to the entire contract rather than specifically to an arbitration clause does not defeat a motion to compel arbitration; however, when a defense is aimed directly at the arbitration provision rather than the entire contract, state law contract defenses may be applied to hold that no enforceable agreement to arbitrate was made. Further, acceptance or consent by the party against whom a contract is sought to be enforced is required before a contract is enforceable. The language in the handbook was ambiguous and construed against the drafter. The ambiguity prevented Hubner from knowing and accepting that she was agreeing to binding arbitration by signing the handbook. Thus, no contract to arbitrate was formed by virtue of the handbook and Hubner's acknowledgment, even when the arbitration provision was considered separately from the rest of the handbook. The District Court was affirmed. Hubner v. Cutthroat Communications, Inc., 2003 MT 333, 318 M 421, 80 P3d 1256 (2003).

Mental Weakness Short of Incapacity Not Sufficient to Invalidate Premarital Agreement: When Mary and Larry were married, Mary was 21 and developmentally disabled and Larry was 62 and in poor health. Larry had three children from a previous marriage. Two days before the marriage, Mary and Larry signed a prenuptial agreement prepared by Larry's attorney that provided that each would keep the individual's separate property, whether owned then or acquired thereafter, free from any claim of the other by virtue of the marriage. Two years later, Larry died, and Mary brought an action to challenge the enforcement of the premarital agreement on grounds that, because of her disability, she was incapable of understanding the agreement and thus could not have given the required consent. The District Court found that Mary was mentally competent to understand the agreement when she signed it and that the contract was valid. The Supreme Court applied Gen. Motors v. Jackson, 900 P2d 345 (Nev. 1995), for the proposition that a person is mentally defective for purposes of capacity when the party, for any reason, is incapable of understanding the force and effect of the agreement, but that a mere mental weakness short of incapacity does not invalidate the agreement because capacity deals with the ability to understand the terms of the agreement, not a person's actual understanding. Capacity relates to the status of the person rather than the circumstances surrounding the transaction. Mary attended special education classes, but nevertheless graduated from high school. She could read and write, although poorly, and could drive a car, although she had no license. Absent any medical or expert testimony regarding Mary's level of competency, the District Court relied on lay testimony, including Mary's, to determine whether Mary met the burden of establishing incompetence. Substantial evidence supported the court's conclusion that Mary failed to meet her burden of proof, and the Supreme Court affirmed the validity of the premarital contract. Wilkes v. Estate of Wilkes, 2001 MT 118, 305 M 335, 27 P3d 433 (2001).

Lack of Consent by All Owners to Purchase Real Property — Contract Unenforceable: Thornton offered to purchase certain real property by executing a buy/sell agreement. The evidence showed that Thornton knew that half of the property was held in trust by Norwest and half was owned by Songstad and her sisters. Thornton obtained the signature of Songstad (representing her sisters) on the buy/sell agreement, but not that of Norwest. Citing Weigand v. Mt. Land & Real Estate Inv., Inc., 223 M 137, 724 P2d 194 (1986), and Rase v. Castle Mtn. Ranch, Inc., 193 M 209, 631 P2d 680 (1981), the Supreme Court held that even though Thornton intended to purchase 100% of the interests in the property, he did not obtain consent for the sale of 100%. Therefore, no contract was formed and specific performance was unavailable to require the sale of the property. Thornton v. Songstad, 263 M 390, 868 P2d 633, 51 St. Rep. 104 (1994), followed in Austin v. Cash, 274 M 54, 906 P2d 669, 52 St. Rep. 1119 (1995).

Claim of Economic Duress — Showing of Lack of Free Will Necessary: A claim of economic duress requires a showing that the contract at issue was made under circumstances evincing a lack of free will on the part of the contracting parties. It is not sufficient to show that consent was secured by the pressure of financial circumstances or that one of the parties merely insisted on its legal right. Aldrich & Co. v. Donovan, 238 M 431, 778 P2d 397, 46 St. Rep. 1393 (1989), following Shiplet v. First Sec. Bank of Livingston, 234 M 166, 762 P2d 242, 45 St. Rep. 1816 (1988), and followed in Hoven v. First Bank (N.A.)-Billings, 244 M 229, 797 P2d 915, 47 St. Rep. 1563 (1990), and Stanley v. Holms, 1999 MT 41, 293 M 343, 975 P2d 1242, 56 St. Rep. 178 (1999). See also Somersille v. Columbia Falls Aluminum Co., 255 M 101, 841 P2d 483, 49 St. Rep. 904 (1992), and Hughes v. Pullman, 2001 MT 216, 306 M 420, 36 P3d 339 (2001).

Offer and Acceptance:

Wife offered to convey shares of stock to husband to satisfy a dissolution judgment, but husband did not accept her offer; he merely agreed to consider it. Husband subsequently rejected wife's offer because of negative tax consequences associated with the transfer. There can be no binding contract without the mutual consent of the parties, and consent is established if there has been an offer and an acceptance of that offer. In re Marriage of Dalley, 237 M 287, 773 P2d 295, 46 St. Rep. 808 (1989).

In order to effect a contract there must be an offer by one party and an unconditional acceptance of it by the other party. Kuchinski v. Sec. Gen. Ins. Co., 141 M 515, 380 P2d 889 (1963).

Economic Duress Not Established: Economic duress is not established merely by proof that consent was secured by the pressure of financial circumstances or by the fact that one party insisted upon a legal right and the other party yielded to such insistence. Where plaintiffs were forced to continue to refinance because of inability to pay their loans and consequent threat of bank foreclosure, there is no "economic duress" that will void the loan contract. Shiplet v. First Sec. Bank of Livingston, Inc., 234 M 166, 762 P2d 242, 45 St. Rep. 1816 (1988).

Ignorance of Contract Contents Not Grounds for Relief From Liability: One who executes a written contract is presumed to know its contents and to assent to them. Ignorance of the contents is not grounds for relief from liability. Johnson v. Estate of Shelton, 232 M 85, 754 P2d 828, 45 St. Rep. 887 (1988), citing Quinn v. Briggs, 172 M 468, 565 P2d 297 (1977).

Buyer Failed to Sign Closing Agreement — No Consent: The court properly granted specific performance of the buy-sell agreement to the sellers of real property without reference to the proposed closing agreement. That agreement was not signed by the buyer and is not enforceable without his consent. Hillstrom v. O'Neil, 226 M 452, 736 P2d 126, 44 St. Rep. 795 (1987).

"Earnest Money Receipt and Agreement to Sell and Purchase" — Not Legally Enforceable Contract Without Consent: Plaintiffs made an offer to purchase certain property, provided $1 earnest money, and signed an "Earnest Money Receipt and Agreement to Sell and Purchase". Sellers never signed the agreement, acquired another prospective buyer, and returned the earnest money. The Supreme Court affirmed the trial court's finding that since the sellers never accepted the offer to purchase, under this section no contract existed. The court further noted that to find the offer to be a contract would be contrary to black letter contract law and would "wreck [sic] havoc on the real estate business". Weigand v. Mont. Land & Real Estate Inv., Inc., 223 M 137, 724 P2d 194, 43 St. Rep. 1595 (1986), followed in Thornton v. Songstad, 263 M 390, 868 P2d 633, 51 St. Rep. 104 (1994).

Later Agreement on Alleged Ambiguity — Ratification: Plaintiff offered to buy defendants' ranch. After much negotiation, plaintiff paid earnest money, for which he received a receipt, and the parties entered into a buy-sell agreement on April 20, 1981. The April 20, 1981, buy-sell agreement contained all the essential elements of a contract. The closing documents prepared by defendants' attorney did not correspond to the April 20 agreement. On May 15, 1981, the parties met and plaintiff was again presented with closing documents not corresponding to the April 20 agreement. A dispute arose over a clause releasing a parcel of land up to 320 acres to plaintiff for building purposes on the date of closing. Plaintiff agreed to defendants' interpretation at the May

15 meeting. On May 20, 1981, plaintiff received a third set of closing documents not reflecting the April 20 or May 15 meetings. On June 2, the parties met and defendants presented new terms, one of which was transferring title to the real property in 1981 rather than in 1982, destroying plaintiff's planned income tax advantages, one of his reasons for buying the ranch. Defendants claimed the land was required to be transferred at the time the cattle were transferred or grazing permits would be lost. A Forest Service official informed defendants in a June 3, 1981, letter that three alternatives existed. At the end of a June 5, 1981, meeting, plaintiff's attorney prepared a contract based on the April 20 buy-sell, the May 15 interpretation of the release, and the June 5 meeting. On June 12, plaintiff signed the contract and attached a check for the downpayment. Defendants refused to sign, and suit was filed on July 2, 1982. The District Court held that a valid contract existed and that defendants had breached the contract. On appeal, the Supreme Court held that the buy-sell contained all the essential elements of a contract. The court held that the release clause appeared unambiguous. The evidence presented showed that the parties' differing interpretations of the language were resolved and agreement on the clause was reached at the May 15, 1981, meeting. Under 28-2-304, a contract voidable for want of due consent may be ratified by subsequent consent. The May 15 agreement was held to be a ratification. Any delay in performance on plaintiff's part was due to defendants' failure to prepare documents conforming to the agreed-upon contract. The District Court was affirmed. Ehly v. Cady, 212 M 82, 687 P2d 687, 41 St. Rep. 1611 (1984).

Novation of Lease — New Lessee's Obligation Not Affected by His Ownership Rights: Franchisor took possession of franchise after franchisee indicated a desire to sell the franchise. To make the franchise more attractive to prospective purchasers, franchisor agreed with Godwin, who had leased equipment to the franchise, to make the rental payments on the equipment if Godwin would forgo repossession of the equipment. In a proceeding involving right to possession of the equipment and recovery of rental payments, although franchisor claimed a right under the Uniform Commercial Code to possession of the equipment under its security agreement with franchisee, the lower court correctly found franchisor liable for rent. That franchisor may have been entitled to possession did not preclude it from making a binding agreement with Godwin to take over franchisee's rental payments. Taylor Rental Corp. v. Ted Godwin Leasing, Inc., 209 M 124, 681 P2d 691, 41 St. Rep. 594 (1984).

Written Public Contract Bid — Oral Acknowledgment of Part — Meeting of Minds: The State's solicitation for bids for construction of building provided that the bid acknowledge receipt of any addenda. The State accepted the bid of a contractor that did not make the acknowledgment in its bid. The evidence that the State phoned the contractor regarding two addenda and contractor stated it knew of them and had begun preparation for fulfilling them was adequate to show that contractor had actual knowledge of the addenda and showed there was a meeting of the minds as to their existence and the requirements for fulfillment of their terms. Martel Constr., Inc. v. Bd. of Examiners, 205 M 332, 668 P2d 222, 40 St. Rep. 1340 (1983).

Executed Oral Agreement — Meeting of Minds Required: The parties entered into an agreement for the lease of a truck. The lease agreement contained a noncancellation provision and provided alternative remedies to the lessor in the event of a default. Lessee returned the truck with current payments to lessor prior to the termination date of the lease. Lessor had to make repairs to the truck. Lessee contended the return was a fully executed oral contract to terminate the lease. Lessor contended that termination was dependent on the condition of the truck. There was substantial evidence to support the finding that there was no meeting of the minds and therefore no agreement to terminate the lease. Diede v. Davis, 203 M 205, 661 P2d 838, 40 St. Rep. 394 (1983).

Claims Examiner Not Authorized to Make Final Workers' Compensation Settlement for State Fund: Claimant was injured at work in 1973. Her employer was enrolled under Workers' Compensation Plan No. 3. State fund accepted liability and paid some compensation to claimant. For 1½ years state fund negotiated with claimant to reach a final settlement of claimant's disability benefits. Claimant was represented by counsel, and the negotiations were conducted through a claims examiner with state fund who was supervised by the state fund bureau chief. In March 1981, the parties reached a tentative settlement. Claimant and her lawyer signed a petition for full and final compromise settlement. When the petition was presented to the state fund bureau chief, he rejected it as being excessive and beyond the liability of the state as an insurer. Claimant brought the matter to the Workers' Compensation Court where she claimed that she had entered into a binding final agreement with state fund. The Supreme Court affirmed the Workers' Compensation Court ruling that no binding contract was created because the state fund bureau chief had not consented to the terms and the claims examiner had neither actual nor ostensible authority to bind the state fund to a settlement contract. Christenson v. Billings Livestock Comm'n Co., 201 M 207, 653 P2d 492, 39 St. Rep. 2060 (1982).

Option Agreement — Sufficiency of Consent and Consideration: The defendant appealed from a judgment granting specific performance of an option agreement to the plaintiff and ordering the property involved conveyed to the plaintiff. On appeal, the Supreme Court rejected the defendant's contention that the writing involved was not an option agreement because it failed to meet the essential requirements for the validity of a contract. In particular, he contended that there was a lack of consent and that the consideration was legally insufficient. The Supreme Court found the actual payment of $1 and actual participation in a family corporate dissolution sufficient consideration for the agreement. A memorandum here acted as an offer, and a binding agreement resulted from action on that offer by the offeree. The trial court was affirmed. Van Atta v. Schillinger, 191 M 472, 625 P2d 73, 38 St. Rep. 426 (1981), followed in Hetherington v. Ford Motor Co., 257 M 395, 849 P2d 1039, 50 St. Rep. 325 (1993), which was distinguished in Murphy v. The Home Depot, 2012 MT 23, 364 Mont. 27, 270 P.3d 72.

Finality of Workers' Compensation Decision — Grounds for Overturning: A full and final compromise settlement agreement between an injured worker and the Workers' Compensation State Fund was set aside because of mutual mistake of material fact by both parties. Kienas v. Peterson, 191 M 325, 624 P2d 1, 37 St. Rep. 1747 (1980), distinguished in Sollie v. Travelers Indem. Co., 212 M 197, 686 P2d 920, 41 St. Rep. 1684 (1984). A petition for rehearing was filed. The Supreme Court reaffirmed the decision. The petitioner argued the Workers' Compensation Court had no power to alter or rescind the agreement 4 years after its execution. The Supreme Court pointed out that it, not the Workers' Compensation Court, set aside the agreement. It noted the scope of its appellate power and also the code provision on lack of consent through mutual mistake of material fact. The Supreme Court was not broadening the possibilities of reopening such settlements; it merely found that no contract existed initially. Kienas v. Peterson, 38 St. Rep. 320 (1981) (apparently not reported in Montana Reports or Pacific 2d Reporter).

Mutual Assent on Elements of Contract — Raising at Trial Level: Plaintiff and defendants entered a buy-sell agreement for a parcel of land owned by defendants. From the filing of the complaint to eventual trial, both parties contended that the buy-sell was valid and enforceable against the other. The issue at trial was not the validity of the contract but whether it included certain alleged easements. Plaintiff was granted specific performance. On appeal, defendants contended that the parties had never agreed on the same terms, that there was no mutual assent or meeting of the minds, and therefore no enforceable contract. Because this contention had not been raised at the trial level, it could not be considered on appeal. Chadwick v. Giberson, 190 M 88, 618 P2d 1213, 37 St. Rep. 1723 (1980).

Contract Barred at Law as in Equity: The legal deficiencies of inadequacy of consideration and lack of consent are equally applicable to bar enforcement of a written contract at law as in equity. Schlegel v. Moorhead, 177 M 456, 582 P2d 336 (1978).

Bilateral Agreement: To constitute a bilateral agreement, the parties must have given their free and voluntary assent to the terms, which is a question of fact. Babcock v. Engel, 58 M 597, 194 P 137 (1920).

OBJECT

Limited Exceptions for Only One Party Insufficient to Render Arbitration Clause Facially Unconscionable: A contract between the defendant-appellee and a third-party provider ("TPP") of home automation products allowing remote control over property access, HVAC, and hot water systems included a clause requiring the parties to arbitrate disputes, with two narrow exceptions, both of which would allow the TPP to seek relief in court in lieu of arbitration. The District Court held that the arbitration clause was unenforceable because the exceptions unreasonably favored the TPP, resulting in a lack of mutuality. The Supreme Court disagreed and upheld the arbitration clause. The two exceptions allowed the TPP to join the defendant-appellee as a third-party defendant for purposes of enforcing the contract indemnification provisions and allowed the TPP to seek injunctive relief if the defendant-appellee breached the contract with respect to the TPP's intellectual property, proprietary rights, or business reputation. The Supreme Court held that the defendant-appellee and TPP were dissimilarly situated such that the defendant-appellee had no need for either of the narrow exceptions. Therefore, the limited exceptions being available only for the TPP was insufficient to show the arbitration agreement was lacking in mutual consideration or was otherwise unconscionable. Stowe v. Big Sky Vacation Rentals, Inc., 2019 MT 288, 398 Mont. 91, 454 P.3d 655.

Sufficient Evidence of Implied Contract to Preclude Summary Judgment — City Ordinance Not Bar to Liability: The plaintiffs sued the city of Dillon for damages after their water service was interrupted, claiming breach of contract, negligence, and infliction of emotional distress. The District Court granted summary judgment to the city, reasoning that no contract existed between the parties because the city commission never approved a contract for the plaintiffs' water service, as required by a city ordinance, and the plaintiffs' claims were barred by a city ordinance that provided that the city could shut off water and avoid liability for the resulting interruption of water service. The Supreme Court reversed. The city's conduct manifested the existence of a contract to furnish water to the plaintiffs' lot, and therefore the city was estopped from asserting that no contract existed. Because the city ordinance that bars claims arising from a break in water service applies only to situations in which the city decides to shut off water services, rather than when water is shut off from a creek and main line freezing as occurred in this case, summary judgment for the city was not appropriate. Conner v. Dillon, 2012 MT 21, 364 Mont. 8, 270 P.3d 75.

Timely Exercise of Third-Party Option to Purchase Real Property — No Breach of Buy-Sell Agreement: A provision in a buy-sell agreement between Palmer and Bahm allowed a third party 72 hours after the Palmer-Bahm agreement was signed to decide whether to purchase a strip of land from Bahm that was contained in the parcel covered by the agreement. Although the third party did not complete the transaction or enter into a separate buy-sell agreement within 72 hours, the buy-sell agreement required only that a purchase decision be made within 72 hours. Uncontroverted evidence showed that the third party made a timely decision to purchase the strip and communicated that decision to Bahm, so Bahm did not violate the agreement with Palmer or break the covenant of good faith and fair dealing by selling the strip to the third party. Palmer v. Bahm, 2006 MT 29, 331 M 105, 128 P3d 1031 (2006).

Failure of Teacher to Exhaust Grievance Procedures Required Under Unambiguous Contract — Estoppel Inapplicable Absent Factual Representation of Material Fact — Summary Judgment Proper: When Wurl's speech-language pathology contract was not renewed, Wurl brought an action against the school district alleging that termination procedures were not followed pursuant to a collectively bargained master agreement and also brought claims for wrongful discharge and due process violations. The parties disagreed whether the master agreement applied because Wurl was not certified. The District Court found that the master agreement did not apply and granted summary judgment to the school district, and Wurl appealed. The Supreme Court found that the language of the employment contract unambiguously incorporated the entirety of the master agreement by reference, so the District Court erred in holding otherwise. Wurl also contended that because the District Superintendent had stated that the master agreement did not apply, collateral estoppel should bar the district from asserting that Wurl failed to go through the collectively bargained grievance procedure. On this point, the Supreme Court disagreed. The superintendent's statement was a legal interpretation rather than a factual representation of a material fact, so Wurl failed to prove the first required element of collateral estoppel, and the district was therefore allowed to argue that Wurl's claims should be barred by failure to exhaust the grievance procedure. Because the master agreement applied and Wurl failed to implement the mandatory grievance procedure, Wurl's claims were barred. The Supreme Court affirmed the summary judgment. Wurl v. Polson School District No. 23, 2006 MT 8, 330 M 282, 127 P3d 436 (2006), following Elk Park Ranch, Inc. v. Park County, 282 M 154, 935 P2d 1131 (1997).

Interest Owed on State Highway Right-of-Way Condemnation Agreement Pursuant to Clear Language of Stipulation: The Department of Transportation filed a condemnation action against defendants in connection with a highway construction project. As part of the action, the parties entered a stipulation granting the Department possession of the right-of-way in exchange for $35,780, $11,000 payable immediately and $24,780 still owing, plus interest, at 10% a year, on the final award or settlement from the date of service of summons until the date of withdrawal by defendants. A dispute arose over the amount of interest owed. The District Court applied 70-30-302 and determined that the Department owed interest on $7,187 of the total remainder, the amount of land-leveling costs, which the Department paid. Defendants appealed the order, contending that interest was actually owed on the entire $24,780 remaining settlement. The Supreme Court agreed. The language in the stipulation was clear and unambiguous and required the Department to pay interest on the excess of the final settlement award, which was $24,780. The District Court erred in applying the statute to the exclusion of the actual stipulation language to which the parties agreed. The clear language of the stipulation and the intent of the parties controlled. The case was remanded with instructions to order the Department to pay interest on the entire final settlement, with credit for amounts already paid. St. v. Asbeck, 2003 MT 337, 318 M 431, 80 P3d 1272 (2003).

Modification of Nonexistent Contract Impossible — Minutes of Preconstruction Meeting Inadmissible Extrinsic Evidence Absent Ambiguity in Subsequent Contract: Keeney Construction (Keeney) subcontracted to perform certain construction work for James Talcott Construction Co., Inc. (Talcott). The subcontract stated that time was of the essence, but contained no specific date of completion, Rather, Keeney was to complete the work as directed by Talcott and on Talcott's completion schedule. Keeney asserted that the parties intended a 1996 completion date, but the project was not finished until 1997. Keeney sued for damages for delay and extra work, contending that extrinsic evidence in the form of minutes from a preconstruction meeting, held 2 days before the contract was finalized, would verify the parties' intent and represented an executed oral agreement that modified the written contract. The Supreme Court found no ambiguity in the written contract to warrant further examination of the intent of the parties. Because the intent of the contract was clear, the extrinsic evidence was inadmissible to support the contention that a specific completion date was intended. Keeney could not assert a claim for damages based on Talcott's direction of the timing of the completion of the project when the contract authorized Talcott to do so. Further, because an oral agreement cannot modify a contract that does not yet exist, the meeting and conversations held prior to the contract signing could not be interpreted as a modification of the subsequent written contract. Keeney Constr. v. James Talcott Constr. Co., Inc., 2002 MT 69, 309 M 226, 45 P3d 19 (2002).

Mistaken Valuation of Stock Insufficient Grounds for Rescission of Contract: Following termination from employment with Bitterroot International Systems, Inc. (Bitterroot), Knutson sought to exercise his buyout rights under the shareholders' agreement. Bitterroot refused to pay and sought rescission on grounds of mistake of fact, arguing that both parties had mistakenly valued stock exchanged during the purchase of another business. The District Court could not rescind a validly formed contract simply because Bitterroot undervalued the stock. A mutual mistake as to value is not necessarily sufficient to rescind a contract (see 17A C.J.S. Contracts §149). The District Court did not err in dismissing the affirmative defense of mistake of fact because the law does not protect a business from its improvident valuation of stock. Knutson v. Bitterroot Int'l Sys., Inc., 2000 MT 203, 300 M 511, 5 P3d 554, 57 St. Rep. 800 (2000).

Truth Regarding Value of Stock Discoverable by Party Claiming Estoppel — Defense Not Available: Following termination from employment with Bitterroot International Systems, Inc. (Bitterroot), Knutson sought to exercise his buyout rights under the shareholders' agreement. Bitterroot refused to pay and sought rescission on grounds of equitable estoppel, arguing that stock had been mistakenly valued during the purchase of another business, that Spencer, majority shareholder and president of both Bitterroot and the company that was acquired, relied on Knutson's valuation to Spencer's detriment, and that Spencer was unaware of factors that Knutson failed to consider. Spencer may have been mistaken about the value of the stock, but he was in a position to discover all the information necessary to value it and participated in its valuation. The truth regarding the stocks' value was as discoverable to Spencer as to anyone else, and the District Court did not err in dismissing Bitterroot's defense of equitable estoppel. Knutson v. Bitterroot Int'l Sys., Inc., 2000 MT 203, 300 M 511, 5 P3d 554, 57 St. Rep. 800 (2000), following Elk Park Ranch, Inc. v. Park County, 282 M 154, 935 P2d 1131 (1997).

Mutual Mistake of Any Material Fact as Warranting Rescission of Workers' Compensation Settlement: South injured her back on the job and underwent surgery twice to correct the problems. She entered into a full and final compromise settlement agreement with her insurer. The agreement listed seven jobs that both parties felt were acceptable for South to do. One of the jobs was massage therapy. South began training as a massage therapist but began experiencing back pain again, forcing her to quit the training and to undergo back surgery a third time. South then petitioned the Workers' Compensation Court to rescind the settlement agreement on grounds of mutual mistake of fact. The court denied her petition, treating the current problem as a new and different injury. The Supreme Court clarified Kienas v. Peterson, 191 M 325, 624 P2d 1 (1980), in holding that under fundamental contract principles for rescission, a mutual mistake regarding the nature or extent of a claimant's injury is not the only mutual mistake sufficient to set aside a final settlement agreement. Rather, if a party can show a mutual mistake of any material fact that impacts the contract to such an extent that the intended bargain of the parties is defeated, the contract may be rescinded. The operative question is whether a mutual mistake existed that justified rescission, without limitation to how or when the mistake was made. Even though the parties were not mistaken regarding the nature and extent of South's injury at the time that the contract was formed, both parties mistakenly believed that massage therapy was an appropriate job for South to pursue, and she relied on that fact to her detriment. It was error for the Workers' Compensation Court to fail to consider South's contention of mutual mistake regarding the propriety of the job approved for her to do; thus, she was entitled to rescission of the settlement agreement. South v. Transp. Ins. Co., 275 M 397, 913 P2d 233, 53 St. Rep. 196 (1996).

Performance Combined With Terms — Valid Contract: An agreement for development of a mineral interest did not include every item that might have been included with respect to operational aspects; however, the parties performed under the agreement for 3 years. The Supreme Court cited Wilkerson v. School District, 216 M 203, 700 P2d 617, 42 St. Rep. 745 (1985), in holding that a contract is not invalid simply because it does not contain all the provisions or conditions the parties might have incorporated into it. Therefore, performance under the agreement, combined with the actual terms provided, demonstrated the existence of a valid contract. Somont Oil Co., Inc. v. Nutter, 228 M 467, 743 P2d 1016, 44 St. Rep. 1685 (1987).

Option Agreement Upheld — Minor Variations Not Fatal: The defendant appealed from a judgment granting specific performance of an option agreement to the plaintiff and ordering the property involved conveyed to the plaintiff. The defendant claimed on appeal that the tender and demand under the option agreement were not a legal tender. Specifically, he contended that the claimed tender actually was a counteroffer, and therefore he was at liberty to ignore it or to impose other terms in response to it. A number of attacks on the actual terms of the "tender and demand" sent by him to the plaintiffs were included in this issue on appeal. Matters that are subsidiary, collateral, or which do not go to the performance of the contract are not essential and do not have to be expressed in the contract. Accordingly, the plaintiffs' obtaining a warranty deed and the signature of the defendant's wife on the deed here, when they had no right to obtain either, was not a fatal variance from the terms of the option agreement. The option agreement did not specify the kind of deed, and in such cases it is presumed that a fee simple is intended to pass. The court noted that the plaintiffs were ready, willing, and able to perform. The demand that the defendant's wife also sign the deed was not such a material variance from the option agreement as to defeat specific performance. Van Atta v. Schillinger, 191 M 472, 625 P2d 73, 38 St. Rep. 426 (1981).

Real Estate Commission — Setting Chain in Motion Required to Collect Commission: Defendant contended that the requirements of a listing agreement were not sufficiently met by plaintiff to allow the collection of her commission. Plaintiff placed an ad in the newspaper, which named an erroneous price. As a result of that ad, the eventual buyer called plaintiff and obtained the location and identification of the property and the sellers. Plaintiff called defendant and advised her of this development. Defendant then negotiated with the buyer and closed the sale. A broker is entitled to his commission if his efforts set in motion a chain of events which finally culminate in the sale of the property. Here, plaintiff set that chain in motion. Barrett v. Ballard, 191 M 39, 622 P2d 180, 37 St. Rep. 2038 (1980), followed in Lane v. Smith, 255 M 218, 841 P2d 1143, 49 St. Rep. 974 (1992), and in Hall & Hall, Inc. v. Hyde, 264 M 190, 870 P2d 1362, 51 St. Rep. 257 (1994).

Application of Liquor Statutes: The sale of an interest in the operation of a bar in which there was no intent to transfer any interest in the liquor license was not contrary to the provisions of liquor statutes and did not constitute an illegal contract. Johnstone v. Svejkovsky, 170 M 504, 554 P2d 1329 (1976).

CONSIDERATION

Arbitration Requirement Not Void or Unconscionable Under Circumstances: A former financial advisor sought to have an arbitration agreement set aside under theories of lack of mutuality, lack of explicit waiver of Montana constitutional rights, and unconscionability. Upon review of the case and after extensive discussion of its circumstances, the Supreme Court disagreed with all such contentions. Bucy v. Edward Jones & Co., 2019 MT 173, 396 Mont. 408, 445 P.3d 812.

Easement Road Maintenance Agreement — Essential Elements of Contract — Agreement Enforceable: Easement owners and landowners entered into a road maintenance agreement for which the landowners did not receive any remuneration. Later, when the easement owners filed suit against the landowners for breach of the agreement, the District Court ruled that the agreement was not enforceable because of a lack of consideration. On appeal, the Supreme Court ruled that the District Court had erred when it concluded that the agreement was not enforceable. The Supreme Court concluded that because the landowners also used the easement road, they received a conferred benefit in its maintenance, and therefore the agreement contained the essential elements of a contract. Low v. Reick, 2016 MT 167, 384 Mont. 101, 376 P.3d 777.

Landowner Subdivision Rights Precluded by Restrictive Covenants — No Oral Contract Without Consideration — Statute of Frauds Applied: Plaintiffs subdivided about 80 acres into a 40-acre water ski lake and five residential lots. Restrictive covenants provided that no more than six landowners would be allowed to use the lake, that five landowners would be owners of lots in the subdivision, and that one landowner would be the owner of a single family dwelling built on property immediately west of the lake. Plaintiffs initially intended to build on the west side of the lake and become the sixth landowner but changed their minds, sold the west side property, and decided to build on the south side instead. Four of the five landowners filed an affidavit that when they purchased their lots, they understood that plaintiffs would be the sixth landowner and that they had orally approved the relocation of plaintiffs' residence to the south shore. After plaintiffs' home was built on the south side, they sought a declaratory judgment that they were the sixth landowner under the restrictive covenants and thus had the right to use the lake. One dissenting landowner opposed the declaratory judgment and moved for summary judgment on grounds that the restrictive covenants prohibited plaintiffs from use of the lake. The District Court agreed and granted summary judgment. On appeal, the Supreme Court agreed that there was no evidence of consideration given to the landowners for modification of the covenants and that as a result, the modification benefited plaintiffs only. The right to use the lake ran with the land and was therefore a real property interest, and under the statute of frauds, any transfer of the right from one parcel to another had to be in writing or altered by an executed oral agreement. However, without consideration, there could be no oral contract, and without an oral contract, there could be no executed oral contract. Plaintiffs' argument that because they relied on oral agreements, equitable estoppel should prohibit defendants from denying plaintiffs' use of the lake also failed because equitable estoppel does not apply under the statute of frauds except when the statute would operate to perpetuate a fraud. The District Court was affirmed. Hanson v. Water Ski Mania Estates, 2005 MT 47, 326 M 154, 108 P3d 481 (2005).

Reciprocal Rights and Obligations Considered Sufficient Consideration to Sustain Shareholders' Agreement: Following his termination from employment with Bitterroot International Systems, Inc. (Bitterroot), Knutson sought to exercise his buyout rights under the shareholders' agreement. Bitterroot refused to pay on grounds of insufficient consideration, contending that the essential consideration for the shareholders' agreement was the exchange of stocks of equal value—an argument based on the premise that the stock exchange and the shareholders' agreement were one agreement. However, the shareholders' agreement was enforceable independent of the stock exchange between the parties, and the creation of reciprocal rights and obligations among the shareholders was sufficient consideration to sustain the shareholders' agreement; thus, the District Court did not err in concluding that the consideration was sufficient. Knutson v. Bitterroot Int'l Sys., Inc., 2000 MT 203, 300 M 511, 5 P3d 554, 57 St. Rep. 800 (2000).

Materiality of Claim of Failure of Consideration to Contract Required Before Rescission Available as Remedy — Partial Failure of Consideration — Meltdown of Ice Cream Distributorship Agreement: Under Johnson v. Meiers, 118 M 258, 164 P2d 1012 (1946), a breach that goes to only part of the consideration, that is incidental and subordinate to the main purpose of the contract, and that may be compensated in damages does not warrant rescission. The injured party is still bound to perform that party's part of the contract, and the only remedy for the breach consists of the damages suffered from the breach. By contrast, under Van Hook v. Baum, 245 M 407, 800 P2d 151, 47 St. Rep. 1883 (1990), a party may rescind if, through the fault of the other party, consideration fails in whole or in part. In clarifying the disparate holdings, the Supreme Court noted that the term "failure of consideration", as either a claim or an affirmative defense, does not relate to the absence of consideration or whether there is good consideration for the formation of a valid, enforceable contract, but rather the term pertains to the failure of one party's performance, which then suspends or excuses the performance of the other party pursuant to the terms of a valid contract. Failure of consideration is generally synonymous with a material breach of performance of a contract, rather than whether a contract was enforceable because of the absence of the essential element of consideration. Thus, a claim or affirmative defense of failure of consideration that gives rise to the equitable remedy of rescission requires a showing by the claiming party that the other party's failure to perform was, in fact, material to the contract, and whether consideration was sufficient or good is immaterial. To reconcile this holding with 28-2-1711, the court went on to hold that failure of part of a promised performance may warrant rescission, but only if the claiming party proves that the deficient part of the other party's performance was material to the contract. If the failure to perform was not material, rescission is not an available remedy, performance cannot be excused, and the claiming party "may only be entitled to money damages for breach". Here, the District Court erred when it did not determine whether Norwood's failure to assign an ice cream distributor agreement to Service Distributing, Inc. (SDI), was material to the transaction as a whole. Absent that finding, SDI could not as a matter of law rescind the contract and be excused from further performance of its obligation to Norwood, so the case was remanded to determine whether a material breach occurred. Norwood v. Serv. Distrib., Inc., 2000 MT 4, 297 M 473, 994 P2d 25, 57 St. Rep. 8 (2000). See also Flaig v. Gramm, 1999 MT 181, 295 M 297, 983 P2d 396, 56 St. Rep. 710 (1999).

Consideration Under Contract Creating Relationship of Lender and Approved Dealer for Making Housing Loans: A contract between the parties created a relationship of Green Tree Financial Corporation (Green Tree) as "lender" and Larson, doing business as Majestic Homes, Inc. (Majestic), as "approved dealer", for purposes of making federal housing loans pursuant to federal Housing and Urban Development (HUD) regulations. Majestic submitted an application to become an approved dealer, and Green Tree then approved Majestic as a dealer and required Majestic to enter into a dealer agreement that included terms expressly provided for by HUD regulations. In order to become and remain an approved dealer, Majestic promised to operate pursuant to HUD regulations—something that it was not otherwise obligated to do in the course of its business. Complying with HUD regulations and meeting other requirements of Green Tree constituted good consideration on the part of Majestic. In return for Majestic's conformance to federal regulations and a security interest in Majestic's assets, Green Tree agreed to perform a service for Majestic by reviewing and approving or rejecting credit applications that Majestic submitted on behalf of its customers. Majestic was allowed to hold itself out as an approved dealer, which provided a competitive advantage in the manufactured home business. The arrangement constituted a contractual relationship whereby the parties exchanged valuable consideration and was enforceable. This relationship is distinguishable from an indefinite requirements or output contract in which there is no exchange of obligations and no establishment of a lender-dealer relationship. Larson v. Green Tree Financial Corp., 1999 MT 157, 295 M 110, 983 P2d 357, 56 St. Rep. 618 (1999). See also Linn v. City County Health Dept., 1999 MT 235, 296 M 145, 988 P2d 302, 56 St. Rep. 922 (1999).

Equipment Rental Agreement Creating Presumption of Consideration — Burden of Proof: Carl Weissman & Sons (CWS) agreed to rent a rock drill to D&L Thomas Equipment (D&L). A clause in the rental agreement required D&L to inspect the drill and notify CWS within 10 days specifying any defects and provided that if CWS was not notified, the drill would be conclusively presumed to have been accepted in its condition at the time of receipt. D&L contended that there were problems with the drill immediately after it was received, but did not notify CWS in writing within the 10-day period specified in the rental agreement. D&L asserted that because the drill malfunctioned and overheated, there was failure of consideration on CWS's part, rendering the agreement void. Under this section, the burden to prove failure of consideration was borne by D&L. Absent notification of defects, D&L accepted the drill in its condition upon receipt, so the Supreme Court affirmed the trial court's decision that there was sufficient consideration in the contract between the parties. Carl Weissman & Sons, Inc. v. D&L Thomas Equip. Corp., 1998 MT 213, 290 M 433, 963 P2d 1263, 55 St. Rep. 896 (1998).

Agreement to Convey Partnership Property Void for Lack of Consideration — Agreement to Fund and Forbearance in Dissolving Partnership Held Insufficient: Marsha and Mac formed M&M Walkers, a partnership for the breeding, raising, training, and marketing of Tennessee Walker horses. Their partnership agreement was oral and was sealed with a handshake. When Marsha became concerned about the amount of time and money that she was putting into the partnership, Mac executed a written conveyance of his share of partnership property, which said that if anything happened to him, Marsha was to get all the partnership property. After Mac died, Marsha tried to enforce Mac's written statement against his estate, but the District Court held the statement to be invalid for lack of consideration. The Supreme Court held that while the written instrument is presumptive evidence of consideration, that presumption could be rebutted by Mac's estate, which sought to invalidate the statement. Marsha contended that her agreement to continue funding the partnership was sufficient consideration, but the Supreme Court held that because she had a legal duty to contribute to the partnership in accordance with her share of the profits, her "agreement" was not sufficient consideration. Marsha also argued that her forbearance from dissolving the partnership was also sufficient consideration. Citing Rudio v. Yellowstone Merchandising Corp., 200 M 537, 652 P2d 1163 (1982), the Supreme Court noted that it had held that forbearance is sufficient consideration only if there is an agreement to forbear, and in this case, there was no evidence in the record that Marsha had made such an agreement with Mac. The Supreme Court therefore affirmed the District Court's finding that there was insufficient consideration to support Mac's written conveyance of the partnership's property to Marsha. Nitzel v. Wickman, 283 M 304, 940 P2d 451, 54 St. Rep. 684 (1997). See also St. v. Keys, 1999 MT 10, 293 M 81, 973 P2d 812, 56 St. Rep. 44 (1999).

Foregoing Advantage or Benefit — Consideration Found: When the plaintiff refused the Montana Power Company's offer of $35,000 to buy out a power purchase agreement based on the plaintiff's understanding that the defendant would pay the plaintiff $35,000 for rights to develop a power project, the change of the plaintiff's legal position constituted consideration, thus creating a contract. It is not essential that consideration imposes a gain or loss to either party, it is sufficient that a party in whose favor the contract is made foregoes some advantage or benefit. Ragland v. Sheehan, 256 M 322, 846 P2d 1000, 50 St. Rep. 83 (1993). See also Larson v. Green Tree Financial Corp., 1999 MT 157, 295 M 110, 983 P2d 357, 56 St. Rep. 618 (1999).

Receiving Reduced Monthly Benefits After Settlement Not Evidence of Lack of Consideration: The claimant argued that after settling his claim with the State Fund, he received less in monthly benefits than he had prior to settling and that therefore the agreement should be void for lack of consideration. The Supreme Court affirmed the lower court's finding that the claimant had received other consideration, including the fact that after the settlement his benefits would continue to be paid to his estate. Hartfield v. St. Comp. Ins. Fund, 246 M 259, 805 P2d 1293, 47 St. Rep. 2001 (1990).

Promise Supported by Past Consideration Unenforceable: The defendant claimed to have a personal service contract with the plaintiff. The consideration for the contract was past service in assisting the plaintiff in obtaining construction contracts. The Supreme Court found that the contract was unenforceable because it was based upon past consideration. Tindall v. Konitz Contracting, Inc., 240 M 345, 783 P2d 1376, 46 St. Rep. 2182 (1989).

Corporation Owners' Personal Guarantee of Corporation's Contract Obligation: Defendant corporation purchased plaintiff's business under a contract which provided that the inventory of the business would not be reduced in value below the amount still owed plaintiff under the contract. When plaintiff became worried about corporation's plan to carry out such a reduction, the owners of the corporation personally guaranteed payment of that part of the sale price still due plaintiff. There was consideration for the guarantee, in that plaintiff, in return for the guarantee, relinquished various legal rights of action which he would otherwise have had upon reduction of the value of the inventory. Therefore, the guarantee was not void for lack of consideration. Rudio v. Yellowstone Merchandising Corp., 200 M 537, 652 P2d 1163, 39 St. Rep. 1923 (1982), followed, with regard to sufficiency of mutual promises as valid consideration, in Kephart v. Portmann, 259 M 232, 855 P2d 120, 50 St. Rep. 771 (1993).

Promissory Note — Lack of Consideration: Where respondent executed a mortgage and promissory note payable to appellant (the victim of alleged theft by the respondent's son), under belief that the note was to provide for her son's bail bond, and the son was later released on his own recognizance, the court held that the promissory note was unenforceable for lack of consideration. Bartmess v. Bourassa, 196 M 231, 639 P2d 1147, 39 St. Rep. 56 (1982).

Option Agreement — Sufficiency of Consent and Consideration: The defendant appealed from a judgment granting specific performance of an option agreement to the plaintiff and ordering the property involved conveyed to the plaintiff. On appeal, the Supreme Court rejected the defendant's contention that the writing involved was not an option agreement because it failed to meet the essential requirements for the validity of a contract. In particular, he contended that there was a lack of consent and that the consideration was legally insufficient. The Supreme Court found the actual payment of $1 and actual participation in a family corporate dissolution sufficient consideration for the agreement. A memorandum here acted as an offer, and binding agreement resulted from action on that offer by the offeree. The trial court was affirmed. Van Atta v. Schillinger, 191 M 472, 625 P2d 73, 38 St. Rep. 426 (1981).

Workers' Compensation Settlement — Mutual Mistake: Plaintiff injured his back when he fell in the restaurant where he worked and a rack of dishes fell on him. He submitted his claim to the Workers' Compensation Division but was not represented by an attorney. He was examined by physicians who found him to be 5% disabled. Plaintiff entered into a full and final compromise settlement. Later examinations by physicians showed that plaintiff's fall had aggravated his preexisting cerebral palsy condition. This information was not available to either party at the time the settlement was entered into. Both parties were mistaken as to a fact material to the contract. The court found that the need to fairly compensate the injured worker is the intent and purpose of the Workers' Compensation Act. The full and final compromise settlement was set aside for mutual mistake of a material fact as to the nature and extent of the injury caused by claimant's accident. The case was remanded to the Workers' Compensation Court to determine the extent of claimant's disability. Kienas v. Peterson, 191 M 325, 624 P2d 1, 37 St. Rep. 1747

(1980), followed in Kimes v. Pac. Employers Ins. Co., 233 M 175, 759 P2d 986, 45 St. Rep. 1402 (1988), Weldele v. Medley Dev., 227 M 257, 738 P2d 1281, 44 St. Rep. 1062 (1987), and Keller v. Liberty NW., Inc., 2010 MT 279, 358 Mont. 448, 246 P.3d 434.

Counterclaim on Contract — Fulfillment of Preexisting Duties Not Consideration — Effect of Lack of Consideration: Plaintiffs contracted with defendant to build their log home. Before and after occupancy of the home, structural problems requiring repair occurred. At trial, defendant counterclaimed against the plaintiffs for his expenses in installing tie rods in the walls of the home. The plaintiffs had authorized the installation of the tie rods after a windstorm had shown the home to be unstable. Although noting the ratification of the agreement after the rods were installed, the Supreme Court also noted that the home remained unstable and that the rods may have been improperly installed. It said that defendant had a common-law duty to construct the home in a workmanlike manner, in a manner as to assure stability. The duty was not fulfilled even after the installation of the tie rods. Because a promise to perform a preexisting legal or contractual obligation is insufficient consideration for a promise made in return, consideration was lacking in the supplemental (tie rod installation) agreement. Under former Rule 41, M.R.Civ.P. (now superseded), a counterclaim may be dismissed where, upon the facts and the law, the claimant has shown no right to relief. With consideration lacking, the contract was unenforceable and the defendant had no right to relief on his counterclaim. Estoppel will not support the defendant's claim without a showing of detrimental reliance, and it has no application when the omissions of the party claiming estoppel brought about the problem. Carroccia v. Todd, 189 M 172, 615 P2d 225, 37 St. Rep. 1437 (1980), followed in McGregor v. Cushman/Mommer, 220 M 98, 714 P2d 536, 43 St. Rep. 206 (1986).

Lack of Consideration: The court found that a "letter of instruction and joint assignment of funds" was unenforceable because it was not supported by consideration. The issuers, a bank and the purchaser of a modular home, were not bound because no benefit was conferred on them by the plaintiff manufacturer of the home and the plaintiff did not incur any detriment. The consideration recited in the letter was "inducement . . . to begin production" of the home. At the time of the execution of the letter, the home had already been manufactured and delivered to the plaintiff's authorized dealer. No dealings occurred between the plaintiff and the bank; the lending arrangement was rather between the bank and the dealer. Boise Cascade Corp. v. First Sec. Bank of Anaconda, 183 M 378, 600 P2d 173 (1979).

Oral Promise to Pay Insufficient Consideration: A mere oral promise to pay, as in this case, is not sufficient consideration to support a contractual obligation. Such a promise must be binding and impose some legal obligation on the one making it. A contract is not made so long as, in the contemplation of both parties thereto, something remains to be done in order to establish contract relations. Schwedes v. Romain, 179 M 466, 587 P2d 388 (1978).

Contract Barred at Law as in Equity: The legal deficiencies of inadequacy of consideration and lack of consent are equally applicable to bar enforcement of a written contract at law as in equity. Schlegel v. Moorhead, 177 M 456, 582 P2d 336 (1978).

Bills of Sale From Bankruptcy Trustee as Consideration: Bills of sale from a trustee in bankruptcy for a reclaimed ranch and personal property were proper consideration for promissory notes by the persons reclaiming the property. Double X Ranch v. Savage Bros., 167 M 231, 536 P2d 1176 (1975).

Failure of Consideration: In a sharecropper agreement, under which the plaintiff allowed defendant to go upon his land and farm it in return for a share in the crops that were grown, the consideration going from the plaintiff to the defendant tenant was the right whereby he was permitted to go upon the farm and farm it. When plaintiff lost his lease upon the land, the contract terminated, because the existence of such consideration was essential to the existence of the contract and written agreement. White v. Saby, 127 M 241, 260 P2d 1116 (1953).

Valuable Consideration: While consideration is an essential element of a valid contract, the contract here involved is a negotiable instrument, which is deemed prima facie to have been issued for a valuable consideration and to which the signer is deemed to have become a party for value. Alley v. Butte & W. Min. Co., 77 M 477, 251 P 517 (1926).

MISCELLANEOUS

Limitations Period Not Tolled — Agent Discovered Elements of Claim — Late Claim Properly Dismissed: A purchaser of real estate and an interest in a partnership sued the seller, alleging failure to disclose the existence of a reserve oil pit before the sale. The purchaser's claims were time-barred because knowledge of the reserve pit was imputed to the purchaser based on knowledge of the purchaser's agent. The commencement of the period of limitation was when the agent discovered the elements of the claim or cause of action. Summary judgment was proper on the seller's counterclaim for enforcement of the purchase agreement because no issues of material fact existed regarding whether it was a valid contract. Payne v. Hall, 2020 MT 46, 399 Mont. 91, 458 P.3d 1001.

Inmate Death From Alcohol Withdrawal Syndrome — County Not Vicariously Liable for Hospital's Medical Negligence: An inmate died from alcohol withdrawal syndrome while in county police custody after being treated and released by a hospital while he was in custody. The inmate's estate sued the county and the hospital. After the hospital settled with the plaintiff, the plaintiff filed a motion for summary judgment, arguing that the county was vicariously liable for the hospital's medical negligence. The District Court granted the plaintiff's motion, and the county appealed, arguing that it could not be held vicariously liable for the hospital's actions. The Supreme Court reversed, holding that none of the exceptions in Beckman v. Butte-Silver Bow County, 2000 MT 112, 299 Mont. 389, 1 P.3d 348, applied and therefore the county could not be held vicariously liable. The Supreme Court remanded for entry of summary judgment in the county's favor. Stricker v. Blaine County, 2019 MT 280, 398 Mont. 43, 453 P.3d 897.

Promissory Estoppel Does Not Require Showing of Intent to Mislead: The elements of promissory estoppel are distinct from the elements of estoppel by silence. Promissory estoppel does not require a showing of an intent to mislead. S & P Brake Supply, Inc. v. STEMCO LP, 2016 MT 324, 385 Mont. 488, 385 P.3d 567. See also NW. Potato Sales, Inc. v. Beck, 208 Mont. 310, 678 P.2d 1138 (1984), and Turner v. Wells Fargo Bank, N.A., 2012 MT 213, 366 Mont. 285, 291 P.3d 1082.

Waiver of Preemption Defense Pursuant to Settlement Agreement — Terms Enforced: Due to the franchisor motor vehicle manufacturer's bankruptcy restructuring, the petitioner car dealership lost its franchise agreement to a competing car dealership. The petitioner successfully pursued arbitration of its franchise termination under federal law. The franchisor then named the petitioner in a declaratory judgment action in federal court in Detroit. Ultimately, the franchisor and the petitioner entered into a settlement agreement in which the petitioner agreed not to assert the defense that federal law preempted Montana law. When the petitioner later raised the defense in the Montana proceedings, the competing dealership argued the petitioner was barred under the settlement agreement from doing so. The District Court agreed and the petitioner appealed to the Supreme Court. The court affirmed, holding that the petitioner had waived its right to raise the defense by executing the settlement agreement. Rimrock Chrysler, Inc. v. St., 2016 MT 165, 384 Mont. 76, 375 P.3d 392.

No Breach When Defendant Failed to Object to Field Conditions on Inspection: Failure to achieve consistent seed placement did not constitute a material breach under the conditions, and substantial credible evidence supported the court's determination that the defendant met its obligations under the agreement. CNJ Distrib. Corp. v. D&F Farms, Inc., 2013 MT 267, 372 Mont. 28, 309 P.3d 1002.

Purchaser's Failure to Conduct Title Search — Promissory and Equitable Estoppel Properly Denied: A husband and wife took out a line of credit secured by the husband's real property. The couple later decided to sell the property to the husband's brother without the brother conducting a title search. They used the funds from the sale to pay off the line of credit. The bank, however, did not close the account, even though an agent for the bank noted that the payment reflected a "mortgage payoff". Later, and without the husband's knowledge, the wife borrowed $170,000 on the line of credit. The couple subsequently divorced. After the brother learned of the wife's debt and that it was secured by his real property, he filed suit against the bank to release the deed of trust based on the doctrines of promissory and equitable estoppel. The District Court refused to apply either doctrine and the brother appealed. The Supreme Court affirmed, ruling that the brother could not satisfy the elements of either doctrine. Turner v. Wells Fargo Bank, N.A., 2012 MT 213, 366 Mont. 285, 291 P.3d 1082.

Grantor-Support Agreement Implied in Pleadings — Trial Properly Allowed: Defendant children contended that plaintiff parents should not have been allowed to proceed to trial on a grantor-support theory when the parents failed to explicitly raise the theory in the pretrial order. The Supreme Court disagreed. A grantor-support agreement is implied when parents transfer assets to their children in consideration for support. The pretrial order stated that the parents transferred corporate stock to the children as long as the children included the father in corporate decisionmaking and continued to meet the parents' physical and financial needs and asserted that the children breached the agreement. Although the parents did not include the theory in the pretrial order, the elements of the theory were set forth, and the District Court did not err in allowing the parents to proceed to trial Hjartarson v. Hjartarson, 2006 MT 273, 334 M 212, 147 P3d 164 (2006).

Three-Year Statute of Limitations Applicable to Breach of Bailment Obligation: Pursuant to a breach of a bailment agreement related to the transfer of 10 horses and tack, plaintiff filed a claim for the value of the property, asserting that under 27-2-202(2), 5 years were allowed to bring the claim as a breach of contract. The District Court concluded that the voluntary bailment agreement was not a contract, but rather an obligation, which was governed by the 3-year statute of limitations in 27-2-202(3), and because the claim was not brought within 3 years, summary judgment for defendants was appropriate. On appeal, the Supreme Court affirmed. Regardless of the fact that plaintiff characterized the claim as a breach of contract, there was no evidence of an expressed agreement for sale of the property, so defendants were obligated but not contractually required to account for the property. Plaintiff's election to sue on a contract theory did not operate to grant 2 additional years for plaintiff to assert her rights. The District Court's conclusion that plaintiff's action was not timely was correct. Demarest v. Broadhurst, 2004 MT 147, 321 M 470, 92 P3d 1168 (2004).

Engagement Ring Given in Contemplation of Marriage Not Considered Gift — Conditional Gift Analysis: Albinger gave Harris a $29,000 diamond engagement ring when the two promised to marry. The relationship was strained, resulting in breakups and the return of the ring to Albinger several times, but each time the couple reconciled, and the ring was returned to Harris. Following their final separation, Albinger told Harris to "take the car, the horse, the dog, and the ring", so Harris moved to Kentucky, marriage plans evaporated, and Harris refused to return the ring. Albinger filed in District Court to settle ownership of the ring. The District Court found the ring to be a gift in contemplation of marriage, implying that the existence of a condition attached to the gift, and held that Albinger was entitled to return of the ring upon failure of the condition of marriage. Harris appealed, and the Supreme Court reversed. The rights and duties of parties regarding property exchanges in contemplation of marriage are determined by existing law and common-law principles. A gift is a transfer of personal property made voluntarily and without consideration, and the essential elements of an inter vivos gift are donative intent, voluntary delivery, and acceptance by the recipient. Delivery, which manifests the intent of the giver, must turn over dominion and control of the property to the recipient, and when made without condition, such a gift becomes irrevocable upon acceptance, so the Supreme Court will not void the transfer when the giver experiences a change of heart. The only revocable gift recognized under Montana law is a gift in view of death, and a gift causa mortis may be revoked by the giver at any time and is revoked by the giver's recovery from the illness or escape from the peril under which the gift was made. However, the Supreme Court declined to analogize gifts in contemplation of marriage with a gift in contemplation of death. Further, a purported gift that is part of the inducement for an agreement to do or not do a certain thing becomes the consideration essential to contract formation. An exchange of promises creates a contract to marry, albeit an unenforceable one, so when an engagement ring is given as consideration for the promise to marry, a contract is formed and legal action to recover the ring is barred by the abolition of breach of promise actions in 27-1-602. Here, the engagement ring was an unconditional, completed gift upon acceptance, and a completed gift is not revocable. Thus, the ring remained in Harris's ownership and control. Albinger v. Harris, 2002 MT 118, 310 M 27, 48 P3d 711 (2002).

Sale of Property Contingent on Financing — Financing Contingent on Grant of Contract — Oral Agreement to Purchase Additional Property Contingent on Initial Sale — Summary Judgment Proper Absent Genuine Issue of Fact: Community, Counseling, and Correctional Services, Inc. (Community), agreed to purchase Albright's property for a prerelease center. An additional oral agreement provided that Community would also purchase furnishings on the property when the sale was completed. The sale was contingent on Community's ability to obtain financing, and financing was contingent upon a grant for the prerelease center to Community from the Department of Corrections. Ultimately, the Department declined to issue the contract for prerelease services, Community was unable to obtain financing, and Albright was unable to sell the property or furnishings. Albright sued Community for breach of contract. The District Court granted summary judgment to Community, holding that under the plain language of the contract, the offer terminated when the Department did not issue the contract. Albright appealed, but the Supreme Court affirmed. No question of fact existed with respect to the conditions for the agreement because the agreement conditioned formation of any contract to buy the real property on Community's ability to obtain financing and Community could not obtain financing without the Department contract. Further, Albright's own affidavit stated that the oral agreement to purchase the furnishings was contingent on purchase of the property, so no issue of fact existed regarding the sale of the furnishings either, and that issue was also properly disposed of by summary judgment. Albright v. Community, Counseling, & Correctional Serv., Inc., 2001 MT 272, 307 M 289, 37 P3d 675 (2001).

Unenforceability of Buy-Sell Agreement on Grounds of Impossibility or Impracticality of Performance — Requiring Performance of Contract With Potential for Environmental Degradation Unconstitutional: Cape-France Enterprises (Cape-France) entered a buy-sell agreement with Peed (now deceased) and Moore to purchase some property near Bozeman for a subdivision. Before the subdivision could be completed, water needed to be procured for the site. According to the agreement, as buyers, Peed and Moore were responsible to bring water to the property, but because city water was not available, a well needed to be drilled. However, the presence of a pollution plume was discovered near the land. After the subdivision process was commenced, the Department of Environmental Quality notified Cape-France that: (1) the plume may have advanced under the property; (2) a subdivision would not be approved unless a well was drilled and tested; (3) a well could be drilled, but if testing showed pollution in the water, treatment would be extensive; and (4) if drilling or pumping of the water caused expansion of the pollution, then Cape-France, as owner of the property, would be held liable for cleanup costs. On cross-motions for summary judgment, the District Court held that the buy-sell agreement could be rescinded on the basis of mutual mistake of fact and impossibility or impracticality of performance and that specific performance would not be granted. The Supreme Court affirmed. A court may determine that an act is impossible in legal contemplation when it is not practicable, when the act can be done only at an excessive, unreasonable, and unbargained-for cost. The doctrine of impossibility or impracticability is applied when, aside from the object of a contract being unlawful, the public policy underlying the strict performance of the contract is outweighed by the senselessness of requiring performance. The doctrine is not limited to cases of literal impossibility but may also be applied in cases that present a potential for substantial and unbargained-for damages. In this case, requiring Cape-France to go forward with the performance of the contract when there was a very real possibility of substantial environmental degradation and resultant financial liability for cleanup was not in the public interest or in the interests of the contracting parties and was not in accord with the guarantee of a clean and healthful environment in Art. II, sec. 3, Mont. Const., or the mandate to maintain and improve a clean and healthful environment for present and future generations in Art. IX, sec. 1, Mont. Const. Thus, rescission of the contract was proper. Cape-France Enterprises v. Estate of Peed, 2001 MT 139, 305 M 513, 29 P3d 1011 (2001). See also Smith v. Zepp, 173 M 358, 567 P2d 923 (1977), and Mont. Envtl. Information Center v. Dept. of Environmental Quality, 1999 MT 248, 296 M 207, 988 P2d 1236 (1999).

Conflicting Evidence Whether Indemnity Note on Bail Bond Considered Valid Contract — District Court's Finding Not Clearly Erroneous: Rohrich signed an indemnity agreement with Anderson, who owned a bail bond business, to secure a bond posted for the release of Brummer. When signing the indemnity note, Rohrich did not question Anderson about the note and signed it without discussion regarding the effect of his signature. The note provided that should Anderson become liable for the forfeiture of the bail bond, the indemnitor would indemnify Anderson, with interest, and also pay reasonable attorney fees in the event that a suit was necessary to collect the amount owed. Brummer subsequently fled the state, and the County Attorney moved for bail forfeiture. The District Court ordered that judgment in the full amount of bail be entered against Brummer and against Anderson as the surety. After Anderson satisfied the judgment, he waited to see if Rohrich would indemnify him, but Rohrich did not do so; therefore, Anderson brought an action to enforce the indemnity note. At trial, Rohrich maintained that the note was blank when he signed it and that therefore he did not sign a valid contract. Rohrich also contended that the date on the note, which was 1 year after Brummer was released from prison, was further evidence that Anderson did not complete the terms of the note prior to Rohrich's signature. Anderson testified that the note did contain all essential terms when Rohrich signed it, and that testimony was affirmed by Anderson's assistant. Anderson also testified that the date was a typographical error and that as a matter of business practice, he would not provide an indemnitor with a blank note. Further, Rohrich was familiar with indemnity notes, having signed notes on three prior occasions with Anderson, including two that he signed for himself. After weighing the conflicting evidence, the District Court ordered Rohrich to pay the full amount, plus attorney fees, interest, and costs. Rohrich appealed, and the Supreme Court affirmed, paying substantial deference to the trial court because as the factfinder, the trial court was in the best position to evaluate the testimony and judge the credibility of the witnesses. Anderson v. Rohrich, 2001 MT 106, 305 M 274, 26 P3d 99 (2001).

Statement of Present Intent to Perform or Not Perform Not Considered Contract — Lease Not Altered by Gratuitous Promise: Defendants had a 99-year lease on a ranch owned by Earl. The lease provided that in case of need, it was subject to recall on demand by Earl. When Earl had to be placed in a nursing home without the assets to bear her expenses and needed to liquidate the property in order to qualify for federal benefits, defendants were notified that the lease was being terminated. Defendants objected, citing a letter from Earl purporting to gift to them all interest in the ranch. However, to be a gift, a transfer of property must be irrevocable, complete, without adequate or full consideration, and unmistakably intended to divest the donor of title, dominion, and control over the property. The District Court concluded that sufficient need existed to terminate the lease and denied defendants' motion to resolve any effect that the letter had on the original lease. The Supreme Court affirmed, finding that the letter was a mere statement by Earl of present intent to perform or not perform an act in the future and that such a gratuitous promise did not constitute a valid written modification of the original lease. Earl v. Beager, 2001 MT 44, 304 M 258, 20 P3d 788 (2001).

Real Estate Sale — Disclosure Statement Not Susceptible to Violation — Standard Listing Agreement Violation: In an action against a realtor for breach of contract, May alleged violation of both a document entitled "Disclosure Regarding Types of Real Estate Agency Relationships Available" (disclosure statement), listing the duties of a real estate agent, and a "Standard Listing Contract". The Supreme Court held that the disclosure statement was not a contract and could not serve as the basis for a breach of contract action. The Supreme Court also held that the Standard Listing Contract could be violated and that May had sufficiently alleged breach of a specific provision of that contract, that provision being one that the broker was employed to find a buyer ready and willing to acquire the property on the terms stated in the contract, to survive a motion for summary judgment. May v. ERA Landmark Real Estate of Bozeman, 2000 MT 299, 302 M 326, 15 P3d 1179, 57 St. Rep. 1256 (2000).

Broker to Produce Ready, Willing, and Able Buyer to Be Entitled to Commission: Aasheim argued that he was entitled to a commission for the sale of Reum's property on the basis that the failure of the sale being consummated was due to wrongful acts on Reum's part. The Supreme Court held that there was substantial evidence to support the lower court's ruling that the sale was not completed because of the financial inability of the purchaser to close the transaction and therefore Aasheim was not entitled to a broker's commission. Aasheim v. Reum, 277 M 471, 922 P2d 1167, 53 St. Rep. 771 (1996).

Incomplete Form Contract When Signed — Unenforceable Contract: Pearson was responsible for placement of youths in need of supervision (now youth in need of intervention) for Youth Court services and sought to place a youth with Findleys in their foster home. Findley told Pearson that they would need $41 a day to care for the youth and asked Pearson to sign a written contract so that Youth Court services would ensure their $41-a-day payment. Findley produced a form contract with blank spaces for the child's name, name of the contracting party, and rate of compensation for the placement. The extent to which the blanks were filled in was disputed, but Pearson testified that he told the Findleys that he was responsible only for placement, that reimbursement was administered through the Department of Social and Rehabilitation Services (now Department of Public Health and Human Services), and that he could not guarantee a daily payment rate. The Department informed Findleys that the standard daily rate was $11.63. Findleys later brought a claim for contract damages against Youth Court services. The District Court properly held that the form contract was not enforceable because it was substantially incomplete when the parties signed it, with neither the date nor the rate amount having been filled in. There was no evidence that Youth Court services ratified the contract. Equitable estoppel did not apply because Findleys knew within 1 month that they would not be paid $41 a day, but instead of terminating the foster care relationship, they continued for nearly 5 years with no assurance that they would ever receive more than the standard rate for foster care. Findley v. District Court, 277 M 242, 921 P2d 870, 53 St. Rep. 627 (1996).

Oral Estate Settlement Agreement Not Binding: An estate settlement agreement reached by the parties' attorneys over the telephone was not binding on the parties because the agreement was not in writing and was not filed with the Clerk of Court or entered upon the minutes of the court. In re Estate of Goick, 275 M 13, 909 P2d 1165, 53 St. Rep. 12 (1996), overruled, to the extent that a client is not bound to a settlement agreement unless the agreement is filed with the District Court or entered in the court's minutes, in Lockhead v. Weinstein, 2003 MT 360, 319 M 62, 81 P3d 1284 (2003).

Standard Real Estate Buy/Sell Form a Binding Contract: The parties executed a standard form agreement provided by the real estate agent for the sale and purchase of real estate. The agreement contained a clause allowing the buyers to have the home inspected. The buyers informed the sellers that the inspection had raised a few areas of concern that needed to be addressed and negotiated. Ultimately, the sellers refused to change the purchase price or to agree to have any needed repairs made. The buyers then informed the sellers that they were willing to proceed under the terms of the original agreement, at which time the sellers' attorney informed the buyers' attorney in writing that the original agreement was no longer in effect and that the sellers did not intend to sell the property to the buyers. The buyers sued for specific performance. The sellers argued that the agreement was only an option contract and did not constitute a binding buy/sell agreement. The Supreme Court held that the agreement contained the essential elements of a contract and was a binding contract. Klawitter v. Dettmann, 268 M 275, 886 P2d 416, 51 St. Rep. 1296 (1994), following Cady v. Burton, 257 M 529, 851 P2d 1047 (1993), and distinguishing Pollard v. Bozeman, 228 M 176, 741 P2d 776 (1987).

Covenant Limiting Structures to Single-Family Residences Not Restriction of Commercial Use: The McClains argued that the Kannons were violating subdivision covenants by operating a bed and breakfast in their home. The Supreme Court held that a restrictive covenant limiting buildings to single-family residences limited the type of structure and did not limit use of the structure, so that a bed and breakfast operation did not violate the covenant. Patton v. Madison County, 265 M 362, 877 P2d 993, 51 St. Rep. 536 (1994).

Lower Court's Finding of Substituted Contract Reversed: The parties were involved in litigation concerning a development's covenants and informed the District Court that they had reached an agreement conditioned upon approval of the appropriate settlement documents. The lower court subsequently granted summary judgment for one side based upon the oral agreement presented to the District Court. The Supreme Court held that an accord or substitute contract had not been established because there was no unconditional offer, no acceptance, and no meeting of the minds. The proposed settlement was subject to approval of the settlement documents, and they were ultimately not agreed upon by the parties. Patton v. Madison County, 265 M 362, 877 P2d 993, 51 St. Rep. 536 (1994).

Real Estate Sale Not Occurring — Broker Entitled to Commission Based on Terms of Contract: Language in a listing agreement was clear and unambiguous in stating that a broker was entitled to a commission upon procuring a buyer who was "ready and willing to purchase" and who entered into a written agreement to make the purchase. The District Court did not err in granting summary judgment in favor of the broker when the seller was obligated to pay the commission even though the proposed sale did not go through. Sayegusa v. Rogers, 256 M 269, 846 P2d 1005, 50 St. Rep. 89 (1993), followed in Johnson v. Nyhart, 269 M 379, 889 P2d 1170, 52 St. Rep. 37 (1995).

Application of Procuring Cause Doctrine to Exclusive Listing Agreements: The procuring cause doctrine, which permits a broker to show that the broker's part of the contract was performed and that the principal reaped a benefit from the efforts, is not confined to consideration of nonexclusive listing agreements. It applies in all situations unless the parties agree otherwise in the listing contract. Lane v. Smith, 255 M 218, 841 P2d 1143, 49 St. Rep. 974 (1992), clarifying Flinders v. Gilbert, 141 M 442, 378 P2d 385 (1963), and followed in Hall & Hall, Inc. v. Hyde, 264 M 190, 870 P2d 1362, 51 St. Rep. 257 (1994).

Date of Lease-Purchase Agreement as Effective Date of Sale in Determining Broker's Commission: When negotiated within the time parameters of a listing agreement, the date on which a lease-purchase agreement is entered into is the effective date of sale for purposes of determining a broker's commission. Lane v. Smith, 255 M 218, 841 P2d 1143, 49 St. Rep. 974 (1992).

Essential Terms: A letter between landlord and tenant was not an enforceable lease on which the tenant could bring a contract action because it failed to set forth material and essential terms necessary for the enforcement of the renewal provisions of a lease. Therefore, only a month-to-month lease existed. Drug Fair NW. v. Hooper Enterprises, Inc., 226 M 31, 733 P2d 1285, 44 St. Rep. 435 (1987).

Reliance on Insurance Coverage — Elements of Promissory Estoppel Met: Where an insurance company treated son as an insured when it paid prior medical bills and when it represented to a medical center that he was insured, these acts constituted a promise to pay medical bills. Father and son were injured by their reliance on the promise when the company later refused coverage of medical center bills. As reliance was reasonable and foreseeable, these facts constituted ample evidence for a jury finding of promissory estoppel. Tynes v. Bankers Life Co., 224 M 350, 730 P2d 1115, 43 St. Rep. 2243 (1986).

Lack of Appeal of Federal Agency Decision Not to Affect Contract Rights: Popp had an oral agreement to plant and harvest land owned by Frank and Gountanis. Popp attempted to enroll the land in the federal payment in kind program (PIK) but was informed by the Agricultural Stabilization and Conservation Service (ASCS) that he must have a written lease to be eligible. He never appealed the ASCS decision. Frank later contended that the failure to appeal precluded Popp from collaterally attacking that determination in District Court. The Supreme Court held that Popp's filing of a lawsuit was not a collateral attack on the ASCS decision but rather that the amended complaint showed it was a breach of contract action. The court supported the finding that the PIK program could not be used to destroy Popp's contract rights. Popp v. Gountanis, 221 M 267, 718 P2d 340, 43 St. Rep. 801 (1986).

Oral Contract for Purchase of House — Part Performance — Statute of Frauds Inapplicable — No Refund to Purchasers on Default: Defendant agreed to sell home to friends upon a $10,000 downpayment and assumption of defendant's loan. Plaintiffs did not qualify for assumption, so defendant prepared lease for plaintiffs' signature. They refused to sign because it was not a contract for deed. Defendant allowed plaintiffs to take occupancy, and they made sporadic payments for 4 years. Defendant's patience waned when the bank exercised acceleration provision for delinquencies. Plaintiffs sued for refund of payments. The court found an oral contract for deed. The Statute of Frauds was inapplicable because defendant was, at all times, willing to effect sale and transfer of the home. He was not required to refund plaintiffs' payments. Since no lease was ever signed and no rental relationship created, landlord and tenant law was inapplicable. Hayes v. Hartelius, 215 M 391, 697 P2d 1349, 42 St. Rep. 457 (1985).

Public Contract Bid — Submission Binds Bidder: State's solicitation for bids provided that all written addenda would become part of the contract documents, that all bidders would be bound by the addenda, whether or not they were received by the bidder, and that the owner reserved the right to reject all bids and waive any informality or irregularity in any bid. One bid did not acknowledge receipt of certain addenda, though the bidder stated during a phone conversation with the State that he knew of the addenda. The solicitation provisions bound the bidder to full performance of the contract documents, including all addenda, whether received or not, and in submitting its bid the bidder bound itself to the full performance of the contract documents, including the addenda. Martel Constr., Inc. v. Bd. of Examiners, 205 M 332, 668 P2d 222, 40 St. Rep. 1340 (1983).

Effect of Unanticipated Condition on Contractor's Obligation: Even though a contract incorporates by reference federal, state, or local laws, a contractor is not required to alter construction plans to comply with health standards when the condition to be alleviated is abnormal, unanticipated, or substantially different from those in the contract plans and drawings. Ace Plumbing & Heating, Inc. v. School District, 204 M 81, 662 P2d 1327, 40 St. Rep. 678 (1983).

Late Payment — Waiver of Payment Date — Time Not of the Essence: Defendants, on behalf of plaintiff, exercised their option to purchase a ranch, with plaintiff paying $10,000 downpayment required by ranch owner and agreeing to pay defendants $15,000 on November 1 and $15,000 after the following January 1. The timing of the two $15,000 payments was requested by defendants, time was not stated to be of the essence, and there was no forfeiture provision. Plaintiff paid $2,000 on November 2, and defendants accepted it, gave numerous extensions for payment of the remainder of the first $15,000 payment, and did not notify plaintiff that he had a time limit for payment or his interest would be forfeited. Prior to December 12, at least three tenders of payment were refused by defendant, and on that date plaintiff filed suit for specific performance. Defendant could not forfeit plaintiff's interest and waived strict compliance with the payment date. Time was not of the essence, plaintiff's tender was timely, and plaintiff was entitled to specific performance. Stoddard v. Gookin, 203 M 435, 661 P2d 865, 40 St. Rep. 554 (1983).

Grantor Support Agreement Enforceable as Contract: Over a period of years, grantor, a 95-year-old woman, had deeded various parcels of land near her home to several relatives. She filed a complaint against grantees, alleging that the land had been conveyed in return for their promise to support her and that they had failed to live up to their agreement. As relief, grantor sought either damages or, in the event that the agreement was determined to be unenforceable under the Statute of Frauds, return of the land. Grantees denied the existence of any agreement and pleaded the Statute of Limitations as a defense. The District Court granted grantees' motion for summary judgment and further ruled that grantor's claims were barred by the Statute of Limitations. The Supreme Court reversed in part, ruling that grantor was entitled to present evidence on two of her claims because Montana law provides for the enforcement of a grantor support agreement, that there was a genuine issue of fact as to whether or not such an agreement had been made, and that the trial court's ruling on the Statute of Limitations was premature. Additionally, the court ruled that grantor had no claim for return of the land since, if an agreement existed, grantor's partial performance of that agreement rendered the Statute of Frauds inapplicable, and if no agreement existed, grantor was not entitled to any relief. Sands v. Nestegard, 198 M 421, 646 P2d 1189, 39 St. Rep. 1101 (1982).

Existence of Contract — Payment of Tort Judgment as Precluding Determination: Plaintiffs sued defendant for damages claimed to have occurred to their farmlands when a seismograph hole drilled and shot by defendant brought a continuous water flow to the surface, damaging farmland. Defendants left the area and later tried unsuccessfully to plug the hole. The jury found for plaintiffs and awarded actual and punitive damages. Defendant paid the award for actual damages and appealed the award of punitive damages. Defendant claimed the case involved a contract and that punitive damages were not properly allowable. By satisfying the judgment for actual damages, defendant acceded to the correctness of the judgment and accepted its benefits. When a judgment is paid, it passes beyond the review of a superior court. The question of whether a contract existed was submitted to the jury. Their judgment was based on a tort theory, comparative negligence. Because this judgment was satisfied, the Supreme Court could not rule on whether a contract was involved. Dahl v. Petroleum Geophysical Co., 194 M 294, 632 P2d 1136, 38 St. Rep. 1474 (1981).

Contract by Promissory Estoppel — Requirements of Promise: In an action involving a pump delivered and set up by plaintiff, based upon a phone conversation mentioning only "prevailing rates", followed 6 days later by a written agreement prepared by plaintiff and signed by both parties, detailing specific rates and terms such as duration, maintenance, fuel, and accessories, defendant could not rely upon the doctrine of promissory estoppel to create a contract from the transaction prior to the written agreement. Citing section 90, Restatement of Contracts, the Supreme Court found that the need for a promise clear and unambiguous in its terms was not met. The earlier transaction was a mere agreement to agree at a further date (i.e., negotiation), lacking specifics such as those in the written agreement, and hence there was no valid contract prior to the written agreement. Keil v. Glacier Park, Inc., 188 M 455, 614 P2d 502, 37 St. Rep. 1151 (1980), followed in Keesun Partners v. Ferdig Oil Co., Inc., 249 M 331, 816 P2d 417, 48 St. Rep. 710 (1991). See also Turner v. Wells Fargo Bank, N.A., 2012 MT 213, 366 Mont. 285, 291 P.3d 1082.

Attempted Assignment of Void Option Agreement — Judicial Notice: The District Court did not err in finding appellant was not entitled to exercise an option, which had been assigned to appellant, because the original option agreement between the respondent and the assignor was void. The District Court could take judicial notice of a separate action that had determined the invalidity of the option agreement at the time of the attempted assignment, and there was sufficient independent evidence that the option agreement was void. Berry v. Mann, 188 M 71, 610 P2d 1180 (1980).

28-2-103. Express versus implied contracts.

Case Notes

Express Contracts 116
Implied Contracts 117
Miscellaneous 118

EXPRESS CONTRACTS

Proper Quantum for Architect's Services: Under a contract with a landowner who wished to build housing units on the land, an architect prepared plans and specifications that were approved by landowner. Under the contract, the architect was to receive 5% of the construction cost. Following abandonment of the project, he was entitled to a fee based on quantum meruit. The proper recovery was the number of hours of service, 600, times the architect's hourly rate, $30, or $18,000. It was improper for the court to hold that the architect was entitled to only $10,000 based on the value of his services. Kenneth D. Collins Agency v. Hagerott, 211 M 303, 684 P2d 487, 41 St. Rep. 1375 (1984).

Quantum Meruit: One having an express contract which he has performed may sue in quantum meruit and use the contract as proof of the reasonable value of his services; however, it is a fatal variance to allege an implied contract (quantum meruit) and to prove an express contract except where full performance of the contract was prevented by the defendant. Here, plaintiff is not entitled to a remedy in quantum meruit because he has not been prevented from full performance, since under the termination provisions he has no enforceable contract to continue employment. Keneally v. Orgain, 186 M 1, 606 P2d 127 (1980).

Special Agreement Overrides Implied Contract: The law will not imply a promise to pay the value of services rendered and accepted if there is a special agreement to pay a particular amount or in a particular manner for the service rendered. St. James Community Hosp., Inc. v. Dept. of Social and Rehabilitation Services, 182 M 80, 595 P2d 379 (1979).

IMPLIED CONTRACTS

Sufficient Evidence of Implied Contract to Preclude Summary Judgment — City Ordinance Not Bar to Liability: The plaintiffs sued the city of Dillon for damages after their water service was interrupted, claiming breach of contract, negligence, and infliction of emotional distress. The District Court granted summary judgment to the city, reasoning that no contract existed between the parties because the city commission never approved a contract for the plaintiffs' water service, as required by a city ordinance, and the plaintiffs' claims were barred by a city ordinance that provided that the city could shut off water and avoid liability for the resulting interruption of water service. The Supreme Court reversed. The city's conduct manifested the existence of a contract to furnish water to the plaintiffs' lot, and therefore the city was estopped from asserting that no contract existed. Because the city ordinance that bars claims arising from a break in water service applies only to situations in which the city decides to shut off water services, rather than when water is shut off from a creek and main line freezing as occurred in this case, summary judgment for the city was not appropriate. Conner v. Dillon, 2012 MT 21, 364 Mont. 8, 270 P.3d 75.

Promissory Note Enforceable: A promissory note from husband to wife acknowledging that he owed her for a loan that she obtained for him and that was secured by her home is enforceable as an implied contract at law in a dissolution proceeding. In re Marriage of Rock, 257 M 476, 850 P2d 296, 50 St. Rep. 369 (1993).

Implied Contract — Test: The elements required to establish an implied contract, as set out in Daniels v. Thomas, Dean & Hoskins, Inc., 246 M 125, 804 P2d 359 (1990), are: (1) identifiable parties; (2) consent; (3) a lawful object; and (4) consideration. Presence of all elements constituted sufficient evidence to establish an implied contract. CB&F Dev. Corp. v. Culbertson St. Bank, 256 M 1, 844 P2d 5, 49 St. Rep. 1122 (1992).

Law of Implied Contract as Applied to Grazing Fees: In a dispute between two brothers as to the amount owing for grazing fees, John contended that because there was never any agreement with Glenn that rent would be charged for three horses kept with his cattle, no charges could be made for grazing the horses. The Supreme Court applied the law of implied contracts in holding that John should be required to pay Glenn for the pasturing of the horses after Glenn told John to either pay for their grazing or remove them. Heitz v. Heitz, 244 M 12, 795 P2d 486, 47 St. Rep. 1393 (1990).

Insufficient Evidence to Imply Contract: Defendant bank and plaintiffs loaned money to purchasers of restaurant. When bank accelerated the note due from the purchasers and sold the restaurant's assets, plaintiffs claimed breach of an implied contract between bank and themselves. Letter from bank to plaintiffs did not establish implied contract but merely an attempt by the bank to collect a loan from one of the plaintiffs. Lythgoe v. First Sec. Bank of Helena, 222 M 163, 720 P2d 1184, 43 St. Rep. 1140 (1986).

Value of Completed Implied Contract Proved by Value of Completed Express Contract: Where the defendant property owner made an agreement with the plaintiff photographer in May for aerial photos of two parcels of property after receiving an estimate for those services and in October directed the plaintiff to proceed with photographing two other sites as well, the District Court erred in holding that proof of the later agreement, an implied contract, could not be introduced as it was at variance with the first agreement, an express contract. It is fatal to allege an implied contract and prove an express one, but what the defendant attempted to do was prove the value of an implied contract by introducing proof of the express contract. The District Court's limitation on the plaintiff's recovery was in error. Survco v. Kenyon Noble Ready-Mix, 204 M 411, 664 P2d 943, 40 St. Rep. 971 (1983).

Union Contract as Implied Part of Employment Relationship: Bishop was hired by petitioner to be head of his wine department. The specifics of the employment were not discussed. Bishop was given a copy of a union contract covering other employees although he was not a union member. After his discharge, Bishop filed a wage claim with the Department of Labor and Industry. The hearings officer found the union contract to be the best indicator of the employment relationship and awarded back wages. The District Court reversed, saying there was no mutual consent as to overtime or holiday pay. On appeal, the Supreme Court reinstated the hearing officer's findings because they were supported by substantial evidence. There were a number of correlations between the parties' actual conduct and the union contract. The union contract was held to be an implied part of the employment relationship between Bishop and the petitioner. Bronken's Goodtime Co. v. Bishop, 201 M 360, 664 P2d 292, 39 St. Rep. 2165 (1982).

Witness Testimony — Substantial Evidence to Support Implied Fee Agreement: The trial court's determination that an oral agreement was entered into between the parties but that no express agreement was reached as to the fee to be paid plaintiff for architectural services and that there was an implied agreement at law to pay the reasonable value of those services was supported by substantial evidence. Most of the evidence consisted of witness testimony, and where the credibility of the witnesses is of prime importance, the determination of weight given to testimony is the primary function of the trial judge sitting without a jury. Knight & Co. v. Manaras, 184 M 448, 603 P2d 675 (1979).

Implied Contract — Medicaid Payments: The principle underlying the implied contract doctrine is that one person should not be permitted to be unjustly enriched at the expense of another but should be required to make restitution for property or benefits received where it is just and equitable that such restitution be made and where such action involves no violation or frustration of law or opposition to public policy, either directly or indirectly. The circumstances on the record do not justify payment be made on any formula other than the "reasonable costs" formula as set forth in federal Medicaid statutes and regulations. Flathead Health Center v. Flathead County, 183 M 211, 598 P2d 1111 (1979).

Employee Status Based on Implied Contract: A husband and wife who were working as managers of a bar under an express contract for money remaining from bar revenues after operating and fixed costs were paid became employees for purposes of a suit for wages under 39-3-214 when they stayed on as managers because of representations by the agent of the corporate defendant that gave rise to an implied contract for reasonable compensation that revoked the express contract. McNulty v. Bewley Corp., 182 M 260, 596 P2d 474 (1979).

Service Contract: Evidence that it was understood plaintiff should be paid for her services and that plaintiff maintained a detailed record of services and expenses, even though including contrary indications, was sufficient under this section to support plaintiff's claim under an implied contract. Cartwright v. Joyce, 155 M 478, 473 P2d 515 (1970).

Implied Contract — Defined: An implied contract is one the terms and existence of which are manifested by the conduct of the parties; the element of consideration for such a contract is furnished by the benefit conferred upon the promisor and the prejudice suffered by the promisee, and the element of intention on the part of the former may be furnished by his conduct and declarations. Erie v. Wahl, 116 M 515, 155 P2d 201 (1945); Rentfro v. Dettwiler, 95 M 391, 26 P2d 992 (1933).

Creation by Law: Contracts implied by law, or quasi or constructive contracts, are a class of obligations which are imposed or created by laws without regard to the assent of the party bound, on the ground that they are dictated by reason and justice, and may be enforced by an action ex contractu. French v. County of Lewis & Clark, 87 M 448, 288 P 455 (1930).

One Signator: A contract which is signed by only one party but which is acted upon by the other party is binding on both. Steinbrenner v. Minot Auto Co., 56 M 27, 180 P 729 (1919).

MISCELLANEOUS

Surrogacy Contract — Express Written Contract Limited to Clear and Unambiguous Terms — Contract Did Not Preclude Subsequent Establishment of Parental Interest Under Montana Law Not Based on Fact of Surrogacy. Sayler v. Yan Sun, 2023 MT 175, 413 Mont. 303, 536 P.3d 399.

Dispute Over Contract to Deliver Log Home — No Requirement That Seller Provide Name of Third Party Boom Truck Operator — Rescission Proper Remedy for Material Breach of Contract: Anderson agreed to purchase a log home from Eschenbacher. The home was designed to be constructed on Anderson's homesite. Eschenbacher drafted the purchase contract, which provided that Eschenbacher would act only as a manufacturer, not as a building contractor, and also required Anderson to coordinate and ensure availability of a boom truck to assemble the structure at the site. Anderson contacted a third party to supply a boom truck instead of using Eschenbacher's truck. Eschenbacher then refused to deliver the logs unless Anderson supplied the name of the other boom truck operator. Both parties sued for breach of contract. The District Court concluded that Anderson was under no duty to provide Eschenbacher with the name of the boom truck operator, and the Supreme Court agreed. The contract clearly placed the responsibility for acquiring a boom truck with Anderson, but did not require Eschenbacher to use it, because other language required Anderson to pay any expenses incurred by Eschenbacher for waiting once the logs were delivered, if, for instance, the boom truck that Anderson provided was inadequate. Construing the contract most strongly against the drafter, Eschenbacher, the court found that Eschenbacher could easily have inserted provisions in the contract regarding specifications of an adequate boom truck, but he did not. Eschenbacher materially breached the contract by refusing to deliver the logs until the boom truck dispute was settled. The contract did not specify a remedy; thus, the District Court did not err in granting Anderson rescission of the contract. Eschenbacher v. Anderson, 2001 MT 206, 306 M 321, 34 P3d 87 (2001).

Limited Agreement Not to Prosecute for Deviate Sexual Conduct — Not Grant of Statutory Immunity — Independently Derived Evidence Applicable: The Jefferson County Attorney contractually agreed not to prosecute Myrhow for criminal acts related to an investigation of deviate sexual conduct by Marks, of which Myrhow had knowledge. However, until other incidents came to light as part of a separate investigation, Myrhow at no time related that he was involved in other unrelated incidents of deviate sexual conduct, including an incident committed prior to the contractual agreement. Myrhow contended that the immunity granted for his information regarding Marks's conduct also extended to his own conduct. The District Court properly found that Myrhow had been granted de facto immunity from prosecution for acts directly related to the Marks investigation, but that immunity was a limited, contractual, transactional immunity arising solely from the agreement not to prosecute, rather than from 46-15-331. The statutory immunity provided by 46-15-331 did not apply because that immunity is granted only when a witness is compelled to testify by court order, a circumstance inapplicable to this case. Because the evidence used to convict Myrhow was derived independently of the Marks investigation and independently of any immunized evidence Myrhow provided through his agreement with the County Attorney, the District Court correctly convicted Myrhow for deviate sexual conduct committed prior to the immunity agreement. St. v. Myrhow, 262 M 229, 865 P2d 231, 50 St. Rep. 1528 (1993).

Accountant's Duty Based on Whether Employment Contract Express or Implied: The defendant argued that only an implied contract had existed between it and the plaintiff and therefore its duty to the plaintiff was defined by its conduct toward the plaintiff and the plaintiff's acceptance of that conduct. The Supreme Court held that although the duty of an accountant may vary depending on whether a contract is express or implied, the jury's factual determination that the defendant had breached its duty made the distinction irrelevant. Billings Clinic v. Peat Marwick Main & Co., 244 M 324, 797 P2d 899, 47 St. Rep. 1464 (1990).

Unjust Enrichment — Misconduct by Defendant Required — Denial of Restitution to Defaulting Purchaser: Upon default by purchasers, seller resold the property. Purchasers sought restitution, contending it was unfair to allow seller to be unjustly enriched by selling the property twice. However, restitution is normally denied to a defaulting purchaser. (See Contract Damages in Montana Part II: Reliance and Restitution, Burnham, 45 Mont. L. Rev. 1 (1984).) Further, in order for the equitable doctrine of unjust enrichment to apply, plaintiff must show some element of misconduct or fault on the part of defendant. Schweigert v. Fowler, 240 M 424, 784 P2d 405, 47 St. Rep. 1 (1990). See also Owen v. Skramovsky, 2013 MT 348, 372 Mont. 531, 313 P.3d 205.

Parties' Dealings Creating Neither Express nor Implied Contract: The plaintiffs argued that the dealings between themselves and the bank showed the existence of either an express or implied contract, requiring the bank to make the necessary loans to finance the plaintiffs' farming operation. The Supreme Court held that no agreement existed between the parties that obligated the bank to continue to make loans to the plaintiffs. The court went on to say that a series of promissory notes had been entered into by the parties and that under the doctrine of merger, even if the bank had made any oral representations, those representations would merge with the terms of the notes that would then represent the contract reached by the parties. Blome v. First Nat'l Bank of Miles City, 238 M 181, 776 P2d 525, 46 St. Rep. 1186 (1989).

Use of Plats to Induce Purchasers: In order to sell lots, a subdivider prepared and recorded subdivision plat maps that designated common areas and roadways. The purchase and sale contracts did not state who would construct roads or common areas. The issue of whether purchasers of lots have any legally enforceable right to have roads constructed depends not on their designation in the plats but on the subdivider's use of the plats in inducing purchasers. The instruments in question do not comprise a promise, express or implied, to construct roads. The purchasers did acquire an easement for the designated use. The case was remanded to determine factual issues relating to the use of the plats in inducing purchasers. Majers v. Shining Mtns., 219 M 366, 711 P2d 1375, 43 St. Rep. 16 (1986).

Unjust Enrichment Measure of Damages — Quantum Meruit or Value of Enhancement to Land: Where the plaintiffs failed to make a final payment to the defendant under a lease of property upon which the plaintiffs expended considerable time and effort to grow wheat and the defendant wrongfully terminated the lease, the District Court erred in awarding damages to the plaintiffs consisting of a composite of enhanced land value, custom work, fixed costs, and/or crop value. The measure of damages for unjust enrichment is either the quantum meruit value of the plaintiffs' labor or the value of the enhancement to the defendant's property, whichever is greater. In this case the total unjust enrichment as measured by the enhancement to the defendant's property was more than the quantum meruit measure of unjust enrichment, but both measures of damages cannot be used. The damages awarded to the plaintiffs were therefore reduced. Robertus v. Candee, 205 M 403, 670 P2d 540, 40 St. Rep. 1391 (1983), followed in Storms v. Bergsieker, 254 M 130, 835 P2d 738, 49 St. Rep. 655 (1992).

Valuation of Plaintiffs' Work in Unjust Enrichment Claim — Substantial Evidence Found: Where the plaintiffs brought an action for damages against the defendant on the theory of unjust enrichment of the defendant by the plaintiffs' work in breaking and planting land leased to them by the defendant, the Supreme Court found that there was substantial evidence to support the District Court's valuation of the plaintiffs' groundbreaking work. The trial court properly considered the plaintiffs' expert testimony and exhibits, which were based on assumptions in evidence, and properly considered the profit margin included in the plaintiffs' calculations. Under the rationale of Cameron v. Cameron, 179 M 219, 587 P2d 939 (1978), the court refused to disturb the District Court findings because they were based on substantial, though conflicting, evidence. Robertus v. Candee, 205 M 403, 670 P2d 540, 40 St. Rep. 1391 (1983).

Conduct and Declarations: The intention of the parties to a contract may be furnished by their conduct and declarations. Stensvad v. Miners & Merchants Bank of Roundup, 196 M 193, 640 P2d 1303, 39 St. Rep. 27 (1982).

Existence of Contract — Payment of Tort Judgment as Precluding Determination: Plaintiffs sued defendant for damages claimed to have occurred to their farmlands when a seismograph hole drilled and shot by defendant brought a continuous water flow to the surface, damaging farmland. Defendants left the area and later tried unsuccessfully to plug the hole. The jury found for plaintiffs and awarded actual and punitive damages. Defendant paid the award for actual damages and appealed the award of punitive damages. Defendant claimed the case involved a contract and that punitive damages were not properly allowable. By satisfying the judgment for actual damages, defendant acceded to the correctness of the judgment and accepted its benefits. When a judgment is paid, it passes beyond the review of a superior court. The question of whether a contract existed was submitted to the jury. Their judgment was based on a tort theory, comparative negligence. Because this judgment was satisfied, the Supreme Court could not rule on whether a contract was involved. Dahl v. Petroleum Geophysical Co., 194 M 294, 632 P2d 1136, 38 St. Rep. 1474 (1981).

No Express or Implied Contract — Same Subject: There cannot be an express and implied contract for the same thing existing at the same time. It is only when parties do not expressly agree that the law imposes and raises a promise. No agreement can be implied where there is an express one existing. McNulty v. Bewley Corp., 182 M 260, 596 P2d 474 (1979), following Keith v. Kottas, 119 M 98, 172 P2d 306 (1946).

Bank Deposit: Where a special administratrix had a deposit as such in a bank, and another, claiming to have been appointed special administrator, made demand on the bank for the payment of the deposit, and the bank notified the depositor of the demand and was requested to refuse the demand and retain the deposit in the depositor's name, thereupon the demandant sued the bank. After the removal of the depositor, demandant recovered judgment against the bank for the deposit and interest from the date of the demand. The depositor was not liable to the bank for the interest, since there was no implied contract to indemnify the bank. Murphy v. Nett, 51 M 82, 149 P 713 (1915).

28-2-104. Executed versus executory contracts.

Case Notes

Surrogacy Contract Terminated by Its Own Terms on Surrogate's Relinquishment of Child. Sayler v. Yan Sun, 2023 MT 175, 413 Mont. 303, 536 P.3d 399.

Executed Oral Agreement — Meeting of Minds Required: The parties entered into an agreement for the lease of a truck. The lease agreement contained a noncancellation provision and provided alternative remedies to the lessor in the event of a default. Lessee returned the truck with current payments to lessor prior to the termination date of the lease. Lessor had to make repairs to the truck. Lessee contended the return was a fully executed oral contract to terminate the lease. Lessor contended that termination was dependent on the condition of the truck. There was substantial evidence to support the finding that there was no meeting of the minds and therefore no agreement to terminate the lease. Diede v. Davis, 203 M 205, 661 P2d 838, 40 St. Rep. 394 (1983).

Oral Modification of Written Property Settlement — Effect on Debts: An alleged oral modification of a written property settlement agreement could not have the effect of altering a written agreement to repay a loan made to spouses prior to divorce. Thus, payment by one obligor (purportedly in the form of a loan to the obligee) of part of the balance was considered as a discharge of the other obligor's obligation to pay that portion. Davidson v. Lewis, 177 M 55, 579 P2d 762 (1978).

Revocation of Executory Contract: Parol contracts for the sale of growing timber do not convey an interest in the land, but are executory contracts for the sale of the timber after severance, together with a license to cut and remove the timber, and while such license is irrevocable as to that part of timber which has been severed it remains executory as to timber not yet severed, and is revocable at the will of the owner, by his death, or his conveyance of the land without reservation. Gullicksen v. Shadoan, 124 M 56, 218 P2d 714, 18 ALR 2d 1142 (1950).

Executed Oral Agreement:

An oral agreement altering a written agreement is not an executed oral agreement within the statute authorizing modification of a written contract by an executed oral agreement unless its terms have been fully performed, and performance on one side is not sufficient. Ikovich v. Silver Bow Motor Car Co., 117 M 268, 157 P2d 785 (1945).

In an action to foreclose a chattel mortgage securing some promissory notes, in which the defense was that the maturity of the notes had been extended 2 years by an executed oral agreement and payment of $1,000 in consideration of that agreement, immediately upon payment of that consideration, the agreement became fully executed and effective to modify the written contract of the parties. Griffiths v. Thrasher, 95 M 210, 26 P2d 995 (1933).

Contract Partially Executed and Executory: An executory contract conveys a chose in action, while an executed contract conveys a chose in possession. A contract may be partly executed and partly executory and may be executory as to one party and executed as to the other. Lewis v. Lambros, 58 M 555, 194 P 152 (1920).

Part 2
Parties

Part Case Notes

Prior Incorrect Surveys — Plaintiffs Not Intended Third-Party Beneficiaries to Contract — No Standing to Sue for Breach: Plaintiffs sued a surveying company and its owner for misrepresenting the boundaries of their property. They alleged that they had met with an employee of the surveying company prior to buying the parcel and he told them that the property consisted of waterfront property. Relying on his information, the plaintiffs purchased the parcel and built a structure on property belonging to a neighboring landowner. The plaintiffs sued for breach of contract and negligent misrepresentation. The plaintiffs successfully argued to the District Court they were third-party beneficiaries to at least one of two prior surveys performed by the surveying company for previous land owners. On appeal, however, the Supreme Court disagreed, concluding that the plaintiffs were incidental beneficiaries who were not specifically contemplated at the time the prior surveys were completed. Because they were strangers to the contracts, they lacked standing to sue for breach of contract. Kurtzenacker v. Davis Surveying, Inc., 2012 MT 105, 365 Mont. 71, 278 P.3d 1002. See also St. John v. Lewistown, 2017 MT 126, 387 Mont. 444, 395 P.3d 486.

Shareholder Cannot File Claim Belonging to Corporation — Stranger to Contract — No Standing to Seek Damages — Summary Judgment Affirmed: A majority shareholder of a corporation filed suit for damages arising from the termination of the corporation's food services contract with the federal government against the defendants who sold a coffee urn for the corporation's use. The District Court properly granted summary judgment in favor of the defendants because the shareholder did not have standing to file claims that belonged to the corporation; he was not a party to the contract between the corporation and the federal government; and the deadline to amend his pleadings to include the corporation as a party had expired. Weaver v. Advanced Refrigeration, 2011 MT 174, 361 Mont. 233, 257 P.3d 378.

Lack of Standing of Stranger to Contract to Bring Action to Enforce Contract: A stranger to a contract who is not an intended third-party beneficiary lacks standing to bring an action based on a violation of the contract, including compliance with the statute of frauds. Palmer v. Bahm, 2006 MT 29, 331 M 105, 128 P3d 1031 (2006), followed in Dick Anderson Constr., Inc. v. Monroe Constr. Co., LLC, 2009 MT 416, 353 M 534, 221 P3d 675 (2009). See also Ludwig v. Spoklie, 280

M 315, 930 P2d 56 (1996), Kurtzenacker v. Davis Surveying, Inc., 2012 MT 105, 365 Mont. 71, 278 P.3d 1002, and Turner v. Wells Fargo Bank, N.A., 2012 MT 213, 366 Mont. 285, 291 P.3d 1082.

Corporation Considered Real Party in Interest on Claim for Lost Corporate Profits — No Exception for S. Corporations: Gullett paid $10,000 earnest money for the purchase of real property. The money was drawn on the account of Gullett's corporation. When defendants refused to return the money after the purchase agreement failed, Gullett filed a complaint for return of the money and for profits allegedly suffered by the corporation's business through lack of the funds. Although the money was ultimately repaid to Gullett, the District Court summarily dismissed the claim for lost business profits on grounds that the corporation, not Gullett, was the real party in interest. On appeal, the Supreme Court affirmed. The cause of action for recovery of lost business profits belonged to the corporation, not to a shareholder. Gullett's argument that he should not be barred from the claim because the corporation was an S. corporation also failed because even though an S. corporation is treated differently for taxation purposes, it remains a corporation in all other ways, and the corporation and its shareholders remain separate entities. Gullett v. Van Dyke Constr. Co., 2005 MT 105, 327 M 30, 111 P3d 220 (2005), following Richland Nat'l Bank & Trust v. Swenson, 249 M 410, 816 P2d 1045 (1991), and followed in Cleveland v. Ward, 2016 MT 10, 382 Mont. 118, 364 P.3d 1250. See also Smith Setzer & Sons, Inc. v. S.C. Procurement Review Panel, 20 F3d 1311 (4th Cir. 1994).

No Duty of Care Absent Relationship Between Plaintiff and Insurance Agent: Seal sold saddles and tack to Hart. Hart was to procure insurance on the goods to protect against casualty loss and theft, so Hart contracted with a South Dakota insurance agent for property insurance. Seal was not named in the policy as a loss payee. The goods were subsequently stolen, but the insurer refused to pay on grounds that Hart was not a common carrier and, as owner of the property, was not hauling the property of another. Seal sued the insurance agent for breach of contract and failure to procure insurance on Seal's behalf. The District Court concluded that Seal did not contract with the agent to insure any person, property, or risk in Montana, so no relationship existed between the parties to establish a duty on the agent's behalf to procure insurance for Seal. The Supreme Court affirmed. The question of duty is a problem of the relationship between individuals that imposes upon one a legal obligation for the benefit of the other. Here, the only conversations regarding the procurement of insurance occurred between Hart and the agent. Seal never contacted the agent, so no relationship existed between Seal and the agent that gave rise to a corresponding duty to allow Seal to recover on the claim. The certificate of insurance alone did not constitute a contract to procure insurance or impose a duty on the certificate issuer to procure insurance. Seal v. Hart, 2002 MT 149, 310 M 307, 50 P3d 522 (2002). See also Lu-An-Do, Inc. v. Kloots, 721 NE 2d 507 (Ohio Ct. App. 1999).

No Authority to Contract — Contract Not to Be Ratified or Enforced: Defendants entered into an installment contract to buy land from plaintiffs. The contract was entered by directors of the corporation acting without authority who were defrauding the corporation at the time. When the rightful stockholders came into control, they brought an action to nullify the contract and were awarded summary judgment. Defendant contends that by its actions, plaintiff ratified the contract. A contract entered into without the power to contract cannot be ratified or enforced, and the incapacity to contract cannot be removed by estoppel. Larry C. Iverson, Inc. v. Bouma, 195 M 351, 639 P2d 47, 38 St. Rep. 1911 (1981).

28-2-201. Who may contract.

Case Notes

Surviving Spouse's Agreement to Sell Daughter's Interest in Decedent's Business Invalid: The surviving spouse entered into an agreement to sell her daughter's interest in the decedent's business. The Supreme Court held that the contract was void at its inception because it was prior to the surviving spouse being appointed conservator for her minor daughter and that therefore she had no authority to act on behalf of her child. In re Estate of Griffin, 248 M 472, 812 P2d 1256, 48 St. Rep. 517 (1991).

Workers' Compensation — Disaffirmation of Settlement Agreement by Minor: A minor was injured while working and filed for workers' compensation benefits. He subsequently signed a settlement agreement after negotiating with a claims adjuster. The claimant's filing of a petition to reopen his claim resulted in a hearing and the conclusion that the case was closed. The claimant appealed, based on his minority status at the time of the settlement and his concomitant right to disaffirm contracts. The Supreme Court held that the close relationship and continuing awareness of the claimant's mother during the claims negotiations were of no avail to the defendants because only the minor claimant had signed the settlement. The defendant should have required the claimant's legal guardian to sign as well as the claimant. Accordingly, the final compromise settlement was set aside. Parrent v. Midway Toyota, 192 M 118, 626 P2d 848, 38 St. Rep. 559 (1981).

Annulment of Marriage Contract: To justify annulment of a marriage contract because of mental incompetency of one of the parties, there must be clear and convincing proof that the party was incompetent at the time the contract was entered into. Murphy v. La Chapelle, 95 M 36, 24 P2d 131 (1933).

28-2-202. Contracts of persons entirely without understanding.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Validity of Contract: Contract made with person who is entirely without understanding is void ab initio, while one made with person of unsound mind "but not entirely without understanding" is voidable only at suit of one seeking to rescind on one of grounds mentioned in laws on rescission. Fleming v. Consol. Motor Sales Co., 74 M 245, 240 P 376 (1925).

Restoration of Consideration: Where plaintiff based her action on ground that deceased grantor did not have capacity to make a contract under this section, and not on ground that she was entitled to rescind under 28-2-203, an allegation that she had restored or offered to restore everything of value deceased had received from defendant was not required. Kiley v. Danahey, 61 M 608, 202 P 1110 (1921).

Overpowering Will of Grantee: In action by administratrix to set aside deed on ground that when her intestate executed it she was without understanding sufficient to make a valid contract, complaint was examined and held sufficient to permit of proof from which inference could properly be drawn that grantor in putting her cross to and delivering the deed acted in obedience to the overpowering will of grantee. Kiley v. Danahey, 61 M 608, 202 P 1110 (1921).

28-2-203. Contracts of persons with limited understanding.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

Case Notes

Modification Proper Despite Wife's Limited Capacity: After the parties' divorce, the husband, Arthur, was given an opportunity to retire early from the railroad. He contacted his ex-wife, Shirley, and the parties modified the divorce settlement to allow him to take early retirement. At the hearing to modify the decree, Shirley's attorney argued that the modification was inequitable and that Shirley had been diagnosed with a schizoaffective disorder so that she was unable to give an informed consent to the modification. The Supreme Court held that the evidence indicated that Shirley was better off under the new agreement and that the evidence also showed that the modification negotiations between the parties were amiable and that Shirley had consulted with her adult children and parents prior to signing the agreement. In re Marriage of Brownell, 263 M 78, 865 P2d 307, 50 St. Rep. 1714 (1993).

Undue Influence: Where defendant in an action on a note pleaded in defense undue influence and lack of consideration, and in addition relied upon this section, the fact that he did not proceed to have the note rescinded after evidence was found insufficient to warrant a verdict in his favor as to undue influence and lack of consideration was immaterial. Stagg v. Stagg, 96 M 573, 32 P2d 856 (1934).

Validity of Contract: Contract made with person entirely without understanding is void ab initio under 28-2-202, while one made with person of unsound mind "but not entirely without understanding" is voidable only at suit of one seeking to rescind on one of grounds mentioned in laws on rescission. Fleming v. Consol. Motor Sales Co., 74 M 245, 240 P 376 (1925).

Restoration of Consideration: Where plaintiff based her action on ground that deceased grantor did not have capacity to make a contract under 28-2-202, and not on ground that she was entitled to rescind under this section, an allegation that she had restored or offered to restore everything of value deceased had received from defendant was not required. Kiley v. Danahey, 61 M 608, 202 P 1110 (1921).

28-2-204. When person of unsound mind cannot disaffirm contract.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

28-2-205. When contract for benefit of third person may be enforced by third person.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Prior Incorrect Surveys — Plaintiffs Not Intended Third-Party Beneficiaries to Contract — No Standing to Sue for Breach: Plaintiffs sued a surveying company and its owner for misrepresenting the boundaries of their property. They alleged that they had met with an employee of the surveying company prior to buying the parcel and he told them that the property consisted of waterfront property. Relying on his information, the plaintiffs purchased the parcel and built a structure on property belonging to a neighboring landowner. The plaintiffs sued for breach of contract and negligent misrepresentation. The plaintiffs successfully argued to the District Court they were third-party beneficiaries to at least one of two prior surveys performed by the surveying company for previous land owners. On appeal, however, the Supreme Court disagreed, concluding that the plaintiffs were incidental beneficiaries who were not specifically contemplated at the time the prior surveys were completed. Because they were strangers to the contracts, they lacked standing to sue for breach of contract. Kurtzenacker v. Davis Surveying, Inc., 2012 MT 105, 365 Mont. 71, 278 P.3d 1002. See also St. John v. Lewistown, 2017 MT 126, 387 Mont. 444, 395 P.3d 486.

Third-Party Administrators Not Liable for Made-Whole Violation Under State Employee Benefit Plan: Insureds under the state of Montana employee benefit plan sued the state and the third-party administrators (TPAs) who administer the state benefit plan, alleging violations of the subrogation statutes, Title 2, chapter 18, part 9. The District Court determined the subrogation statutes did not apply to the TPAs. The Supreme Court affirmed, concluding that the TPAs are not "insurers" under Title 2, chapter 18, part 9, and therefore could not be held independently liable under the subrogation statutes in this case. In addition, the TPAs were not liable under a third-party beneficiary theory because the insureds failed to demonstrate that the benefits they received from the expertise of the TPAs in administering claims were anything but incidental, rather than a benefit that the state and the TPAs intended to bestow upon the insureds when they contracted for administrative services. Diaz v. Blue Cross & Blue Shield of Mont., 2011 MT 322, 363 Mont. 151, 267 P.3d 756.

Lack of Standing of Stranger to Contract to Bring Action to Enforce Contract: A stranger to a contract who is not an intended third-party beneficiary lacks standing to bring an action based on a violation of the contract, including compliance with the statute of frauds. Palmer v. Bahm, 2006 MT 29, 331 M 105, 128 P3d 1031 (2006), followed in Dick Anderson Constr., Inc. v. Monroe Constr. Co., LLC, 2009 MT 416, 353 M 534, 221 P3d 675 (2009). See also Ludwig v. Spoklie, 280 M 315, 930 P2d 56 (1996), Kurtzenacker v. Davis Surveying, Inc., 2012 MT 105, 365 Mont. 71, 278 P.3d 1002, and Turner v. Wells Fargo Bank, N.A., 2012 MT 213, 366 Mont. 285, 291 P.3d 1082.

Third-Party Materialman — Action Against Surety: A third-party materialman was not entitled to recover on a cause of action against a surety on its surety bond that named the general contractor as the sole obligee and when the general contractor, subcontractor, and surety did not intend to benefit or protect any third-party materialmen by the execution of the bond. Treasure St. Indus., Inc. v. Welch, 173 M 403, 567 P2d 947 (1977).

Employment Contract: Employee was not third-party beneficiary, within the meaning of statute, of a contract between his employer and United States providing that employer should at all times be fully responsible for and exercise reasonable precaution for health and safety of his employees engaged in performance of work under contract; hence employee was not entitled to maintain action for employer's breach of safety clauses in the absence of express promise in contract to pay damages in addition to employee's rights to Workers' Compensation. Hensley v. U.S., 279 F. Supp. 548 (D.C. Mont. 1968). See also West v. Morrison-Knudsen Co., 294 F. Supp. 1336 (D.C. Mont. 1969), affirmed in 451 F2d 493 (9th Cir. 1971).

Surety Contract for the Sale of Grain: When grain buyers entered into a surety contract for the benefit of grain sellers as required by statute, and not for the benefit of the state, the grain sellers and not the Department of Agriculture were the real parties in interest in an action for the purchase price of the grain, although the Department of Agriculture had a statutory right and duty to protect the grain sellers' interest. State ex rel. Farmers Elev. Co. v. District Court, 147 M 72, 410 P2d 160 (1966).

Contracts for Hospitalization Under Workmen's Compensation Act: A contract made pursuant to the Workmen's Compensation Act for supplying hospital, medical, and surgical care to all employees assenting thereto is one made for the benefit of third persons, the employees, who, upon its acceptance by them, become entitled to enforce it in accordance with its terms under this section. Kelly v. Mont. Power Co., 111 M 118, 106 P2d 339 (1940).

Where Plaintiff Was Not the Benefited Party: Where the manager of a motor car company fraudulently filled in a conditional sales contract signed by a customer in blank, the manager and company were liable for the fraud, but when the manager afterward sold his interest in the company to another under an agreement stating that such other should not be responsible for obligations of the company "due to outsiders", the latter contract was not made for the benefit of the defrauded customer so as to enable him to maintain suit against the buyer of the manager's interest to recover what he paid the finance company to release his conditional sales contract. Koontz v. Sharon, 109 M 180, 94 P2d 668 (1939).

Description of Beneficiary: The party for whose benefit the contract is made must be named or otherwise sufficiently described or designated. However, if the contract was made expressly for the benefit of a class of persons to which class the party seeking enforcement belongs, he may obtain the benefit of it. Conley v. USF&G Co., 98 M 31, 37 P2d 565 (1934).

Contractor's Bonds:

Mere statement of duties to be discharged by highway contractor which may incidentally benefit third party or class to which latter belongs, without more, does not make surety liable to third person for contractor's failure to discharge duty. Nat'l Sur. Co. of New York v. Ulmen, 68 F2d 330 (9th Cir. 1933). See also Ulmen v. Nat'l Sur. Co. of New York, 3 F. Supp. 348 (D.C. Mont. 1933); Ulmen v. Nat'l Sur. Co. of New York, 4 F. Supp. 194 (D.C. Mont. 1933).

Surety on state highway contractor's bond was held not liable to pay unsatisfied judgment against contractor and in favor of driver of automobile which hit culvert along highway under construction, notwithstanding contractor's failure to maintain danger and warning signs as required by contract. Nat'l Sur. Co. of New York v. Ulmen, 68 F2d 330 (9th Cir. 1933).

Stranger to highway contract or bond securing performance thereof cannot recover against surety even though referred to in contract or bond, in absence of specific promise to pay such third person. Nat'l Sur. Co. of New York v. Ulmen, 68 F2d 330 (9th Cir. 1933). See also Ulmen v. Nat'l Sur. Co. of New York, 3 F. Supp. 348 (D.C. Mont. 1933); Ulmen v. Nat'l Sur. Co. of New York, 4 F. Supp. 194 (D.C. Mont. 1933).

Statutory action by laborers and materialmen against surety on contractor's bond was held distinct from obligee's action for benefit of laborers and materialmen, and therefore former decision is not res judicata. Cove Irrigation District v. Am. Sur. Co. of New York, 42 F2d 957 (9th Cir. 1930), reversing Cove Irrigation District v. Am. Sur. Co. of New York, 35 F2d 933 (9th Cir. 1929).

Decision on former appeal holding materialman not entitled to recover under highway contractor's bond obligating contractor to furnish labor and material at his own expense should be adhered to on second appeal, though decision was based on construction of state law. The intermediate decision of state Supreme Court held that materialman could recover under the statute, permitting enforcement by third person of contract made expressly for his benefit, where contract there involved contained promise of contractor to pay for labor and material used; agreement of contractor to furnish labor and material at his own expense not being expressly for benefit of materialman, since "express" means made known distinctly and explicitly and not left to inference. Minn. Steel & Mach. Co. v. Fed. Sur. Co., 34 F2d 270 (9th Cir. 1929).

Where the State Highway Commission (now Transportation Commission) requires a road construction contractor to promise in the contract awarded to him that he will pay laborers and materialmen, and the surety on his bond for the faithful performance of the work agrees to pay persons furnishing material and labor if the contractor fails to do so, laborers and materialmen may sue the surety directly in their own names as on a contract made for their benefit, as third parties, under this section; it being otherwise where the contract is silent as to paying such claims, though the surety promises to pay them, the bond in that regard then being unenforceable because not supported by a consideration. Gary Hay & Grain Co., Inc. v. Carlson, 79 M 111, 255 P 722 (1927), distinguished in Minn. Steel & Mach. Co. v. Fed. Sur. Co., 34 F2d 270 (9th Cir. 1929).

Burglary Insurance: In action against surety on robbery and burglary policy issued to County Treasurer to recover for loss of county money and securities stolen from Treasurer, the county was a proper, though not a necessary, party plaintiff, where the surety agreed to pay assured for loss sustained by assured or by owner, and county paid premiums on policy and was owner of property stolen. Nat'l Sur. Co. v. Sheridan County, 33 F2d 473 (9th Cir. 1929).

Incidental Beneficiary:

To entitle a person not a party to a contract between two others to recover thereunder, the contract must under this section have been made expressly for his benefit, the fact that it may incidentally benefit him being insufficient to bring him within the terms of this section. Martin v. Am. Sur. Co., 74 M 43, 238 P 877 (1925), overruled on another point in Gary Hay & Grain Co., Inc. v. Carlson, 79 M 111, 225 P 722 (1927), explained in Cove Irrigation District v. Am. Sur. Co. of New York, 35 F2d 933 (9th Cir. 1929); Conley v. USF&G Co., 98 M 31, 37 P2d 565 (1934).

Under this section, providing that "a contract made expressly for the benefit of a third person may be enforced by him at any time before the parties thereto rescind it", as construed by the Supreme Court of the state, which construction is binding on the federal courts, a contract, to come within the scope of the statute, must be one where the promisor undertakes to pay or discharge some debt or duty which the promisee owes to the third person. Where no consideration passes from the third person, but the provision for his benefit is voluntary on the part of the promisee, he cannot maintain an action for its enforcement. McNaught v. Hoffman, 274 F 918 (9th Cir. 1921).

Sufficiency of Complaint:

To entitle a third person to enforce a contract made between two others under this section, the complaint must show that it was expressly made for his benefit, or for the benefit of a class of persons to which he belongs, i.e., he, or they, either must be named therein or otherwise sufficiently described or designated; the fact that the contract may incidentally benefit him or them being insufficient. McKeever v. Oregon Mortgage Co., Ltd., 60 M 270, 198 P 752 (1921).

The complaint in an action by the vendors of land to recover the balance of the purchase price from a mortgage company which loaned the money to the vendee, setting forth the mortgage contract and alleging that the company had arranged with one of plaintiffs to hold the balance due until patent for the land should be received and recorded and then pay it directly to her, was insufficient, under this section, in the absence of an averment that the contract contained a provision that the mortgage was made expressly for the benefit of plaintiffs or either of them. McKeever v. Oregon Mortgage Co., Ltd., 60 M 270, 198 P 752 (1921).

Executory Contracts: The executory contract made expressly for the benefit of a third person must be one whereby the promisor undertakes to pay or discharge some debt or duty which the promisee owes to the third person. Tatem v. Eglanol Min. Co., 45 M 367, 123 P 28 (1912); McDonald v. Am. Nat'l Bank, 25 M 456, 65 P 896 (1901).

Application of Section: Plaintiffs were not entitled to enforce a contract for the payment of the balance of the purchase price as a contract made for their benefit, since this section does not apply to executory contracts without consideration. McDonald v. Am. Nat'l Bank, 25 M 456, 65 P 896 (1901).

Law Review Articles

Third Party Beneficiary Contracts in Montana, Burgess, 3 Mont. L. Rev. 97 (1942).

28-2-206. Assignment of nonnegotiable written contract.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Ambiguous Assignment — Construction of Document as a Whole: Peterson sold property to the Blairs under a contract for deed that reserved one-half the mineral rights in Peterson. Peterson then assigned her rights under the contract to Hopkins. The Blairs paid Hopkins and recorded. Peterson sued Hopkins to quiet title when the lessee of Peterson's one-half mineral rights claimed Peterson had assigned them to Hopkins by mistake. Hopkins was granted summary judgment because the assignment conveyed all of Peterson's right, title, and interest in the property, together with the contract for deed. The judgment was reversed, and judgment was granted Peterson. The assignment stated that it was subject to the contract for deed, thus creating an ambiguity. Taken as a whole, it appeared that the assignment was of the contract for deed and was not itself a deed of the entire surface and mineral interests to Hopkins. This was supported by the conduct of the parties, for Peterson leased her reserved interest for the 22 years following the assignment until lessee raised the alleged mistake, and at no time up to his death in the 17th year of the 22 years did Hopkins claim all the mineral rights or demand Peterson's one-half interest. Peterson v. Hopkins, 210 M 429, 684 P2d 1061, 41 St. Rep. 1140 (1984).

Ambiguous Assignment — Explanatory Evidence Admissible: A contract for deed reserved one-half the mineral rights in seller. Seller's subsequent assignment was ambiguous where it assigned all of seller's right, title, and interest in the property, together with the contract for deed, yet also stated that it was subject to the contract for deed. Therefore, the evidence was admissible to explain the ambiguity and the intent of seller and assignee of seller's rights under the contract for deed. Peterson v. Hopkins, 210 M 429, 684 P2d 1061, 41 St. Rep. 1140 (1984).

Assignor Not Liable for Breach by Debtor: Plaintiffs, tribal members, obtained a loan from the Blackfeet Tribe. Plaintiffs defaulted, and the tribe obtained a judgment in tribal court. The tribe filed notice with the Clerk and Recorder and the District Court. Plaintiffs agreed to sell their ranch to Robertson and to provide title insurance. A portion of the purchase price was placed in escrow to cover the amount owing the tribe. The escrow agreement contained a provision assigning pasturage fees to which plaintiffs were entitled to Robertson. Plaintiffs later filed suit against the tribe and Robertson. On appeal, the Supreme Court held that it is an established rule of contract law that the assignor does not guarantee that the obligor will pay and that the assignor is not liable to the assignee for breaches of the assignment by the debtor. Robertson could not recover pasturage fees from the plaintiffs, because plaintiffs did not owe them. Wippert v. Blackfeet Tribe, 201 M 299, 654 P2d 512, 39 St. Rep. 2117 (1982), overruled in part on other grounds by Green v. Gerber, 2013 MT 35, 369 Mont. 20, 303 P.3d 729.

Chattel Mortgage: Assignee of chattel mortgage given by buyer of automobile took the mortgage subject to buyer's defenses and equities existing at time of assignment. Sonnek v. Univ. C.I.T. Credit Corp., 140 M 503, 374 P2d 105 (1962).

What Contracts Assignable: As a general rule contracts between private individuals are assignable even in the absence of words making them so, subject, however, to the exceptions, among others, that they are not contracts wherein rights are coupled with liabilities, or for personal services, or which involve the relation of personal confidence. Standard Sewing Mach. Co. v. Smith, 51 M 245, 152 P 38 (1915).

No Conflict With or Expansion of Other Statute: This section is not in conflict with 27-1-503, and neither in any way enlarges the scope of the other nor the purpose which it was intended to accomplish. Cornish v. Woolverton, 32 M 456, 81 P 4 (1905); Stadler v. First Nat'l Bank, 22 M 190, 56 P 111 (1899).

Purpose:

The purpose of this section is to protect assignee of nonnegotiable contract against counterclaims, including setoffs, alleged as defenses, unless they are in existence and available at date of assignment. Cornish v. Woolverton, 32 M 456, 81 P 4 (1905); Stadler v. First Nat'l Bank, 22 M 190, 56 P 111 (1899).

Demand against assignor of nonnegotiable contract could not be set off against assignee, unless due and payable when assignment was made, and notice was unnecessary to prevent setoff of demand becoming payable subsequently. Cornish v. Woolverton, 32 M 456, 81 P 4 (1905); Stadler v. First Nat'l Bank, 22 M 190, 56 P 111 (1899).

Law Review Articles

Montana Law and the Uniform Commercial Code, 21 Mont. L. Rev. 1 (1959).

Part 3
Consent in General

Part Case Notes

Bodily Injury in Insurance Policy May Include Mental or Psychological Injury Accompanied by Physical Manifestations — Jacobsen Overruled: Defendant caused an automobile accident that injured two brothers, one of whom suffered severe trauma and was hospitalized for an extended period. The boys' mother filed a negligence action against defendant claiming emotional and physical injuries to herself and the brother who was not struck by the vehicle, including the mother's stress, migraine headaches, pain, depression, and a rapid heartbeat when hearing sirens, and the brother's withdrawal. Defendant sought liability coverage from her insurer, and the District Court, relying on Jacobsen v. Farmers Union Mut. Ins. Co., 2004 MT 72, 320 M 375, 87 P3d 995 (2004), granted the insurer's motion for a declaratory judgment on grounds that the insurer was not obligated to provide a defense or coverage to defendant because defendant's policy did not cover the claimed emotional injuries or physical injuries resulting from the emotional injuries within the definition of bodily injury. On appeal, the Supreme Court reexamined the Jacobsen analysis in light of subsequent case law and overruled Jacobsen. Bodily injury as construed in an insurance policy includes a mental or psychological injury that is accompanied by physical manifestations. Defendant's insurance policy provided general coverage for damages that the insured was legally obligated to pay because of a bodily injury sustained by any person, which in this case included the physical manifestations that accompanied the mother's and brother's mental and psychological injuries. Allstate Ins. Co. v. Wagner-Ellsworth, 2008 MT 240, 344 M 445, 188 P3d 1042 (2008), followed in Tucker v. Farmers Ins. Exch., 2009 MT 247, 351 M 448, 215 P3d 1 (2009).

Bodily Injury Not Inclusive of Emotional or Psychological Injury Within Terms of Uninsured Motorist Policy: Jacobsen was driving a car insured by defendant when he stopped to assist another motorist who was unconscious with a bleeding head wound. Despite Jacobsen's ministrations, the motorist died a few days later, and the cause was determined to be suicide. The next year, Jacobsen began seeking treatment for emotional distress suffered as a result of the incident and filed a claim with defendant to recover uninsured motorist benefits and medical pay benefits. The District Court granted summary judgment for defendant, and Jacobsen appealed on grounds that his policy for uninsured motorist coverage included damages for bodily injury sustained by the insured caused by an accident. The Supreme Court held that the term "bodily injury" was not ambiguous and was limited to physical injury caused by an accident but did not include emotional or psychological injuries. Thus, Jacobsen's emotional injury, including resulting physical manifestations, did not constitute bodily injury as defined in the insurance contract and was not compensable. Jacobsen v. Farmers Union Mut. Ins. Co., 2004 MT 72, 320 M 375, 87 P3d 995 (2004), following Bain v. Gleason, 223 M 442, 726 P2d 1153 (1986), and Aetna Life & Cas. Co. v. First Sec. Bank of Bozeman, 662 F. Supp. 1126 (D.C. Mont. 1987). Jacobsen was overruled in Allstate Ins. Co. v. Wagner-Ellsworth, 2008 MT 240, 344 M 445, 188 P3d 1042 (2008), to the extent that bodily injuries include mental or psychological injuries that are accompanied by physical manifestations.

Contract to Arbitrate Not Formed by Employee Handbook and Employee's Acknowledgment — Ambiguous Arbitration Provisions: When Hubner began working for defendant communications company, she signed an acknowledgment in an employee handbook that contained an arbitration provision. The arbitration clause provided that all controversies would be subject to binding arbitration, but the clauses in the handbook specified that the handbook did not constitute a contract of employment or create any relationship other than an employment-at-will relationship. When Hubner's employment was subsequently terminated, she brought a state claim for wrongful discharge, and defendant moved for a summary disposition compelling arbitration pursuant to 27-5-115. The District Court agreed with Hubner that there was no agreement to arbitrate and denied the motion, so defendant appealed. Defendant argued that because the arbitration clause was separable, it could be independently enforced. A state contract law defense that goes to the entire contract rather than specifically to an arbitration clause does not defeat a motion to compel arbitration; however, when a defense is aimed directly at the arbitration provision rather than the entire contract, state law contract defenses may be applied to hold that no enforceable agreement to arbitrate was made. Further, acceptance or consent by the party against whom a contract is sought to be enforced is required before a contract is enforceable. The language in the handbook was ambiguous and construed against the drafter. The ambiguity prevented Hubner from knowing and accepting that she was agreeing to binding arbitration by signing the handbook. Thus, no contract to arbitrate was formed by virtue of the handbook and Hubner's acknowledgment, even when the arbitration provision was considered separately from the rest of the handbook. The District Court was affirmed. Hubner v. Cutthroat Communications, Inc., 2003 MT 333, 318 M 421, 80 P3d 1256 (2003).

Blank Security Agreement Signed by Borrower and Filled Out by Bank: Borrower signed a blank security agreement that bank then filled out and mailed to her. The record shows that she had the agreement in her possession in December 1985; thus, she had the means to discover the fraud that she alleged bank committed in setting the agreement's terms. Because she did not file a claim until December 1988, her claim was barred by the 2-year statute of limitations. Richland Nat'l Bank & Trust v. Swenson, 249 M 410, 816 P2d 1045, 48 St. Rep. 730 (1991).

Method of Acceptance of Bid by County Commissioners — Recorded Vote Held Sufficient: Where the Commissioners of the defendant county voted to accept the plaintiff's bid for a rock crusher but did not issue a written notice of bid award, as was usually done, informing the successful bidder of the acceptance of his bid, the Supreme Court held that the acceptance motion approved by the Commission and recorded in the Commission minutes constituted an acceptance of the bid and that there was no statutory provision for the procedure argued by the county. Modern Mach. v. Flathead County, 202 M 140, 656 P2d 206, 39 St. Rep. 2383 (1982).

Option Agreement — Sufficiency of Consent and Consideration: The defendant appealed from a judgment granting specific performance of an option agreement to the plaintiff and ordering the property involved conveyed to the plaintiff. On appeal, the Supreme Court rejected the defendant's contention that the writing involved was not an option agreement because it failed to meet the essential requirements for the validity of a contract. In particular, he contended that there was a lack of consent and that the consideration was legally insufficient. The Supreme Court found the actual payment of $1 and actual participation in a family corporate dissolution sufficient consideration for the agreement. A memorandum here acted as an offer, and a binding agreement resulted from action on that offer by the offeree. The trial court was affirmed. Van Atta v. Schillinger, 191 M 472, 625 P2d 73, 38 St. Rep. 426 (1981).

Part Law Review Articles

Gaps in Contracts: A Critique of Consent Theory, Kalevitch, 54 Mont. L. Rev. 169 (1993).

28-2-301. Essential characteristics of consent.

Case Notes

No Entitlement to Severance Benefits Following Rejection of Severance Package: Patterson's job was eliminated through a corporate restructuring, and Patterson was offered a severance package that was conditioned upon the release of all claims against the employer. Patterson declined the severance package and instead filed an employment discrimination claim against the employer. When the claim failed about 1 year later, Patterson signed the severance agreement and mailed it to the employer, who refused to honor it. Patterson then sued, claiming entitlement to the severance benefits. Following discovery, the District Court granted summary judgment for the employer. On appeal, the Supreme Court affirmed. The severance contract offer could no longer be considered valid because there was no mutual consent between the parties and because Patterson sought to accept the severance contract after violating the release provision. An acceptance upon terms varying from those offered is a rejection of the offer. Unless the party who made the original offer renews it or assents to a modification, an offeree cannot later revive a contract through acceptance after rejecting the offer. Patterson's purported acceptance was at best a counteroffer that the employer did not accept, so no contract arose between the parties as to severance, and Patterson was not entitled to severance benefits. Patterson v. Verizon Wireless, 2005 MT 261, 329 M 79, 122 P3d 1193 (2005).

Offer and Acceptance as Elements of Consent: To have consent, there must be both an offer and an acceptance of that offer. The Supreme Court reversed a lower court finding of consent when testimony was insufficient to establish that an offer for purchase of stock had been made and a lack of evidence existed showing that any offer was ever accepted. Daniels v. Thomas, Dean & Hoskins, Inc., 246 M 125, 804 P2d 359, 47 St. Rep. 2293 (1990).

No Mutual Mistake in Workers' Compensation Settlement: Claimant sought to have his workers' compensation settlement reopened on grounds of mutual mistake. The Supreme Court affirmed the District Court's denial of the request after finding: (1) claimant was capable of understanding the terms of the settlement agreement; (2) although claimant may have experienced an increased level of pain, there was no evidence to indicate the parties were mutually mistaken about the condition of claimant's back at the time of settlement; (3) there was no evidence to link claimant's personality disorder to his back injury; and (4) the claim was barred by the statute of limitations. Whitcher v. Pac. Employers Ins. Co., 236 M 289, 769 P2d 1215, 46 St. Rep. 367 (1989).

Ignorance of Contract Contents Not Grounds for Relief From Liability: One who executes a written contract is presumed to know its contents and to assent to them. Ignorance of the contents is not grounds for relief from liability. Johnson v. Estate of Shelton, 232 M 85, 754 P2d 828, 45 St. Rep. 887 (1988), citing Quinn v. Briggs, 172 M 468, 565 P2d 297 (1977).

Undue Influence: Undue influence negates the free consent necessary for the proper formation of the contract. Adams v. Allen, 209 M 149, 679 P2d 1232, 41 St. Rep. 610 (1984).

Meeting of Minds — Oral Acknowledgment of Part of Written Contract Bid Specifications: The State's solicitation for bids for construction of building provided that the bid acknowledge receipt of any addenda. The State accepted the bid of a contractor that did not make the acknowledgment in its bid. The evidence that the State phoned the contractor regarding two addenda and contractor stated it knew of them and had begun preparation for fulfilling them was adequate to show that contractor had actual knowledge of the addenda and showed there was a meeting of the minds as to their existence and the requirements for fulfillment of their terms. Martel Constr., Inc. v. Bd. of Examiners, 205 M 332, 668 P2d 222, 40 St. Rep. 1340 (1983).

Finality of Workers' Compensation Decision — Grounds for Overturning: A full and final compromise settlement agreement between an injured worker and the Workers' Compensation State Fund was set aside because of mutual mistake of material fact by both parties. Kienas v. Peterson, 191 M 325, 624 P2d 1, 37 St. Rep. 1747 (1980), distinguished in Sollie v. Travelers

Indem. Co., 212 M 197, 686 P2d 920, 41 St. Rep. 1684 (1984). A petition for rehearing was filed. The Supreme Court reaffirmed the decision. The petitioner argued the Workers' Compensation Court had no power to alter or rescind the agreement 4 years after its execution. The Supreme Court pointed out that it, not the Workers' Compensation Court, set aside the agreement. It noted the scope of its appellate power and also the code provision on lack of consent through mutual mistake of material fact. The Supreme Court was not broadening the possibilities of reopening such settlements; it merely found that no contract existed initially. Kienas v. Peterson, 38 St. Rep. 320 (1981) (apparently not reported in Montana Reports or Pacific 2d Reporter).

Workers' Compensation Settlement — Mutual Mistake: Plaintiff injured his back when he fell in the restaurant where he worked and a rack of dishes fell on him. He submitted his claim to the Workers' Compensation Division but was not represented by an attorney. He was examined by physicians who found him to be 5% disabled. Plaintiff entered into a full and final compromise settlement. Later examinations by physicians showed that plaintiff's fall had aggravated his preexisting cerebral palsy condition. This information was not available to either party at the time the settlement was entered into. Both parties were mistaken as to a fact material to the contract. The court found that the need to fairly compensate the injured worker is the intent and purpose of the Workers' Compensation Act. The full and final compromise settlement was set aside for mutual mistake of a material fact as to the nature and extent of the injury caused by claimant's accident. The case was remanded to the Workers' Compensation Court to determine the extent of claimant's disability. Kienas v. Peterson, 191 M 325, 624 P2d 1, 37 St. Rep. 1747 (1980), followed in Kimes v. Pac. Employers Ins. Co., 233 M 175, 759 P2d 986, 45 St. Rep. 1402 (1988), Weldele v. Medley Dev., 227 M 257, 738 P2d 1281, 44 St. Rep. 1062 (1987), and Keller v. Liberty NW., Inc., 2010 MT 279, 358 Mont. 448, 246 P.3d 434.

Duress or Undue Influence — Determination by Trial Court: The determination by a trial court of whether consent to a contract is obtained through duress or undue influence will not be disturbed on appeal where there is substantial evidence to support the judgment on the record, which the Supreme Court should view in a light most favorable to the prevailing party at the trial level. Keil v. Glacier Park, Inc., 188 M 455, 614 P2d 502, 37 St. Rep. 1151 (1980).

Misconception of Meaning: Though the mutual consent of the parties to a contract is an essential element thereof, where a written agreement is susceptible of but one meaning, a misconception thereof by one of the parties not authorized by the language used does not affect the contract. J. Neils Lumber Co. v. Farmers Lumber Co., 88 M 392, 293 P 288 (1930).

Menace: Under this section, the consent of a party to a contract must be free; this is not free when obtained through menace (28-2-401), and under 28-2-403, a threat of unlawful confinement of the person threatened constitutes menace. Clifford v. Great Falls Gas Co., 68 M 300, 216 P 1114 (1923). See also Fronk v. Collins, 2011 MT 315, 363 Mont. 110, 266 P.3d 1271, which held that the parties' contract did not suffer from lack of consent due to menace when the communication was between the parties' attorneys; the communication did not threaten imprisonment to compel payment, but only mentioned criminal and civil remedies; and the parties were free to abandon negotiations at any time.

28-2-302. Effect of consent which is not free.

Case Notes

False Representations: The sellers of a business falsely represented the profitability of the business and its standing with suppliers and wholesalers to prospective buyers. The buyers relied on and had a right to rely on the truth of the representations and were induced to purchase the business because of the false representations. Upon learning of the falsity of the representations that had induced them to purchase the business, the purchasers had the right to rescind the contract for deed for the purchase of the business. Lumby v. Doetch, 183 M 427, 600 P2d 200 (1979).

28-2-303. When consent is mutual.

Case Notes

Question Whether Parties Consented to Contract — Material Fact Precluding Summary Judgment: The District Court determined that defendant did not consent to a title policy, so the contract was invalid and defendant was entitled to summary judgment. On appeal, the Supreme Court found that the issue of whether and when plaintiff instructed defendant to issue the title policy in plaintiff's name was a material fact that was disputed by the parties. The extent and nature of the parties' consents are questions of fact that must be first determined, so summary judgment was inappropriate and the case was reversed and remanded for further proceedings. Amerimont, Inc. v. Fidelity Nat'l Title Ins. Co., 2009 MT 212, 351 M 292, 210 P3d 691 (2009).

Failure to Establish Uninterrupted Possession to Qualify as Extinguished Easement — Summary Judgment Proper: A deed of restriction reserved easements on all existing roads within a subdivision for the scenic views and enjoyment of the property and for the reasonable general use of all subdivision property owners to access public lands. In 1984, defendants bought three subdivision tracts and promptly erected a locking gate across the road that intersected their property. Plaintiff subdivision association requested that defendants remove the gate because it was interfering with property owners' access to public lands. However, defendants refused and threatened legal action, so the association took no immediate action. The association eventually filed a complaint in 2000, accusing defendants of violating the deed of restriction by interfering with the easement. Defendants contended that the association had waived or abandoned any easement by not using the road for over 17 years. The District Court disagreed and granted summary judgment to the association. Defendants appealed on grounds that summary judgment was improper because a material fact existed as to whether the easement had been extinguished, but the Supreme Court affirmed. The association established the existence of a valid recorded easement that encumbered defendants' land, and defendants failed to show that their use of the road was continuous and uninterrupted for 5 years. In fact, the record was replete with admissions that association members continued to use the road, interrupting defendants' attempted adverse possession of the easement. Additionally, defendants testified that the gate was not locked all the time, that they lived outside the state part of the year, during which time they were unable to enforce their claim of right, and that the association had graded and maintained the road during the time in question. Thus, defendants' own testimony contradicted their claim of abandonment and adverse possession. The District Court did not err in finding that defendants' claims failed to establish a genuine issue of material fact that would preclude summary judgment. Meadow Lake Estates Homeowners Ass'n v. Shoemaker, 2008 MT 41, 341 M 345, 178 P3d 81 (2008).

No Entitlement to Severance Benefits Following Rejection of Severance Package: Patterson's job was eliminated through a corporate restructuring, and Patterson was offered a severance package that was conditioned upon the release of all claims against the employer. Patterson declined the severance package and instead filed an employment discrimination claim against the employer. When the claim failed about 1 year later, Patterson signed the severance agreement and mailed it to the employer, who refused to honor it. Patterson then sued, claiming entitlement to the severance benefits. Following discovery, the District Court granted summary judgment for the employer. On appeal, the Supreme Court affirmed. The severance contract offer could no longer be considered valid because there was no mutual consent between the parties and because Patterson sought to accept the severance contract after violating the release provision. An acceptance upon terms varying from those offered is a rejection of the offer. Unless the party who made the original offer renews it or assents to a modification, an offeree cannot later revive a contract through acceptance after rejecting the offer. Patterson's purported acceptance was at best a counteroffer that the employer did not accept, so no contract arose between the parties as to severance, and Patterson was not entitled to severance benefits. Patterson v. Verizon Wireless, 2005 MT 261, 329 M 79, 122 P3d 1193 (2005).

Bridle Path Easement — Express Easement by Reservation Versus Implied Easement — Extrinsic Evidence Regarding Parties' Intent Inadmissible: Purchasers in a subdivision had language in their deeds creating an express easement for a bridle path in the subdivision. The bridle path was never built, and over the years, the easement was obstructed by improvements on the lots of several subdivision residents. Eventually, the subdivision association attempted to extinguish the easement at a meeting of the board of directors. Some residents asked the District Court to establish the validity of the easement and to restrain obstruction of the easement, and their request was granted by partial summary judgment. On appeal, the Supreme Court noted the difference between an implied easement, which is a creature of equity dependent on the intent of the parties, and an express easement by reservation, which is a creature of the documents of conveyance and the record. An express easement by reservation arises when the purchaser's deed refers to the plat where the easement is clearly depicted and labeled. In this case, the intent of the parties to create a bridle path easement was manifested through the language in the deeds and the plat, so under 28-2-905, extrinsic evidence regarding the intent of the parties was inadmissible. Further, the subdivision association was given oversight of the easement, but not ownership of it, and so lacked authority to extinguish the easement. The lower court's finding that a valid bridle path easement existed was affirmed. Pearson v. Virginia City Ranches Ass'n, 2000 MT 12, 298 M 52, 993 P2d 688, 57 St. Rep. 65 (2000), following Missoula v. Mix, 123 M 365, 214 P2d 212 (1950), Bache v. Owens, 267 M 279, 883 P2d 817 (1994), Halverson v. Turner, 268

M 168, 885 P2d 1285 (1994), and Tungsten Holdings, Inc. v. Parker, 282 M 387, 938 P2d 641, 54 St. Rep. 399 (1997), and distinguishing White v. Landerdahl, 191 M 554, 625 P2d 1145, 38 St. Rep. 412 (1981).

No Meeting of Minds Concerning Stock Transfer: Wife offered to convey shares of stock to husband to satisfy a dissolution judgment, but husband did not accept her offer; he merely agreed to consider it. Husband subsequently rejected wife's offer because of negative tax consequences associated with the transfer. There can be no binding contract without the mutual consent of the parties, and consent is established if there has been an offer and an acceptance of that offer. In re Marriage of Dalley, 237 M 287, 773 P2d 295, 46 St. Rep. 808 (1989).

Breach of Contract Action Sounding in Equity — Mutuality of Consent: Although an action for breach of contract to lend money is usually an action at law, the case sounded in equity where borrower argued that the contract was illusory and thus void because it lacked mutuality and that the lender's interpretation of the contract rendered the contract unconscionable and required the contract to be voided or reformed, and the lender raised the equitable defenses of estoppel, waiver, and laches. Shimsky v. Valley Credit Union, 208 M 186, 676 P2d 1308, 41 St. Rep. 258 (1984).

Commissioner to Determine Standard Prevailing Rate of Wages: Plaintiff was awarded the mechanical subcontract on a research laboratory being constructed by the State. The State received a complaint that plaintiff was not paying the "standard prevailing rate" (SPR) of wages. The State investigated and concluded that the complaint was legitimate. Plaintiff commenced a declaratory judgment action, and judgment was entered in his favor. On appeal, the Supreme Court held that the authority to determine the SPR rests exclusively with the Commissioner of Labor and Industry. The District Court was incorrect in allowing the contractor to determine the SPR. The court also held that this was not reversible error since the SPR existed only somewhere in the bureaucracy and plaintiff was unaware of it. Because of this, there was no mutual assent under the contract. Thompkins v. Fuller, 205 M 168, 667 P2d 944, 40 St. Rep. 1192 (1983).

Factual Question: Consent is not mutual unless the parties agree upon the same thing in the same sense, and such mutuality requires a factual determination of the extent and nature of the parties' consents. Soha v. West, 196 M 95, 637 P2d 1185, 38 St. Rep. 2153 (1981).

Real Estate Listing Agreement — Attempt of Broker to Find Purchaser on Owner's Terms as Creating Mutuality: Buechler entered into a contract with Payne, granting him the right to sell Buechler's property. Payne attempted to sell the property and expended time and money to attract purchasers. Buechler canceled the contract before its term expired and sold the property herself. Buechler argued that the contract lacked mutuality. The court found that mutuality of obligation was created by the efforts of the broker to find a purchaser for the property on the owner's terms and the broker's expenditures of time and money in this effort. Payne v. Buechler, 192 M 311, 628 P2d 646, 38 St. Rep. 799 (1981).

Implied Easements — When Found — Effect of Contract: The plaintiffs sold a parcel of land to the defendants after a series of negotiations. No easement was specified through that parcel to the plaintiff's adjoining parcel and no other access existed to that second parcel. The Supreme Court found no implied easement, noting that the trial court would have been rewriting the contract had it found an implied easement. The trial court cited eight offers and counteroffers regarding an easement in this land sale and noted that there was a final decision between the parties that there would be no easement across the defendants' land. A court may not create as a matter of law an implied easement when the facts indicate the parties did not intend that an easement be created. Implied easements rest upon the intent of the parties gathered from the evidence. The record contained insufficient evidence to support an implied easement but contained substantial evidence to support the trial court's findings, conclusions, and judgment. White v. Landerdahl, 191 M 554, 625 P2d 1145, 38 St. Rep. 412 (1981), distinguished in Pearson v. Virginia City Ranches Ass'n, 2000 MT 12, 298 M 52, 993 P2d 688, 57 St. Rep. 65 (2000), with regard to the applicability of an implied easement, which is a creature of equity dependent on the intent of the parties, versus an expressed easement by reservation, which is a creature of the documents of conveyance and the record.

Mutual Assent on Elements of Contract — Raising at Trial Level: Plaintiff and defendants entered a buy-sell agreement for a parcel of land owned by defendants. From the filing of the complaint to eventual trial, both parties contended that the buy-sell was valid and enforceable against the other. The issue at trial was not the validity of the contract but whether it included certain alleged easements. Plaintiff was granted specific performance. On appeal, defendants contended that the parties had never agreed on the same terms, that there was no mutual assent or meeting of the minds, and therefore no enforceable contract. Because this contention had not been raised at the trial level, it could not be considered on appeal. Chadwick v. Giberson, 190 M 88, 618 P2d 1213, 37 St. Rep. 1723 (1980).

Lack of Mutuality: The court found that a "letter of instruction and joint assignment of funds" lacked mutuality but did not discuss the issue. Boise Cascade Corp. v. First Sec. Bank of Anaconda, 183 M 378, 600 P2d 173 (1979).

28-2-304. Ratification of contract void for want of consent.

Case Notes

Guarantor's Obligation Not Barred by Statute of Limitations as to Obligation of Principal: A creditor's claim against a guarantor is not exonerated by the running of the statute of limitations as against the principal. Mercury Marine v. Monty's Enterprises, Inc., 270 M 413, 892 P2d 568, 52 St. Rep. 255 (1995). See also Dupree v. Jordan, 252 P 67 (Okla. 1927), Bloom v. Bender, 313 P2d 568 (Calif. 1957), and Restatement of Security 130 (1941), Comment a on subsection (1) and illustration 2.

Written Memorialization Modifying Contribution Obligations Unenforceable—Audit of Payroll Records Allowed: It was error for a District Court to conclude that a written memorialization modifying an employer's obligation to contribute to a union trust fund was enforceable because the memorialization did not comply with the requirements in either the labor contract or the pension certification for making a contribution modification binding on the trust fund. The memorialization had not been subjected to the procedure for obtaining the trust fund's consent for modification. After noting that the issue had been properly raised at the trial level, the Supreme Court remanded for a recalculation of delinquent contributions, interest, and liquidated damages without regard to the memorialization. The court also affirmed the trust fund's right to audit the employer records for the time in question and vacated an award of attorney fees that had been premised on the employer as prevailing party. Hughes v. Blankenship, 266 M 150, 879 P2d 685, 51 St. Rep. 699 (1994).

Later Agreement on Alleged Ambiguity — Ratification: Plaintiff offered to buy defendants' ranch. After much negotiation, plaintiff paid earnest money, for which he received a receipt, and the parties entered into a buy-sell agreement on April 20, 1981. The April 20, 1981, buy-sell agreement contained all the essential elements of a contract. The closing documents prepared by defendants' attorney did not correspond to the April 20 agreement. On May 15, 1981, the parties met and plaintiff was again presented with closing documents not corresponding to the April 20 agreement. A dispute arose over a clause releasing a parcel of land up to 320 acres to plaintiff for building purposes on the date of closing. Plaintiff agreed to defendants' interpretation at the May 15 meeting. On May 20, 1981, plaintiff received a third set of closing documents not reflecting the April 20 or May 15 meetings. On June 2, the parties met and defendants presented new terms, one of which was transferring title to the real property in 1981 rather than in 1982, destroying plaintiff's planned income tax advantages, one of his reasons for buying the ranch. Defendants claimed the land was required to be transferred at the time the cattle were transferred or grazing permits would be lost. A Forest Service official informed defendants in a June 3, 1981, letter that three alternatives existed. At the end of a June 5, 1981, meeting, plaintiff's attorney prepared a contract based on the April 20 buy-sell, the May 15 interpretation of the release, and the June 5 meeting. On June 12, plaintiff signed the contract and attached a check for the downpayment. Defendants refused to sign, and suit was filed on July 2, 1982. The District Court held that a valid contract existed and that defendants had breached the contract. On appeal, the Supreme Court held that the buy-sell contained all the essential elements of a contract. The court held that the release clause appeared unambiguous. The evidence presented showed that the parties' differing interpretations of the language were resolved and agreement on the clause was reached at the May 15, 1981, meeting. Under 28-2-304, a contract voidable for want of due consent may be ratified by subsequent consent. The May 15 agreement was held to be a ratification. Any delay in performance on plaintiff's part was due to defendants' failure to prepare documents conforming to the agreed-upon contract. The District Court was affirmed. Ehly v. Cady, 212 M 82, 687 P2d 687, 41 St. Rep. 1611 (1984).

Ratification of Lease by Accepting Compensation — Lease in Trust: Real property for which a lease was executed by husband and wife to lessee in 1956 for a 10-year term with 3-year extensions was transferred to a trust upon their divorce. The trustees were husband, wife, and daughter, with husband having "general control" over the business of the trust, but in other matters two of the three trustees were required to sign. At the expiration of the lease and the original three renewals, husband alone executed a new lease agreement to original lessee that was similar to the original but increased the rent. The rent increase was received and noted by wife and daughter. Three years later they sued husband and lessee for damages, unlawful detention, and liquidated damages, contending there was no valid lease signed by two of the three trustees. The Supreme Court held that by "generally operating" the trust the husband had authority to make a new lease. The actions of wife and daughter receiving increased compensation were notification to them of the lease change, and failure to act ratified the lease agreement even if the signature of one of them was required for its execution. Wyman v. Wyman, 208 M 57, 676 P2d 181, 41 St. Rep. 170 (1984).

Ratification of Collective Bargaining Agreements: The court improperly found that respondent construction contractor had no duty to make contributions to a union trust fund under the terms of a collective bargaining agreement. The record shows that respondent made contributions to the fund over an 8-year period, consistent with a recognition of its obligation under the collective bargaining agreement. As such, the respondent must be held to have ratified and approved the agreements. Audit Serv., Inc. v. Francis Tindall Constr., 183 M 474, 600 P2d 811 (1979), followed in Audit Serv., Inc. v. Harvey Bros. Constr., 204 M 484, 665 P2d 792, 40 St. Rep. 1019 (1983). See also Audit Serv., Inc. v. Houseman, 227 M 57, 737 P2d 71, 44 St. Rep. 891 (1987), Hughes v. Blankenship, 239 M 519, 781 P2d 1132, 46 St. Rep. 1880 (1989), and Audit Serv., Inc. v. Frontier-West, Inc., 252 M 142, 827 P2d 1242, 49 St. Rep. 186 (1992).

Part 4

Circumstances Which Affect Validity of Apparent Consent

Part Case Notes

Sale of Trust Lands Within Flathead Reservation — No Jurisdiction Found for Purposes of Breach of Contract, Fraud, and Negligent Misrepresentation: Neuman, an enrolled member of the Confederated Salish and Kootenai Tribes, sought assistance from the Bureau of Indian Affairs (BIA) to clear the title to trust land within the Flathead Reservation so that Neuman could sell it. He also engaged a real estate broker. Both Neuman and prospective buyers, the Krauses, made considerable efforts to consummate the sale, but Neuman was informed by the BIA that there was a substantial cloud on the title. Neuman therefore terminated the listing agreement, and the Krauses sued for damages, alleging breach of contract, fraud, constructive fraud, fraud in the inducement, and negligent misrepresentation. The District Court, on the recommendation of a special master and after applying the test laid out in State ex rel. Iron Bear v. District Court, 162 M 335, 512 P2d 1292 (1973), found a lack of subject matter jurisdiction. The Supreme Court held that 25 U.S.C. 345 and 28 U.S.C. 1353 vest exclusive jurisdiction in the federal courts over disputes involving allotted lands within Indian reservations and that 28 U.S.C. 1360 preempted its jurisdiction. The Supreme Court also held that the Krauses' lawsuit was a dispute involving title to allotted lands even though the action was a tort claim and breach of contract claim because all of the Krauses' claims could not be separated from questions of title to Indian trust lands. Noting that it had already held in In re Marriage of Wellman, 258 M 131, 852 P2d 559 (1993), that an attempt by state courts to adjudicate rights in Indian trust land for the purpose of money damages was precluded by federal law, the Supreme Court held that it made no difference that the Krauses had deleted from their complaint a prayer for specific performance. The claims could still not be separated from the issue of title to Indian lands. Krause v. Neuman, 284 M 399, 943 P2d 1328, 54 St. Rep. 937 (1997). In In re Estate of Big Spring, 2011 MT 109, 360 Mont. 370, 255 P.3d 121, the Supreme Court overruled Iron Bear in its entirety and Krause v. Neuman to the extent it relied on the Iron Bear test.

U.C.C. Unconscionability Provision — Application to Leases: The Montana Uniform Commercial Code provision relating to unconscionable sales contracts (30-2-302) can, at least by analogy, be applied to lease transactions and should guide the Supreme Court in determining whether a lease is unconscionable. All-States Leasing Co. v. Top Hat Lounge, 198 M 1, 649 P2d 1250, 39 St. Rep. 425 (1982).

Unconscionability — Leases Between Businessmen: Courts have readily applied the doctrine of unconscionability of contracts as between consumers and businessmen but are reluctant to rewrite the terms of a contract between businessmen themselves. When, as in instant case, all provisions of a lease are agreed to by businessmen on both sides, none of the surrounding circumstances suggest oppression of lessee's freedom to select another lessor, nothing on the record suggests disparity of bargaining power, and lessee selected both the equipment leased and the supplier of the equipment to the lessor and notified lessor of lessee's desire to make the lease, the lease cannot be considered unconscionable. All-States Leasing Co. v. Top Hat Lounge, 198 M 1, 649 P2d 1250, 39 St. Rep. 425 (1982).

Unconscionability — Success of Unsupported Claim: The mere unsupported claim that equipment lease under which appellants were sued was unconscionable and that a more oppressive lease was hard to imagine could not succeed on appeal from summary judgment for delinquent payments under lease. All-States Leasing Co. v. Top Hat Lounge, 198 M 1, 649 P2d 1250, 39 St. Rep. 425 (1982).

28-2-401. When apparent consent not free.

Case Notes

No Error in Determining Firearms Belonged to Wife of Felon in Valid Prenuptial Agreement After Blissful Marriage Fell Apart: The District Court did not err in finding a prenuptial agreement valid and enforceable because the record contained no evidence that the agreement was fraudulent or that the husband lacked capacity, was under duress, or was subject to undue influence when he signed it. Accordingly, because the agreement stated that property gifted to either party would be owned separately, the District Court did not err in finding that guns gifted to the wife by the husband partially because the husband had a federal conviction and could not legally own them properly belonged to the wife. In re Marriage of Bliss, 2016 MT 51, 382 Mont. 370, 367 P.3d 395.

Sufficient Evidence for Rescission of Workers' Compensation Settlement Agreement Based on Mutual Mistake of Material Fact Not Discovered Until After Settlement: Gamble was injured on the job, the parties entered a settlement agreement, and the employer began paying benefits based on a medical diagnosis, yet Gamble's condition worsened. Finally, Gamble went to a specialist who ran additional tests and discovered that Gamble had suffered an odontoid fracture of the spine that was consistent with the job injury but that had been unnoticed at the time of the settlement. Gamble's request for additional medical benefits was denied by the employer because payment for the fracture was not part of the settlement. The Workers' Compensation Court held that the fracture was compensable, and the employer appealed, but the Supreme Court affirmed. If Gamble's fracture existed at the time of settlement, the parties were mutually mistaken regarding the material fact concerning the nature of Gamble's injury, requiring that the agreement be rescinded. The Supreme Court reviewed the findings and found that substantial credible evidence supported the facts that: (1) the fracture was consistent with and caused by the on-the-job injury; (2) Gamble's symptoms were consistent with the injury; (3) there was a basis for ruling out other potential causes of injury; and (4) there was an explanation as to why the injury was not diagnosed at the time of settlement. Because the mutual mistake of fact existed, the settlement agreement was properly rescinded. Gamble v. Sears, 2007 MT 131, 337 M 354, 160 P3d 537 (2007).

Authority of Workers' Compensation Court to Reopen Final Compromise Settlement Agreement Based on Mutual Mistake: Settlement agreements for workers' compensation benefits, like other agreements, are subject to the law of contracts. A Montana court that is not otherwise limited by statute, including the Workers' Compensation Court, has the authority to set those contracts aside based upon a mutual mistake regarding the nature and extent of a claimant's injuries even when express language in the settlement agreement purports to prohibit setting the agreement aside. Wolfe v. Webb, 251 M 217, 824 P2d 240, 49 St. Rep. 1 (1992), distinguishing Bowen v. Anaconda Co., 220 M 185, 714 P2d 142 (1986), and Hutchinson v. Pierce Packing Co., 219 M 18, 710 P2d 64 (1985), and followed in Gamble v. Sears, 2007 MT 131, 337 M 354, 160 P3d 537 (2007).

Blank Security Agreement Signed by Borrower and Filled Out by Bank: Borrower signed a blank security agreement that bank then filled out and mailed to her. The record shows that she had the agreement in her possession in December 1985; thus, she had the means to discover the fraud that she alleged bank committed in setting the agreement's terms. Because she did not file a claim until December 1988, her claim was barred by the 2-year statute of limitations. Richland Nat'l Bank & Trust v. Swenson, 249 M 410, 816 P2d 1045, 48 St. Rep. 730 (1991).

Costs Provided by Contract Allowable Despite Tortious Nature of Claim: In an action by plaintiff to rescind a contract for sale of real property because of alleged fraud, misrepresentation, undue influence, and unconscionability, the award of attorney fees and costs that the contract provided to the successful defendant, relating to his defense and counterclaim of wrongful occupation by the plaintiff, was proper notwithstanding the contention that the action sounded in tort and not in contract (citing Winer v. Jonal Corp., 169 M 247, 545 P2d 1094 (1976)). The underlying action was based on a contract dispute. Westlake v. Osborne, 230 M 364, 750 P2d 444, 45 St. Rep. 277 (1988).

Incompetence and Undue Influence Never Presumed — Presumption of More Satisfactory Evidence Not Error: Although incompetence or undue influence is never presumed and it is clearly the burden of the plaintiff to prove such matters, when the defendant failed to engage in the usual practice of calling upon doctors and nurses from the confining hospital to clearly show mental capacity at the time the instrument was signed, it was not error for the District Court to rely on the presumption in 26-1-602 that provides that more satisfactory evidence would be adverse if weaker and less satisfactory evidence is offered and it is within the pertinent party's power to produce more satisfactory evidence. That presumption relates only to the type and lack of evidence of the defendant, not to the plaintiff's burden of proof. Adams v. Allen, 209 M 149, 679 P2d 1232, 41 St. Rep. 610 (1984).

Finality of Workers' Compensation Decision — Grounds for Overturning: A full and final compromise settlement agreement between an injured worker and the Workers' Compensation State Fund was set aside because of mutual mistake of material fact by both parties. Kienas v. Peterson, 191 M 325, 624 P2d 1, 37 St. Rep. 1747 (1980), distinguished in Sollie v. Travelers Indem. Co., 212 M 197, 686 P2d 920, 41 St. Rep. 1684 (1984). A petition for rehearing was filed. The Supreme Court reaffirmed the decision. The petitioner argued the Workers' Compensation Court had no power to alter or rescind the agreement 4 years after its execution. The Supreme Court pointed out that it, not the Workers' Compensation Court, set aside the agreement. It noted the scope of its appellate power and also the code provision on lack of consent through mutual mistake of material fact. The Supreme Court was not broadening the possibilities of reopening such settlements; it merely found that no contract existed initially. Kienas v. Peterson, 38 St. Rep. 320 (1981) (apparently not reported in Montana Reports or Pacific 2d Reporter).

Workers' Compensation Settlement — Mutual Mistake: Plaintiff injured his back when he fell in the restaurant where he worked and a rack of dishes fell on him. He submitted his claim to the Workers' Compensation Division but was not represented by an attorney. He was examined by physicians who found him to be 5% disabled. Plaintiff entered into a full and final compromise settlement. Later examinations by physicians showed that plaintiff's fall had aggravated his preexisting cerebral palsy condition. This information was not available to either party at the time the settlement was entered into. Both parties were mistaken as to a fact material to the contract. The court found that the need to fairly compensate the injured worker is the intent and purpose of the Workers' Compensation Act. The full and final compromise settlement was set aside for mutual mistake of a material fact as to the nature and extent of the injury caused by claimant's accident. The case was remanded to the Workers' Compensation Court to determine the extent of claimant's disability. Kienas v. Peterson, 191 M 325, 624 P2d 1, 37 St. Rep. 1747 (1980), followed in Kimes v. Pac. Employers Ins. Co., 233 M 175, 759 P2d 986, 45 St. Rep. 1402 (1988), Weldele v. Medley Dev., 227 M 257, 738 P2d 1281, 44 St. Rep. 1062 (1987), and Keller v. Liberty NW., Inc., 2010 MT 279, 358 Mont. 448, 246 P.3d 434.

Duress or Undue Influence — Determination by Trial Court: The determination by a trial court of whether consent to a contract is obtained through duress or undue influence will not be disturbed on appeal where there is substantial evidence to support the judgment on the record, which the Supreme Court should view in a light most favorable to the prevailing party at the trial level. Keil v. Glacier Park, Inc., 188 M 455, 614 P2d 502, 37 St. Rep. 1151 (1980).

Duress as a Defense:

Where dairymen withheld milk from processor until the making of a written "output" agreement, actions of the dairymen did not constitute such duress as to make the written contract void. McNussen v. Graybeal, 146 M 173, 405 P2d 447 (1965).

The defense of duress is based upon the proposition that the consent of the party to the contract over whom it was exercised was not free. Bullard v. Smith, 28 M 387, 72 P 761 (1903).

Menace: Under 28-2-301, the consent of a party to a contract must be free; it is not free when obtained through menace, and under 28-2-403, a threat of unlawful confinement of the person threatened constitutes menace. Clifford v. Great Falls Gas Co., 68 M 300, 216 P 1114 (1923). See also Fronk v. Collins, 2011 MT 315, 363 Mont. 110, 266 P.3d 1271, which held that the parties' contract did not suffer from lack of consent due to menace when the communication was between the parties' attorneys; the communication did not threaten imprisonment to compel payment, but only mentioned criminal and civil remedies; and the parties were free to abandon negotiations at any time.

28-2-402. What constitutes duress.

Case Notes

Premarital Agreement Enforceable — Premarital Agreement Between Father and Surrogate Mother Signed Voluntarily Without Undue Influence or Duress — Parent-Child Relationship

Provision Not Equitably Unconscionable. Sayler v. Yan Sun, 2023 MT 175, 413 Mont. 303, 536 P.3d 399.

Threat to Withdraw as Legal Counsel: Duress was not present when attorney, minutes before he was to defend client on criminal charges, threatened to withdraw as counsel unless client executed security agreement and quitclaim deed as security for attorney's fee. Attorney had given the instruments to client weeks before trial but client had failed to execute them. Matthews v. Berryman, 196 M 49, 637 P2d 822, 38 St. Rep. 2112 (1981).

Threat of Breach: The threat of breach on existing agreement does not constitute duress in order to obtain a different agreement. Kovash v. Knight, 169 M 227, 545 P2d 1091 (1976).

Unlawful Detention of Property — Economic Duress: An allegation of economic duress does not constitute a defense when there is no allegation of an unlawful detention of property as is required by this section. Double X Ranch v. Savage Bros., 167 M 231, 536 P2d 1176 (1975).

Economic Duress:

While equity recognizes the doctrine of economic duress, the vast majority of cases still require wrongful or unlawful conduct as an essential element. McNussen v. Graybeal, 146 M 173, 405 P2d 447 (1965).

Dairymen who withheld milk from processor under an oral "requirement" agreement did not use such duress as to make subsequent written "output" contract void, since "requirement" agreement put them under no legal obligation to deliver milk, and duress requires an unlawful act. McNussen v. Graybeal, 146 M 173, 405 P2d 447 (1965).

Threats to Take Legal Action:

To threaten to do only those things which a person has a legal right to do under an existing contract does not constitute duress, nor may a charge of duress be based on mere vexation and annoyance, mere pecuniary distress, or a refusal to surrender property on which one has a lien. Pederson v. Thoeny, 88 M 569, 295 P 250 (1930).

Threats to enforce payment of promissory notes in the manner provided in a contract of sale in case of nonpayment do not constitute duress. Ott v. Pace, 43 M 82, 115 P 37 (1911).

Duress Upon Third Person — Comaker of Note — Threat of Criminal Prosecution: As a general rule, a contractual obligation cannot be avoided because of duress imposed upon a third person, with the possible exception of persons who bear a close relationship to the threatened person. The defense of duress was not available to the maker of a note given to prevent a threatened criminal prosecution against his comaker for failure to pay over money collected by the latter. Spear v. Ryan, 64 M 145, 208 P 1069 (1922).

Threatened Arrest: Where it was believed that defendant was connected with theft of sheep and he gave a promissory note for damages occasioned by the theft, defense that note sued upon was executed under duress was not sustained by evidence that defendant had been threatened with arrest. Bullard v. Smith, 28 M 387, 72 P 761 (1903).

28-2-403. What constitutes menace.

Case Notes

Validity of Promissory Note Executed to Satisfy Charge-Back Liability in Nigerian Scam: Hughes executed a promissory note to satisfy a charge-back liability necessitated by Hughes' participation in a Nigerian scam. Hughes made the first payment on the note, but failed to make any more payments, and the bank that issued the note initiated an action for judicial foreclosure. The District Court granted summary judgment to the bank on the promissory note, and Hughes appealed. The Supreme Court considered Hughes' arguments regarding lack of consideration, menace, and undue influence. Hughes became liable under 30-4-212 for satisfying the entire charge-back debt, so the note did not fail for lack of consideration. Hughes' first quarterly payment comprised a ratification of the contract, so the note did not fail for consent because of menace. Whatever influence the bank employee exerted over Hughes, it did not rise to the level of substituting the employee's will for that of Hughes, nor was there any indication that Hughes was in a mentally or physically weak state or in a confidential relationship with the employee, so the note did not fail for lack of consent as a result of undue influence. Based on the claims made and the facts asserted, summary judgment for the bank was affirmed. Valley Bank of Ronan v. Hughes, 2006 MT 285, 334 M 335, 147 P3d 185 (2006), following Averill Mach. Co. v. Taylor, 70 M 70, 223 P 918 (1924), and Heintz v. Vestal, 185 M 233, 605 P2d 606 (1980).

Detention of Property: To threaten to do only those things which a person has a legal right to do under an existing contract does not constitute duress, nor may a charge of duress be based on mere vexation and annoyance, mere pecuniary distress, or a refusal to surrender property on which one has a lien. Pederson v. Thoeny, 88 M 569, 295 P 250 (1930).

Threat to Prosecute:

A threat to send one to the penitentiary for an alleged crime unless he execute a promissory note and a mortgage securing it constitutes menace, and renders the instruments thereupon executed void, since the element of consent freely given, indispensable to a valid contract, is absent in such a case. Averill Mach. Co. v. Taylor, 70 M 70, 223 P 918 (1924).

A threat to prosecute one for a crime of which he is not guilty constitutes menace. Averill Mach. Co. v. Taylor, 70 M 70, 223 P 918 (1924).

Collection of Debt: Plaintiff's testimony in his action to recover $200, claimed to have been obtained from him by defendant gas company by the use of threats, showed that he had surreptitiously used gas without the same having first passed through the gas meter, that defendant's manager upon discovery of that fact had threatened him that unless he paid the $200 he would send him to the penitentiary, and that thereupon to avoid prosecution or being sent to prison he made payment. He contended, however, that he had used only $10 worth, and a motion for nonsuit was improperly granted, since the testimony would have justified a finding that the threats were made for an unlawful purpose—the collection of a debt—and that the acts of defendant's manager constituted a menace under this section. Clifford v. Great Falls Gas Co., 68 M 300, 216 P 1114 (1923). See also Fronk v. Collins, 2011 MT 315, 363 Mont. 110, 266 P.3d 1271, which held that the parties' contract did not suffer from lack of consent due to menace when the communication was between the parties' attorneys; the communication did not threaten imprisonment to compel payment, but only mentioned criminal and civil remedies; and the parties were free to abandon negotiations at any time.

28-2-404. Kinds of fraud.

Case Notes

Sufficient Evidence to Conclude Bank Committed Actual Fraud: The plaintiff financed a home through the defendant bank's predecessor. The plaintiff requested a 30-year residential loan and was told by the bank that she received this loan. However, the bank issued an 18-month commercial loan and did not inform the plaintiff. The plaintiff sued alleging fraud. On the first appeal, the Supreme Court found that several sworn affidavits presented by the defendant were false. On remand, the defendant failed to supplement discovery. A jury awarded $1 million in compensatory damages and $5 million in punitive damages in favor of the plaintiff. The defendant appealed, stating that the evidence did not support a finding of actual fraud. The Supreme Court disagreed, finding that all nine elements of actual fraud were satisfied. McCulley v. U.S. Bank of Montana, 2015 MT 100, 378 Mont. 462, 347 P.3d 247.

Statute of Frauds — No Bar to Fraud Claim: Because the plaintiffs were not merely seeking to enforce an oral agreement, the Supreme Court overturned a District Court finding that the statute of frauds precluded a plaintiff's claim of actual fraud, constructive fraud, and violations of the Montana Consumer Protection Act. Rather, the plaintiffs were alleging that the defendants misrepresented an existing real estate loan and serviced the loan in an unfair and deceptive manner, a claim that relied on the oral contract as evidence of alleged fraud but that did not rely on the validity of the oral contract itself. Morrow v. Bank of America, N.A., 2014 MT 117, 375 Mont. 38, 324 P.3d 1167. However, see Bank of America, N.A. v. Alexander, 2017 MT 31, 386 Mont. 305, 389 P.3d 1020, in which a claim that the parties modified an oral agreement was dismissed because it was barred by the statute of frauds.

Inability to Obtain Real Estate Financing — Return of Earnest Money Proper: Defendants secured prequalification on a real estate loan and, pursuant to the buy-sell agreement, paid $53,000 in earnest money to purchase a condominium from plaintiff. The buy-sell agreement required the defendants to obtain financing for the remaining $946,000 of the purchase price. However, the economic climate later changed and required the need for a larger down payment, which defendants did not have. Defendants notified plaintiff and requested the return of the earnest money, but plaintiff refused and filed a fraud action, contending that defendants falsely represented their borrowing status and failed to obtain the required financing. The District Court summarily dismissed the fraud claims because the purchase agreement provided that if conventional financing could not be obtained, the agreement was void. On appeal, plaintiff asserted that a genuine issue of material fact remained regarding the fraud claims, precluding summary judgment. The Supreme Court disagreed. It was undisputed that defendants applied for loans and were prequalified for financing, so defendants did not misrepresent their borrowing status. Summary dismissal of the fraud claims was appropriate as a matter of law, particularly because plaintiff had the opportunity to be heard on the issue. The District Court properly terminated the purchase agreement when defendants could not obtain financing, and plaintiff was correctly ordered to return the earnest money. Mill Creek Ltd. Partnership v. Lodge, 2010 MT 65, 355 Mont. 478, 228 P.3d 1144.

Sufficient Evidence of Negligent Misrepresentation — Summary Judgment Proper: Plaintiffs sued for negligent misrepresentation because defendants allegedly misled plaintiffs regarding the output of a well on a subdivision lot purchased by plaintiffs. The District Court granted summary judgment for plaintiffs, and defendants appealed. The Supreme Court applied the elements in Cechovic v. Hardin & Associates, Inc., 273 M 104, 902 P2d 520 (1995), to determine whether the record affirmatively established that defendants made a false representation as to a past or existing material fact without any reasonable ground for believing it to be true, with the intent to induce plaintiffs' reliance, and that plaintiffs, unaware of the falsity of the representation, justifiably relied on the representation and suffered damage as a result of the reliance. Plaintiffs established that they had inquired about the well output on numerous occasions and that defendants indicated at closing that the well produced 3,600 gallons of water a day, even though they knew that the well produced only 700 gallons a day. Plaintiffs also established that they relied on defendants' representation and that they suffered damages by having to install a cistern and to haul water to the property instead of using the well. Evidence of negligent misrepresentation was thus proved and summary judgment for plaintiffs was affirmed. Walters v. Luloff, 2008 MT 17, 341 M 158, 176 P3d 1034 (2008).

No Actual Malice Shown in Replacement of Seed With Different Variety: Plaintiff delivered a load of wheat seed to defendant's facility for cleaning and treating. Defendant inadvertently dumped the load into a waste bin, replaced the seed with a similar but different variety, and charged plaintiff for cleaning and treatment without informing plaintiff of the error. When the crop came up, plaintiff noticed that the seed was a different variety, sued defendant for negligent misrepresentation, and sought compensatory and punitive damages. The District Court found no actual malice on defendant's part and declined to award punitive damages. On appeal, the Supreme Court affirmed. Substantial credible evidence showed that defendant's personnel assumed that plaintiff was planting a variety that was commonly used in the area and substituted that common variety, assuming that no injury would result in the misrepresentation that the seed plaintiff was going to plant was the same seed plaintiff delivered. Defendant neither had knowledge of facts nor intentionally disregarded facts that created a high probability of injury to plaintiff, so the definition of actual malice was not met and the District Court correctly declined to award punitive damages without a finding of actual malice. Hallenberg v. Gen. Mills Operations, Inc., 2006 MT 191, 333 M 143, 141 P3d 1216 (2006).

Fraud Committed in Course of Dissolution Proceeding Considered Intrinsic — Claim of Extrinsic Fraud Properly Dismissed: Castonguay brought a claim against her ex-husband, Andrew, on grounds that Andrew offered perjured testimony in a prior dissolution proceeding regarding Andrew's ownership of real property and that the conflicting statements acted as extrinsic fraud on the trial court and resulted in the court awarding Andrew more property than he was entitled to. Castonguay's claim was summarily dismissed on grounds that Castonguay failed to submit any evidence of extrinsic fraud, and Castonguay appealed. The Supreme Court cited Clark v. Clark, 64 M 386, 210 P 93 (1922), for the holding that acts for which a judgment or decree may be set aside or annulled on grounds of fraud have reference only to fraud that is extrinsic or collateral to the matter tried by the court and not to fraud that is intrinsic to the matter on which judgment was rendered. Castonguay's alleged facts, if taken as true, amounted to perjury intrinsic to the dissolution proceeding. Because Castonguay failed to offer evidence of extrinsic fraud for which relief could be granted, Castonguay's claim was properly dismissed. Castonguay v. Estate of Polson, 2005 MT 265, 329 M 103, 122 P3d 1208 (2005).

Previously Raised but Unlitigated Alter Ego Claim Not Barred by Res Judicata: Following a dispute over the sale of irrigation equipment, H-D Irrigating and Lane sued Kimble Properties and Kimble for false representation of the irrigation equipment and damages. Kimble Properties and Kimble counterclaimed for the balance due on the equipment, alleging that H-D Irrigating was a sham and the alter ego of Lane. The alter ego claim was never pursued. The Supreme Court eventually decided the case in H-D Irrigating, Inc. v. Kimble Properties, Inc., 2000 MT 212, 301 M 34, 8 P3d 95 (2000), and remanded for judgment in favor of Kimble. In an effort to collect, Kimble sought to compel Lane to testify regarding the assets of H-D Irrigating, but rather than appear, Lane filed bankruptcy and received a stay on further proceedings. Kimble then filed an action to collect from Lane personally, again raising the alter ego issue. Lane asserted that the issue had been already decided in the prior litigation and sought supervisory control on res judicata grounds. After accepting supervisory control, the Supreme Court decided that res judicata did not bar Kimble's litigation of the alter ego claim. The action to pierce the H-D

Irrigating corporate veil was neither previously adjudicated in District Court nor were the facts upon which the claim was based known to Kimble at the time that the counterclaim was filed or at any other time during the course of the previous action. The case was thus remanded for further proceedings on the alter ego claim. Lane v. District Court, 2003 MT 130, 316 M 55, 68 P3d 819 (2003), applying Berlin v. Boedecker, 268 M 444, 887 P2d 1180 (1994).

Six Elements Required to Prove Negligent Misrepresentation — Exercise of Due Care Question for Jury: A real estate broker appealed a verdict finding that an employee had negligently misrepresented the boundary of property purchased by the Cechovics. The Supreme Court held that a plaintiff had to prove the following six elements in order to show negligent misrepresentation: (1) the defendant made a representation as to a past or existing fact; (2) the representation was untrue; (3) the defendant made the representation without any reasonable ground for believing it to be true; (4) the representation was made with the intent to induce the plaintiff to rely on it; (5) the plaintiff was unaware of the falsity of the representation and was justified in relying on it; and (6) the plaintiff was damaged as a result of relying on the representation. The Supreme Court also held that in addition to the six elements, the plaintiff had to show that the defendant failed to exercise due care in obtaining or communicating the information and that the question of whether the defendant had exercised due care was for the jury and would not be overturned on appeal so long as there was substantial evidence to support the jury's finding. Cechovic v. Hardin & Associates, Inc., 273 M 104, 902 P2d 520, 52 St. Rep. 854 (1995), followed in Walters v. Luloff, 2008 MT 17, 341 M 158, 176 P3d 1034 (2008). However, see Morrow v. Bank of America, N.A., 2014 MT 117, 375 Mont. 38, 324 P.3d 1167.

No Evidence of Fraud — Summary Judgment Appropriate:

When a lender brought suit to foreclose on a promissory note, defendant filed counterclaims, alleging fraud and economic duress. Summary judgment in favor of the lender was proper because the defendant did not make an issue of material fact for fraud. The lender's alleged withdrawal of a promise to add delinquent payments to the end of the contract does not amount to fraud. Avco Financial Serv. v. Foreman-Donovan, 237 M 260, 772 P2d 862, 46 St. Rep. 785 (1989), followed in Bengala v. Conservative Sav. Bank, 250 M 101, 818 P2d 371, 48 St. Rep. 880 (1991).

Since 28-2-404 does not preclude summary judgment when there is no evidence supporting a claim of fraud, under former Rule 56(c), M.R.Civ.P. (now superseded), summary judgment was appropriate. Campbell v. Campbell, 223 M 124, 725 P2d 207, 43 St. Rep. 1584 (1986), followed in Smith v. Howery, 227 M 284, 738 P2d 502, 44 St. Rep. 1085 (1987).

General Assertions of Fraud — Defendant Properly Dismissed: The wife of a defendant convicted of fraudulent misrepresentation of income when selling a business was properly dismissed as a defendant when general assertions of fraud revealed only her involvement as co-owner of the business, her performance of some business bookkeeping functions, and her presence at a few meetings where the sale was discussed. None of the elements of fraud were established by evidence. Selvidge v. McBeen, 230 M 237, 750 P2d 429, 45 St. Rep. 168 (1988). See also Aldrich & Co. v. Donovan, 238 M 431, 778 P2d 397, 46 St. Rep. 1393 (1989).

Dual Prongs for Piercing Corporate Veil — Evidence of Fraud Sufficient: There are two prongs to piercing the corporate veil. First, the person purporting to represent the corporation must be found to be the corporate "alter ego". Second, there must be a showing that the corporate entity was used as a subterfuge to defeat public convenience, justify wrong, or perpetrate either actual or constructive fraud. Drilcon, Inc. v. Roil Energy Corp., Inc., 230 M 166, 749 P2d 1058, 45 St. Rep. 114 (1988), followed in Berlin v. Boedecker, 268 M 444, 887 P2d 1180, 51 St. Rep. 569 (1994).

Instruction Given on Constructive Fraud — Instruction on Bad Faith Superfluous: The District Court instructed the jury on constructive fraud but not on breach of the implied covenant of good faith and fair dealing, which plaintiff contended was error. The Supreme Court noted that the jury found no breach of duty under the instruction on constructive fraud, which does not require a showing of fraudulent intent. An instruction on bad faith would require plaintiff to prove intentional concealment. The court held that if plaintiff could not meet the burden of proof on constructive fraud, she could not meet the higher burden of proof on bad faith; thus, the instruction would have been superfluous. Bushnell v. Cook, 221 M 296, 718 P2d 665, 43 St. Rep. 825 (1986), partially overruled in Cechovic v. Hardin & Associates, Inc., 273 M 104, 902 P2d 520, 52 St. Rep. 854 (1995).

Instruction on Negligent Misrepresentation Not Given — Action for Fraud: There was no error when District Court instructed the jury on constructive fraud but not on negligent misrepresentation. In Montana, an action for negligent misrepresentation is an action for fraud, so the jury was adequately instructed. Bushnell v. Cook, 221 M 296, 718 P2d 665, 43 St. Rep. 825 (1986), partially overruled in Cechovic v. Hardin & Associates, Inc., 273 M 104, 902 P2d 520, 52 St. Rep. 854 (1995).

Fiduciary Relationship Basis for Constructive Fraud Cause of Action: Dealings or transactions between parties who have a fiduciary relationship provide a sufficient contract to support an action for constructive fraud. Local Union No. 400 v. Bosh, 220 M 304, 715 P2d 36, 43 St. Rep. 388 (1986). See also Luke v. Gager, 2000 MT 377, 303 M 474, 16 P3d 377, 57 St. Rep. 1599 (2000).

False Representation as Actual Fraud — No Directed Verdict: Defendants contended that plaintiffs' evidence was insufficient to establish a false representation or justifiable reliance on the representation and that therefore defendants' motions for a directed verdict were improperly denied. The Supreme Court noted that a prospectus given to plaintiff, McGregor, contained financial statements which would be misleading to someone not knowledgeable in accounting and that a jury could find that false representations were made on this evidence. The court found that McGregor adequately investigated the business and reasonably relied on defendants' representations. The Supreme Court found no error in the District Court's failure to direct a verdict for defendants on the claim of actual fraud. McGregor v. Cushman/Mommer, 220 M 98, 714 P2d 536, 43 St. Rep. 206 (1986).

Parol Evidence Rule — Constructive Fraud as Within the Exception: Defendant represented plaintiff in a civil action in federal court. The parties agreed that the case was originally handled on a 50% contingency fee basis. The case lasted almost 10 years. Plaintiff signed a formal authorization for defendant to settle. At the time of settlement, plaintiff contended the parties agreed to replace their 50% of net fee agreement with a percentage distribution of the gross settlement amount. At some point in time, the parties signed an agreement in defendant's handwriting providing for a 75%-25% split of the settlement. The agreement contained a clause stating the agreed sums had been paid in full. Plaintiff contended defendant had retained half the settlement. Defendant contended that the trial court erred in permitting plaintiff to testify concerning the agreement. On appeal, the Supreme Court held that the fraud exception to the parol evidence rule addresses both actual and constructive fraud. The court stated that constructive fraud often exists where the parties to a transaction have a special confidential or fiduciary relation which affords the power and means to one to take undue advantage of or exercise undue influence over the other. The attorney-client relationship is a fiduciary one. Evidence presented along with plaintiff's testimony established constructive fraud on defendant's part. The court held that plaintiff's claim of conduct against defendant, which constituted at least constructive fraud, fell within the ambit of the fraud exception of the parol evidence rule. Eaton v. Morse, 212 M 233, 687 P2d 1004, 41 St. Rep. 1708 (1984).

Constructive Fraud as Basis for Punitive Damages: Section 27-1-221 allows punitive damages for fraud. Section 28-2-404 specifically defines fraud as including constructive fraud. The breach of a fiduciary relationship constituting a constructive fraud forms the basis for an award of punitive damages. Purcell v. Automatic Gas Distrib., Inc., 207 M 223, 673 P2d 1246, 40 St. Rep. 1997 (1983).

Actual Fraud — Summary Judgment Precluded: Actual fraud is a question of fact. Therefore, summary judgment is precluded where willful misrepresentations amounting to fraud are alleged. Jenkins v. Hillard, 199 M 1, 647 P2d 354, 39 St. Rep. 1156 (1982).

Negligent Misrepresentation by a Stockbroker: A stockbroker testified that what he told a customer regarding the risk of a transaction he believed to be true. The customer testified that he did not believe he had been deliberately misinformed by the broker. However, one who in the course of a transaction in which he has a pecuniary interest supplies information for the guidance of others in their transactions must exercise reasonable competence in obtaining or communicating the information. Negligent as well as intentional misrepresentation can be the basis of a tort action in fraud. Brown v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 197 M 1, 640 P2d 453, 39 St. Rep. 305 (1982), followed in Wagner v. Cutler, 232 M 332, 757 P2d 779, 45 St. Rep. 1092 (1988).

Possible Differing Conclusions — No Directed Verdict: Plaintiff applied to defendant for health coverage for himself and his family. He met with an agent who filled out the application, which was signed by both parties. Plaintiff was not given a copy of the application or contract and was not advised that the application was part of the contract. The application was accepted. The family contracted medical bills which defendant declined to pay, claiming that the bills stemmed from "preexisting conditions" not covered by the contract. Defendant then unilaterally canceled the contract, claiming plaintiff had misrepresented his family's health in the application, and plaintiff filed suit. Defendant moved for a directed verdict on the issues of actual and constructive fraud and the tort of bad faith, which was denied. If the representations that induced the plaintiff to enter the contract were false, he would have a case in fraud. If the contract were breached, a cause of action may sound in tort, although it arises out of a breach of contract, if the defaulting party by breaching the contract also breaches the duty to act in good faith owed to the other party independently of the contract. The evidence viewed in a light most favorable to plaintiffs indicated reasonable men could differ as to the conclusions drawn from the evidence. Therefore, the directed verdict was properly denied. Weber v. Blue Cross of Mont., 196 M 454, 643 P2d 198, 39 St. Rep. 245 (1982).

Question of Fraud — No Summary Judgment: When a lessee alleged fraud in the termination of his lease, he was not entitled to a summary judgment since fraud is always a question of fact. Chamberlain v. Evans, 180 M 511, 591 P2d 237 (1979).

Contract to Divide Commission: Where an oral contract was made between two real estate brokers to divide a commission, fraud in failing to perform was not proved when there was a possibility the sale would not go through, since the mere fact that a promise was not carried out is not proof that such promise was made with no intention to perform. Reilly v. Maw, 146 M 145, 405 P2d 440 (1965).

Fraud Not Presumed: Actual fraud is always a question of fact to be established by competent evidence, since fraud cannot be presumed. Reilly v. Maw, 146 M 145, 405 P2d 440 (1965); Harrison v. Riddell, 64 M 466, 210 P 460 (1922).

Burden of Proof:

Where the plaintiff charged actual fraud on the part of the defendant, the burden of establishing such fact was on plaintiff. Hjermstad v. Barkuloo, 128 M 88, 270 P2d 1112 (1954).

In an action based on fraud the question whether actual fraud has been practiced is one of fact, and the burden of proof is upon him who alleges it. Lee v. Stockmen's Nat'l Bank, 63 M 262, 207 P 623 (1922).

Inference of Fraud:

The question of fraud is always a question of fact for the jury, unless the evidence is uncontradicted and it is impossible to draw any inference from it other than that it entered into the particular transaction, whereupon it becomes one of law for the court. Williams v. Mut. Life Ins. Co. of New York, 61 M 66, 201 P 320 (1921).

Where the facts in an action for fraud are not controverted and furnish the basis of but one inference, namely that the defendant is guilty of the fraud alleged, the court may infer the fraud as a matter of law and direct a verdict in favor of plaintiff. Shoudy v. Reeser, 48 M 579, 142 P 205 (1914).

Concealment of Facts: Whether an applicant for life insurance intentionally concealed facts which are material, or made false representations with reference to them, intending to deceive the insurer, thus being guilty of actual fraud, was a question of fact for the jury. Pelican v. Mut. Life Ins. Co. of New York, 44 M 277, 119 P 778 (1911).

28-2-405. What constitutes actual fraud.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Elements of Fraud 142
Pleadings and Proof 145
Defenses 148
False Representations 149
Promises 152
Damages 153
Miscellaneous 153

ELEMENTS OF FRAUD

Sufficient Evidence to Conclude Bank Committed Actual Fraud: The plaintiff financed a home through the defendant bank's predecessor. The plaintiff requested a 30-year residential loan and was told by the bank that she received this loan. However, the bank issued an 18-month commercial loan and did not inform the plaintiff. The plaintiff sued alleging fraud. On the first appeal, the Supreme Court found that several sworn affidavits presented by the defendant were false. On remand, the defendant failed to supplement discovery. A jury awarded $1 million in compensatory damages and $5 million in punitive damages in favor of the plaintiff. The defendant appealed, stating that the evidence did not support a finding of actual fraud. The Supreme Court disagreed, finding that all nine elements of actual fraud were satisfied. McCulley v. U.S. Bank of Montana, 2015 MT 100, 378 Mont. 462, 347 P.3d 247.

Tort Claims Not Precluded by Parties Contracting on Same Matter: The parties entered into an agreement for the defendant to purchase the plaintiff's home. After the defendant reneged on the agreement, the plaintiff filed an action for fraud, deceit, and negligence. The District Court dismissed the claims based on its conclusion that the plaintiff's injuries resulted from the defendant's breach of contract and therefore she was precluded from bringing any tort claims against him. The plaintiff appealed. The Supreme Court explained that tort claims are not prohibited simply because the parties have entered into a contract on the same matter. However, given that the plaintiff had offered only speculative statements regarding the fraud and deceit claims, the Supreme Court agreed with the District Court's grant of summary judgment on behalf of the defendant on those claims, but it remanded the matter to the District Court to allow the negligence claim to proceed. Dewey v. Stringer, 2014 MT 136, 375 Mont. 176, 325 P.3d 1236.

Actual Fraud — Speaker's Knowledge of False Representation or Ignorance of Its Truth Required: Actual fraud does not require the speaker's knowledge of a statement's falsity but may also be proven if the defendant is ignorant of whether the statement is true. Morrow v. Bank of America, N.A., 2014 MT 117, 375 Mont. 38, 324 P.3d 1167.

Fraud Substantiated in Attorney's Handling of Probate Case — Violation of Attorney's Duty of Truthfulness — Public Censure Warranted: Attorney Potts represented parties in a will contest. Two of the parties knew that some joint tenancy accounts were not included in the value of the estate and, in an attempt to secure the funds in the accounts, directed Potts to remain silent as to whether the settlement agreement prepared by Potts included the accounts. Potts failed to notify the court and counsel for the estate that one of his clients intended to obtain the jointly held property regardless of the outcome of any settlement. The Supreme Court subsequently determined in In re Estate of Stukey, 2004, MT 279, 323 M 241, 100 P3d 114 (2004), that the parties intended that the total estate value, including the joint tenancy accounts, be included in the settlement. A professional misconduct complaint was later filed against Potts, alleging that Potts engaged in or assisted in client fraud by failing to disclose material information to opposing counsel and that Potts breached the duty of candor to the tribunal by failing to disclose material information to the court. The Commission on Practice found that Potts knew that his clients were using Potts' services to perpetuate fraud in violation of Rules 1.2(d) and 3.3(a)(2) of the Montana Rules of Professional Conduct (MRPC), that Potts failed to fulfill his ethical obligation to inform the clients that he would not participate in the fraudulent conduct, a violation of Rule 1.2(d), MRPC, and that Potts violated the duty of candor to the tribunal in violation of Rule 3.3(a)(2), MRPC. The Commission recommended that Potts be publicly censured and suspended from the practice of law for 30 days. Potts appealed, raising issues of client confidentiality, asserting that his clients did not engage in fraud because the accounts passed to his client as a matter of law and thus could not have been included as part of the settlement basis, contending that he had no duty to correct opposing counsel's erroneous understanding of the settlement, and arguing that the Commission's proposed sanctions were inappropriate. The Supreme Court held that, by definition, Potts' clients were engaged in fraudulent conduct, that Potts assisted in the conduct by not disclosing the conduct to the court and to opposing counsel in violation of the duty of truthfulness and by drafting a stipulation stating that all disputes had been settled when he knew that the parties relied on a misrepresentation in drafting a settlement, and that Potts could have avoided the situation by withdrawing from representation. Potts' conduct resulted in considerable injury to the parties, requiring one District Court proceeding and two appeals to determine the meaning and scope of the stipulation. The Commission's findings were affirmed. However, the court reversed the suspension of Potts' practice in light of mitigating factors of Potts' history of compliance with the rules of professional conduct and his good character and reputation to this point and held that public censure sufficed to apprise Potts of the gravity of the misconduct. In re Potts, 2007 MT 81, 336 M 517, 158 P3d 418 (2007).

Rescission of Waiver of Interest Document on Grounds of Fraud: Kindsfather's son purchased some land from Kindsfather pursuant to a contract for deed. When the son was unable to make the payments, the son executed a document waiving the back interest that was owing and Kindsfather signed the document. Kindsfather subsequently died, and the son sought a declaratory ruling that the waiver of interest document was valid and that upon receipt of the unpaid balance of the contract, the bank would release the warranty deed held in escrow for the son. Kindsfather's personal representative opposed the judgment, and the District Court found the document to be invalid and ordered the son to make all payments due to the estate. On appeal, the Supreme Court affirmed the District Court's decision to rescind the document because it was obtained by fraud. The Supreme Court examined each of the nine elements of actual fraud and determined that a prima facie case of actual fraud was established. In re Estate of Kindsfather, 2005 MT 51, 326 M 192, 108 P3d 487 (2005), following Davis v. Church of Jesus Christ of Latter Day Saints, 258 M 286, 852 P2d 640 (1993).

Real Estate Sale — Acknowledgment of Offer as Acceptance of Offer — Elements of Fraud Fulfilled: When Frye, a real estate broker, brought May a written offer to purchase May's gas station, Frye asked that May initial the offer to show acknowledgment or receipt of the offer, and May initialed the line reading "Seller Signature". At some later time, the terms of a counteroffer were inserted above May's initials, and the counteroffer was accepted by the buyer without May's knowledge. May consummated the sale and then sued Frye. The Supreme Court held that the District Court improperly granted Frye's motion for summary judgment and held that May had shown sufficient evidence of fraud, including misrepresentation of a material fact, that being the meaning of May's initialing of the line marked "Seller Signature", to survive a motion for summary judgment. May v. ERA Landmark Real Estate of Bozeman, 2000 MT 299, 302 M 326, 15 P3d 1179, 57 St. Rep. 1256 (2000).

Nine Elements of Fraud Applied in Workers' Compensation Case: Taylor submitted workers' compensation claims for three injuries that he alleged occurred in February and November of 1990 and in April of 1991. State Fund paid benefits but later asserted that the claims were fraudulent and then denied benefits. Taylor filed a petition to have the benefits reinstated, and the Workers' Compensation Court found that two of claims were fraudulent. The Supreme Court held that there was substantial credible evidence to support the Workers' Compensation Court's holding that State Fund proved the nine elements of fraud on two of Taylor's three claims. Taylor v. St. Comp. Ins. Fund, 275 M 432, 913 P2d 1242, 53 St. Rep. 201 (1996).

Failure to Keep Promise to Pay Medical Bills if Injured Person Travels to Exam — No Fraud: The District Court properly granted the church summary judgment on issues of fraud and misrepresentation in an action arising after plaintiff fell and was injured on church property. Plaintiff claimed that the church agreed in writing to pay medical bills if plaintiff would travel to Salt Lake City for a medical exam. Plaintiff did so, and the church failed to pay. The promise to pay money in the future was not a representation, the first element of a prima facie case for fraud or misrepresentation. Davis v. Church of Jesus Christ of Latter Day Saints, 258 M 286, 852 P2d 640, 50 St. Rep. 535 (1993).

Alleged Representations Regarding Conditions of Loan Agreement — Failure of Fraud Claim Due to Admissions of Party: Debtor claimed actual or constructive fraud based on bank president's alleged representations that the due date on a note would not be enforced and that the note would only become due if the bank deemed itself insecure or if the debtor violated the agreement. However, debtor's statements and admissions directly conflicted with the claimed representations, and in light of debtor's subsequent violation of the agreement, the claim of fraud failed. Citizens First Nat'l Bank of Wolf Point v. Moe Motor Co., 248 M 495, 813 P2d 400, 48 St. Rep. 528 (1991).

Attorneys' Alleged Failure to Advise on Contingent Fee Arrangement — No Fraud: Where attorneys representing Howerys in a condemnation action allegedly failed to advise Howerys that the written contingent fee contract included a proportionate amount of any interest awarded on the judgment, the District Court properly concluded that any such failure would be insufficient in law to support any of the claims made by the Howerys. Smith v. Howery, 227 M 284, 738 P2d 502, 44 St. Rep. 1085 (1987).

Action to Set Aside Quitclaim Deed — Failure to Prove Fraud: The plaintiff, son of a deceased rancher, received 24½% of the surface rights to his father's ranch in accordance with the terms of an estate plan established for the benefit of the plaintiff and his brothers, the defendants. Upon leaving the ranch, plaintiff executed one quitclaim deed to his mineral interest in 1977 and one quitclaim deed to his surface interest in 1968 in exchange for a promise that the defendants would hold him harmless on a promissory note. The District Court did not err (in a subsequent challenge by the plaintiff to the validity of the quitclaim deeds) in declaring both deeds to be valid and denying the plaintiff any interest in the ranch. The District Court properly found that the evidence does not support a finding of fraud. The plaintiff did not satisfy all nine parts of the test set out in Van Ettinger v. Pappin, 180 M 1, 588 P2d 988 (1978). The plaintiff did not have to rely on the advice given him, did not prove that the defendants knew their representations were anything but true, and did not show that those representations were false or anything but good business sense. Turley v. Turley, 199 M 265, 649 P2d 434, 39 St. Rep. 1336 (1982).

Nine Elements: Appellants must have the ability to make a prima facie showing of nine elements to support their claim of fraud: (1) a representation; (2) falsity of the representation; (3) materiality of the representation; (4) speaker's knowledge of the falsity of the representation or ignorance of its truth; (5) speaker's intent that it be relied on; (6) hearer's ignorance of the falsity of the representation; (7) hearer's reliance on the representation; (8) hearer's right to rely on the representation; and (9) consequent and proximate injury caused by reliance on the representation. Van Ettinger v. Pappin, 180 M 1, 588 P2d 988 (1978), followed in McGregor v. Cushman/Mommer, 220 M 98, 714 P2d 536, 43 St. Rep. 206 (1986), and Krone v. McCann, 197 M 380, 642 P2d 584, 39 St. Rep. 500 (1982). See also Wiberg v. 17 Bar, Inc., 241 M 490, 788 P2d 292, 47 St. Rep. 429 (1990), McNeil v. Currie, 253 M 9, 830 P2d 1241, 49 St. Rep. 312 (1992), Somersille v. Columbia Falls Aluminum Co., 255 M 101, 841 P2d 483, 49 St. Rep. 904 (1992), Barrett v. Holland & Hart, 256 M 101, 845 P2d 714, 49 St. Rep. 1156 (1992), (Barrett was followed in Hickingbotham v. Duncan, 271 M 525, 898 P2d 1215, 52 St. Rep. 574 (1995)), and 50 St. Rep. 63 (1993), Story v. Bozeman, 259 M 207, 856 P2d 202, 50 St. Rep. 761 (1993), NW. Truck & Trailer Sales, Inc. v. Dvorak, 269 M 150, 887 P2d 260, 51 St. Rep. 1530 (1994), Taylor v. St. Comp. Ins. Fund, 275 M 432, 913 P2d 1242, 53 St. Rep. 201 (1996), and In re Estate of Kindsfather, 2005 MT 51, 326 M 192, 108 P3d 487 (2005).

Fraud — Essential Elements: When buyers inspected property purchased and during trial for damages for fraud never stated they would not have entered a purchase agreement had they known falsity of buyer's alleged misrepresentation, they cannot maintain an action based on such alleged misrepresentation. Schulz v. Peake, 178 M 261, 583 P2d 425 (1978).

Prima Facie Case: A party asserting fraud in the execution of a contract (mortgage), to make out a prima facie case, must show a false representation, its materiality, the speaker's knowledge of its falsity or his ignorance of the truth, his intent that it should be acted upon by the party claiming to have been defrauded, the latter's ignorance of its falsity, his reliance on its truth, his right to rely thereon, and his consequent and proximate injury. Morigeau v. Lozar, 81 M 434, 263 P 985 (1928).

Actual Fraud in Contract: The elements of actual fraud in a contract of sale are: a false representation, its materiality, the seller's knowledge of its falsity or ignorance of its truth, his intent that it should be acted upon by the buyer, the latter's ignorance of its falsity, reliance upon its truth, and his consequent and proximate injury; and where the injured party had made out a prima facie case embracing such elements, it is error to direct a verdict for his opponent, the question whether or not there has been fraud generally being a question of fact for the jury. Healy v. Ginoff, 69 M 116, 220 P 539 (1923), followed in McGregor v. Cushman/Mommer, 220 M 98, 714 P2d 536, 43 St. Rep. 206 (1986), followed in H-D Irrigating, Inc. v. Kimble Properties, Inc., 2000 MT 212, 301 M 34, 8 P3d 95, 57 St. Rep. 832 (2000). See also Dewey v. Stringer, 2014 MT 136, 375 Mont. 176, 325 P.3d 1236.

Jury Submission — What Needed: To make out a prima facie case of fraud sufficient to go to the jury, the plaintiff must show a false representation by defendant, its materiality, defendant's knowledge of its falsity or ignorance of its truth, his intent that it should be acted upon by plaintiff in the manner reasonably contemplated, his reliance upon its truth, his right to rely thereon, and his consequent and proximate injury. Lee v. Stockmen's Nat'l Bank, 63 M 262, 207 P 623 (1922).

Belief and Action Required: In order to recover under a contract allegedly entered under fraud, plaintiff must show with reasonable certainty: (1) that the defendant made a representation or statement intending that the plaintiff act upon it; (2) that the representation was false; (3) that the plaintiff believed the statement; and (4) that he acted upon it. Power & Bro., Ltd. v. Turner, 37 M 521, 97 P 950 (1908).

PLEADINGS AND PROOF

Legal Malpractice — Nexus Between Fraudulent Concealment and Discovery Rule: In the context of legal malpractice, a nexus exists between a defendant's fraudulent concealment and the question of whether a plaintiff should have discovered the defendant's negligent act. Estate of Watkins v. Hedman, Hileman & Lacosta, 2004 MT 143, 321 M 419, 91 P3d 1264 (2004). See also Watkins Trust v. Lacosta, 2004 MT 144, 321 M 432, 92 P3d 620 (2004).

Sale of Home by Realtors — Negligent Misrepresentation, Actual and Constructive Fraud, and Real Estate Licensing and Consumer Protection Laws — Expert Witnesses Unnecessary to Prove Standard of Care: Durbins purchased a home through the seller's realtors. Contrary to the representations of the realtors, Durbins discovered that the property had no legal septic system, that the household water was unsafe to use for any purpose, and that the access road was located on the neighbor's property. Durbins brought an action against the realtors, alleging negligent misrepresentation, actual and constructive fraud, and statutory violations involving the Montana real estate licensing laws and the Montana Unfair Trade Practices and Consumer Protection Act of 1973. The defendants sought and achieved dismissal of the case on the grounds that Durbins failed to prove through expert testimony the applicable standard of care of the realtors. The Supreme Court held that because Durbins did not allege professional misrepresentation, the issues of whether the realtors negligently misrepresented the facts, were guilty of actual or constructive fraud, or were guilty of the statutory violations alleged by Durbins, were questions resolvable by common knowledge. The questions did not turn on a standard peculiarly within the knowledge of an expert witness, and scientific, technical, or other specialized knowledge was not necessary to assist the jury. The Supreme Court therefore held that Durbins were not required to provide expert standard of care testimony to establish any of the violations. Durbin v. Ross, 276 M 463, 916 P2d 758, 53 St. Rep. 471 (1996).

Fraud — Refusal to Instruct on Actual Fraud Affirmed: The Supreme Court ruled that an instruction on actual fraud was warranted only if the requesting party raised a question of fact by presenting some evidence on each of the nine elements of actual fraud. The District Court did not err in refusing to instruct the jury on actual fraud when the defendant failed to introduce evidence that the bank made a knowingly false representation and intended the defendant to rely on it to his detriment. First Bank-Billings v. Clark, 236 M 195, 771 P2d 84, 46 St. Rep. 291 (1989).

Corporate Fraud Not Shown With Particularity: Claim of plaintiff who asserted fraud in sale of his interest in a corporation was summarily dismissed upon his failure to produce documentation showing any misrepresentation or to allege fraud with particularity. Pipinich v. Battershell, 232 M 507, 759 P2d 148, 45 St. Rep. 1237 (1988).

No Material Fact to Support Fraud Claims: Plaintiff brought action for fraud, both actual and constructive, as well as undue influence, arising out of a promise by his mother to compensate plaintiff, upon sale of the family corporation's assets, for a portion of value attributable to plaintiff's stock and partnership interest conveyed to corporation for cancellation of promissory note executed by plaintiff for a loan from the corporation. The respondent mother was granted summary judgment. The Supreme Court held that plaintiff failed to establish a fraud claim because of admissions that his mother did not intend to deceive him and that he never relied on his mother's promise to compensate. His claims were also barred by the Statute of Limitations. Fleming v. Fleming Farms, Inc., 221 M 237, 717 P2d 1103, 43 St. Rep. 776 (1986).

Issue of Fact as to Whether Promissory Note Procured by Fraud: In 1978, plaintiff had leased a number of mink to defendants in return for payment by defendants of a portion of the annual kit crop. At the time of the lease, plaintiff strongly suspected that a small percentage of the mink were infected with Aleutian Disease (AD), a disease impairing mink productivity and resistance to other diseases. In December 1980, after 2 years of greater than normal losses among the leased mink, the parties replaced the lease with a promissory note containing a clause releasing plaintiff from any liability arising out of the lease. After the promissory note had been made, plaintiff informed defendants that tests of his mink in November 1980 indicated that 30% were infected with AD. Subsequent testing of defendants' mink revealed that 70% had AD. Defendants made no payments on the note. In a suit on the note, defendants counterclaimed, alleging that the note had been procured by fraud. The District Court granted plaintiff's motion for summary judgment. The Supreme Court reversed, ruling that defendants' affidavit indicated an issue of material fact, i.e., whether defendants learned that the mink had AD before or after the note was signed, and that the plaintiff had not met the burden of establishing that there was no issue of material fact. Rogers v. Swingley, 206 M 306, 670 P2d 1386, 40 St. Rep. 1676 (1983).

Sufficiency of Pleadings and Proof: The defendant sold real estate to plaintiff on a contract for deed, and the District Court reformed the contract, finding fraud by defendant in orally misrepresenting that there were three good wells on the property, that ownership of a cabin on the property would transfer with the property, and that he would survey or provide papers concerning the boundary of the property. The Supreme Court reversed, finding no basis for fraud in that: (1) the water in the wells had never been tested and proven unfit for use, and the lack of pumps on two wells was obvious from visual inspection at the time the contract was entered; (2) plaintiff had, on a verified complaint, in fact acknowledged defendant's continuing ownership of the cabin, contrary to her testimony and the District Court's finding; and (3) plaintiff never alleged that a survey was to be performed, contrary to the District Court's finding, and plaintiff could have easily ascertained the boundaries by looking at an existing survey and talking with a neighbor. Krone v. McCann, 197 M 380, 642 P2d 584, 39 St. Rep. 500 (1982). See also Fossen v. Fossen, 2013 MT 299, 372 Mont. 175, 311 P.3d 743.

Actual Fraud in Execution of Contract for Deed — Compliance With Pollution Laws — Doctrine of "Implied Findings": Where the plaintiffs sued for damages caused by the defendants' fraud in the execution of a contract for deed for the sale of a shale and concrete block plant, alleging misrepresentation by the defendant company and its agents as to the plant's status of compliance with air pollution laws, the court did not err in finding the defendants guilty of actual fraud. Actual fraud is always a question of fact, and there was ample evidence upon which the court could find that the factual requisites for actual fraud had been satisfied. Although the court did not make a specific finding that the plaintiff relied upon the false representations by the defendants, the Supreme Court will engage the doctrine of "implied findings" so long as those findings are not inconsistent with express findings and assume that the court found reliance upon the defendants' misrepresentations. Poulsen v. Treasure St. Indus., Inc., 192 M 69, 626 P2d 822, 38 St. Rep. 218 (1981), followed in H-D Irrigating, Inc. v. Kimble Properties, Inc., 2000 MT 212, 301 M 34, 8 P3d 95, 57 St. Rep. 832 (2000).

Parol Evidence to Show Fraud or Resolve Ambiguity: Parol evidence is admissible to resolve ambiguities and to determine whether the buyers were fraudulently induced into entering a written contract where seller made express warranties that application for SID had been made when he knew that an application had not been made. Dodds v. Gibson Prod. Co., 181 M 373, 593 P2d 1022 (1979).

Fraud — Summary Judgment Not Proper: Conflicting contentions regarding a brochure allegedly misrepresenting land indicate issues of fact precluding summary judgment. Bails v. Wheeler, 171 M 524, 559 P2d 1180 (1977).

Tort Liability: The making of representations to induce a contract imposes on the person making them a duty to act in good faith, and if the representations are fraudulent, the party to whom they were made has an action in tort for fraud and deceit independent of the contract, which he may choose to affirm though he need not. State ex rel. Dimler v. District Court, 170 M 77, 550 P2d 917 (1976).

Fraud as a Question of Fact: Actual fraud is always a question of fact and is never to be presumed, so that plaintiffs must prove by a preponderance of the evidence that a promise was made, that the promisor had no intention of performing it, that the plaintiff relied on the promise, and that he was proximately injured. Reilly v. Maw, 146 M 145, 405 P2d 440 (1965), distinguished in Story v. Bozeman, 259 M 207, 856 P2d 202, 50 St. Rep. 761 (1993), in which it was held that the correct standard for reformation of a contract is clear, convincing, and satisfactory proof.

Sufficiency of Pleadings and Proof: The bare statement in the complaint of landowner of fraudulent representations (which were not of existing facts but no more than promises) was insufficient to allege fraud in procuring mineral lease; failure to allege that defendants had no intention of performing their promises rendered the pleading ineffectual. Hodgkiss v. Northland Petroleum Consol., 104 M 328, 67 P2d 811 (1937).

Averments: An alleged fraudulent representation by vendor that a lot was worth in excess of and would readily sell for more than a given amount was insufficient to charge fraud in the absence of the further averments that he did not believe the statement to be true or knew it to be false or was not warranted by the information he then had and of a showing of facts that the complaining purchaser had a right to rely upon the representation, and in the absence of the further averment that the lot was not worth what the vendor said it was. Howe v. Messimer, 84 M 304, 275 P 281 (1929).

Burden of Proof: In an action for damages for fraud, brought under subsection (4) of this section, where the complaint charged that defendant induced plaintiff to buy corporate stock under the promise, made without any intention of keeping it, that if the stock was not worth a certain sum within 6 years, he would return to him the purchase price, plaintiff had the burden of proving, among other things, that defendant made the promise and that when he made it, he had no intention of performing it, under the rule that a party plaintiff must prove every material allegation of his complaint. Cuckovich v. Buckovich, 82 M 1, 264 P 930 (1928).

No Presumption of Fraud: Fraud can never be presumed but must be proved by a preponderance of the evidence. Good faith will always be presumed, and mere suspicion of fraud is not sufficient. Cuckovich v. Buckovich, 82 M 1, 264 P 930 (1928), followed in Reilly v. Maw, 146 M 145, 405 P2d 440 (1965), Cowan v. Westland Realty Co., 162 M 379, 512 P2d 714 (1973), Krone v. McCann, 197 M 380, 642 P2d 584, 39 St. Rep. 500 (1982).

Statements as Inducing Case: One who relies on fraudulent representations to defeat an action on a promissory note given for the purchase of chattels has the burden of proving that the statements were the inducing cause for signing the note; that they were material and false; that the speaker had knowledge of their falsity or was ignorant of their truth and intended that they should be accepted and acted upon; that the defendant was ignorant of their falsity and rightfully relied upon their truth, not having equal means of knowing the truth or opportunity to examine the property, and that his damage proximately resulted from the representations. Advance-Rumely Thresher Co., Inc. v. Wenholz, 80 M 82, 258 P 1085 (1927).

Proof of Value: Proof of inadequacy of value of land as security for indebtedness against it is not alone sufficient to prove fraud, either actual or constructive. Duffy v. Hastings, 78 M 22, 252 P 316 (1926).

Pleading Intent: Where defendant, in an action to recover the purchase price of personal property, in his answer pleaded that the representation of plaintiff that he had title to the property was false but did not allege that plaintiff knew it to be false, that it was made in a manner not warranted by the information possessed by the seller, that it was made with intent to deceive, that the buyer believed it to be true or relied upon it, and that he was deceived by it and misled to his prejudice, the pleading was insufficient to warrant rescission of the contract on the ground of fraud. Courtney v. Gordon, 74 M 408, 241 P 233 (1925).

Charging Fraud: Allegations in an action to rescind a contract for the sale of city lots on the ground of fraud perpetrated by the vendor in procuring the scrivener to insert in the deed numbers of inside lots instead of corner lots intended to be bought was sufficient to charge actual fraud. Campana v. Dobry, 69 M 240, 221 P 540 (1923).

Burden of Person Alleging: In an action based on fraud, the question whether actual fraud has been practiced is one of fact and the burden of proof is upon him who alleges it. Lee v. Stockmen's Nat'l Bank, 63 M 262, 207 P 623 (1922).

Fraud as an Answer: Where, in a suit to foreclose a purchase-money mortgage, the answer sets up fraud by the plaintiff in inducing the defendant to enter into the transaction and avers, in describing the fraud, particulars coming within the statutory definition of fraud, it is error for the court to strike such averments from the answer. Como Orchard Land Co. v. Markham, 54 M 438, 171 P 274 (1918).

Evidence to Support: In an action for damages for fraud charged by plaintiff to have been practiced upon him in the sale of land, the plaintiff made out his case where the evidence showed that the defendant, acting in collusion with a civil engineer who had been employed by plaintiff to survey the land, falsely represented to him that the tract contained a much larger acreage suitable for fruit growing than was actually embraced in it. Shoudy v. Reeser, 48 M 579, 142 P 205 (1914).

DEFENSES

Blank Security Agreement Signed by Borrower and Filled Out by Bank: Borrower signed a blank security agreement that bank then filled out and mailed to her. The record shows that she had the agreement in her possession in December 1985; thus, she had the means to discover the fraud that she alleged bank committed in setting the agreement's terms. Because she did not file a claim until December 1988, her claim was barred by the 2-year statute of limitations. Richland Nat'l Bank & Trust v. Swenson, 249 M 410, 816 P2d 1045, 48 St. Rep. 730 (1991).

Misrepresentation Not Relied Upon — No Fraud: A cause of action for fraud fails when the alleged misrepresentation is not relied upon. Van Hook v. Baum, 245 M 407, 800 P2d 151, 47 St. Rep. 1883 (1990).

Failure to Inspect — No Defense: When a contract is induced by false representations as to material existent facts which are made with the intent to deceive and upon which the plaintiff relied, it is no defense to the action for rescission or for damages arising out of the deceit that the party to whom the representations were made might have, with due diligence, discovered their falsity and that he made no searching inquiry into facts. Opportunity to inspect in itself is no defense to possible willful misrepresentations that because of their plausibility preclude further investigation. Wortman v. Griff, 200 M 528, 651 P2d 998, 39 St. Rep. 1916 (1982).

Waiver of Fraud: One who discovers that fraud has been practiced on him while the transaction remains wholly executory but nevertheless either executes or performs it on his part or requires performance on the part of the other party thereby waives the fraud and cannot subsequently maintain an action for damages. Van Ettinger v. Pappin, 180 M 1, 588 P2d 988 (1978).

Concealment of Physical Condition: Where the lessee of a hotel building inspected the premises and the inspection revealed or would have revealed the true physical condition of the premises, she would have no right to rely upon any concealment by the lessors with respect to the physical condition of the premises. Lowe v. Root, 166 M 150, 531 P2d 674 (1975).

Laches: Where one claiming to have been defrauded, with full knowledge of the facts relating to the transaction, waits for 5 years before making complaint and until the time when he is called upon to meet the obligation incurred, he will be held to have ratified it even though in the first instance he was induced to execute the instrument in question by his creditor's fraudulent representations. Morigeau v. Lozar, 81 M 434, 263 P 985 (1928). See also Lasby v. Burgess, 88 M 49, 289 P 1028 (1930).

Defense of Caveat Emptor (Buyer Beware): Where a party who claims to have been deceived to his prejudice by false representations had the means at hand to ascertain whether the statements made were true or not but failed to do so, his reliance upon the representations, however false, affords him no ground of complaint. Helena Adjustment Co. v. Claflin, 75 M 317, 243 P 1063 (1926), distinguished in Griffiths v. Trasher, 95 M 210, 26 P2d 995 (1933).

Laches — Evidence: One charged with fraud in causing numbers of inside city lots to be inserted in the deed, whereas the purchaser intended to buy and the vendor agreed to sell corner lots, will not be heard to defend on the ground of laches because of plaintiff's failure to consult the abstract of title for some 2 years, where the evidence showed that immediately after discovering the fraud defendant assured plaintiff that she would "fix it". Campana v. Dobry, 69 M 240, 221 P 540 (1923).

Examination of Title: Where a purchaser of land caused an examination of the title thereto to be made and could have ascertained an alleged defect in it, his reliance upon false representations made with relation thereto by the vendor's attorney was not a defense to an action to foreclose a mortgage for failure to pay balance of the purchase price. Morehouse v. N. Land Co., 68 M 96, 216 P 792 (1923).

Exercise of Care: A judgment of nonsuit was properly entered in an action against a bank for damages claimed to have been suffered by plaintiff in reliance upon alleged fraudulent representations made to him by its cashier that mortgages held by it on automobiles handled by a dealer were in full force, had not been paid, etc. In fact the bank had authorized the mortgagor to sell, and he had sold them, paying the proceeds into the bank. On the strength of the cashier's statements plaintiff had bought the mortgages. It appeared from plaintiff's evidence that he was a director of the bank and a member of its discount committee, with knowledge of the course of business pursued between the bank and the mortgagor with relation to the automobiles. He had himself endorsed the mortgagor's notes secured by mortgaged cars which were sold by the latter notwithstanding the mortgage, etc., it appearing therefrom that any damage he suffered was not traceable to the alleged false representations but to his failure to exercise the care imposed by the rule of caveat emptor. Lee v. Stockmen's Nat'l Bank, 63 M 262, 207 P 623 (1922).

Investigation Precludes Reliance: Where it appears in an action for fraud that plaintiff had investigated or had the means at hand to investigate the truth of an alleged false representation, his reliance upon it affords no ground for complaint. Lee v. Stockmen's Nat'l Bank, 63 M 262, 207 P 623 (1922).

FALSE REPRESENTATIONS

Failure to Attempt to Verify Alleged False Representation — No Right to Rely on That Representation: When the plaintiff deliberately avoided finding out whether the representations made by the defendant regarding the assumption of certain business liabilities were true, the plaintiff could not then claim she relied on those representations to her detriment. Fossen v. Fossen, 2013 MT 299, 372 Mont. 175, 311 P.3d 743.

Misrepresentation of Substituted Seed — Remand for Determination of Damages Beyond Subsequent Crop Loss and for Consideration of Actual Fraud: Plaintiff delivered a load of wheat seed to defendant's facility for cleaning and treating. Defendant inadvertently dumped the load into a waste bin, replaced the seed with a similar but different variety, and charged plaintiff for cleaning and treatment without informing plaintiff of the error. When the crop came up, plaintiff noticed that the seed was a different variety, sued defendant for negligent misrepresentation, and sought compensatory and punitive damages. The District Court held that defendant did not commit actual fraud, but misconstrued the differing definitions of actual fraud in Title 27 and this title in determining that no punitive damages were allowed. The Supreme Court remanded for reconsideration of the punitive damage claim based on actual fraud as defined in 27-1-221. Additionally, the District Court failed to address plaintiff's claim for damages beyond the actual crop loss suffered because of the substituted seed, and that issue was also remanded for further consideration. However, the District Court did not err in refusing to award damages for plaintiff's lost crop insurance payments, in its findings regarding the per acre loss and value per bushel of lost production, by qualifying plaintiff's expert witness, or by awarding prejudgment interest. Hallenberg v. Gen. Mills Operations, Inc., 2006 MT 191, 333 M 143, 141 P3d 1216 (2006).

No Actual Malice Shown in Replacement of Seed With Different Variety: Plaintiff delivered a load of wheat seed to defendant's facility for cleaning and treating. Defendant inadvertently dumped the load into a waste bin, replaced the seed with a similar but different variety, and charged plaintiff for cleaning and treatment without informing plaintiff of the error. When the crop came up, plaintiff noticed that the seed was a different variety, sued defendant for negligent misrepresentation, and sought compensatory and punitive damages. The District Court found no actual malice on defendant's part and declined to award punitive damages. On appeal, the Supreme Court affirmed. Substantial credible evidence showed that defendant's personnel assumed that plaintiff was planting a variety that was commonly used in the area and substituted that common variety, assuming that no injury would result in the misrepresentation that the seed plaintiff was going to plant was the same seed plaintiff delivered. Defendant neither had knowledge of facts nor intentionally disregarded facts that created a high probability of injury to plaintiff, so the definition of actual malice was not met and the District Court correctly declined to award punitive damages without a finding of actual malice. Hallenberg v. Gen. Mills Operations, Inc., 2006 MT 191, 333 M 143, 141 P3d 1216 (2006).

Unjustified Construction Lien Not Constituting Fraud in Sale of Real Property — Knowledge of Seller Held Determinative: Hickingbothams agreed to purchase a part of tract 1-A (1-A-1) from Duncan. Later, Hickingbothams also negotiated for and purchased an additional adjoining tract (portion A of 1-A) from Duncan. At the same time, Duncan was constructing a house on a separate part of tract 1-A. Because of a dispute with the contractor over the value of work performed by the contractor, the contractor placed a construction lien against all of parcel 1-A, including that part owned by Hickingbothams. Hickingbothams sued Duncan, alleging that Duncan committed fraud by executing the receipt and agreement to sell and purchase portion A while knowing that a construction lien had been placed against the property. The Supreme Court held that despite Duncan's knowledge of the ongoing dispute with the contractor, the construction lien had not yet been placed against the property, including portion A of 1-A. The Supreme Court held that Duncan should not be charged with knowing that an unwarranted construction lien would be placed against the property and that therefore any representations by Duncan as to marketability of the property were not false representations. Hickingbotham v. Duncan, 271 M 525, 898 P2d 1215, 52 St. Rep. 574 (1995).

Knowledge of Seller's Lack of Clear Title: The defendant had represented that the seller had good title at the time the contract was entered into, when in fact the seller had no interest in the property. The defendant argued that her actions did not constitute fraud because there was no obligation to produce title to the property until the entire contract was paid. The Supreme Court affirmed the lower court's finding that fraud existed because the statements were false at the time they were made. Lee v. Armstrong, 244 M 289, 798 P2d 84, 47 St. Rep. 1421 (1990).

Truth Regarding Representations Apparent Prior to Signing Contract — Fraud Not Proven: Ranch purchasers claimed that seller made several misrepresentations, which they relied on to their detriment regarding the property. The District Court properly found no fraud based on false representations after noting the purchasers: (1) were experienced ranchers familiar with farming procedures; (2) repeatedly inspected the property prior to signing any agreement; (3) seeded all the spring crops for the growing season prior to signing the purchase contract; (4) seeded, harvested, marketed, and appropriated for their own use two consecutive crops, making no complaints; (5) never complained of any misrepresentations until filing suit; and (6) as to each alleged misrepresentation, learned the true condition of the property before signing the purchase contract and therefore did not rely on the truth of the asserted false statements. Schweigert v. Fowler, 240 M 424, 784 P2d 405, 47 St. Rep. 1 (1990).

Summary Judgment Appropriate When Plaintiff Fails to Make Factual Showing That Any of Defendant's Representations Were False: The plaintiff bought a motorcycle distributorship from the defendant. The plaintiff changed the business's name, location, and product line and fired most of the former employees. The business ceased making a profit, and the plaintiff sued the defendant for fraud and negligent misrepresentation. The Supreme Court affirmed the lower court's dismissal of the claim, agreeing that summary judgment was proper because the plaintiff had failed to make a factual showing that any of the material representations were false. Batten v. Watts Cycle & Marine, Inc., 240 M 113, 783 P2d 378, 46 St. Rep. 1984 (1989), followed in Barrett v. Holland & Hart, 256 M 101, 845 P2d 714, 49 St. Rep. 1156 (1992), and 50 St. Rep. 63 (1993).

Fraud by Misrepresentation of Business Profits: Fraud was properly found where evidence showed that seller of a business, an experienced businessman, gave to potential buyers documents that made false and materially misleading statements of business income, upon which buyers relied in purchasing the business. Selvidge v. McBeen, 230 M 237, 750 P2d 429, 45 St. Rep. 168 (1988).

No Fraud in Representation of Debt: Debtor alleged that he signed a release in favor of the bank in total ignorance of his liabilities and defended his ignorance on the grounds that the bank misrepresented his debt to it. However, the record disclosed that the language of the release agreement, debtor's participation in a conference call in which reaffirmation of a loan was discussed, notice to debtor's attorney regarding the nature of indebtedness, and financial statements estimating debtor's liabilities all indicated debtor's knowledge of his debt load. There was no material question of fraudulent misrepresentation, and summary judgment was proper. Sprunk v. First Bank W. Mont. Missoula, 228 M 168, 741 P2d 766, 44 St. Rep. 1429 (1987), affirmed on separate grounds in Sprunk v. First Bank Sys., 252 M 463, 830 P2d 103, 49 St. Rep. 369 (1992), and followed in Stanley v. Holms, 1999 MT 41, 293 M 343, 975 P2d 1242, 56 St. Rep. 178 (1999).

False Representations — Ability to Construct Hog Barns — Findings Not Clearly Erroneous: There was testimony showing defendant knowingly made material false representations that he could construct water-flush hog barns—promises that he could not keep. Plaintiff had a right to rely on defendant and was injured because of that reliance. Although there were conflicting findings, the Supreme Court found no clear error constituting abuse of discretion. Roberts v. Mission Valley Concrete Indus., Inc., 222 M 268, 721 P2d 355, 43 St. Rep. 1254 (1986).

False Representation as Actual Fraud — No Directed Verdict: Defendants contended that plaintiffs' evidence was insufficient to establish a false representation or justifiable reliance on the representation and that therefore defendants' motions for a directed verdict were improperly denied. The Supreme Court noted that a prospectus given to plaintiff, McGregor, contained financial statements which would be misleading to someone not knowledgeable in accounting and that a jury could find that false representations were made on this evidence. The court found that McGregor adequately investigated the business and reasonably relied on defendants' representations. The Supreme Court found no error in the District Court's failure to direct a verdict for defendants on the claim of actual fraud. McGregor v. Cushman/Mommer, 220 M 98, 714 P2d 536, 43 St. Rep. 206 (1986).

Owner's Valuation of Business — Factual Representations: Statements as to value of property are generally considered declarations of opinion and are not a basis for rescission of a contract. Such statements are opinions when the parties stand on an equal footing and have equal means of knowledge, with no relation of trust or confidence existing between them. Bar owner who was a businessman and had personal knowledge of the bar's financial condition did not stand on an equal footing with baker who frequented the bar and whom bar owner persuaded to invest $25,000 in the business. There was substantial credible evidence to support trial court's finding in action for fraud that bar owner made factual representations of value to baker when bar owner stated that the business was worth $250,000 and allocated stated values to the liquor license, inventory, equipment, and good will. Spence v. Yocum, 201 M 79, 651 P2d 1022, 39 St. Rep. 1966 (1982), followed in Barrett v. Holland & Hart, 256 M 101, 845 P2d 714, 49 St. Rep. 1156 (1992), and 50 St. Rep. 63 (1993).

Fraud — Summary Judgment Not Proper: In course of inspection of hotel prior to purchasing it, buyer asked seller's agent why there was water on the floor of the boiler room. The agent allegedly replied that the cause was a minor problem with the boiler system that could be easily repaired. Shortly after the sale, the buyer paid a substantial amount of money to repair the boiler system. After buyer did not keep up with payments due on his promissory note, seller sued. The buyer defended by alleging that the seller had fraudulently misrepresented the condition of the hotel's heating system. The District Court gave summary judgment for the seller. The Supreme Court reversed, ruling that summary judgment was not proper because the question of whether or not there was fraud in the sales transaction was an issue material to the case upon which buyer should have been permitted to present evidence. Jenkins v. Hillard, 199 M 1, 647 P2d 354, 39 St. Rep. 1156 (1982).

Negligent Misrepresentation by a Stockbroker: A stockbroker testified that what he told a customer regarding the risk of a transaction he believed to be true. The customer testified that he did not believe he had been deliberately misinformed by the broker. However, one who in the course of a transaction in which he has a pecuniary interest supplies information for the guidance of others in their transactions must exercise reasonable competence in obtaining or communicating the information. Negligent as well as intentional misrepresentation can be the basis of a tort action in fraud. Brown v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 197 M 1, 640 P2d 453, 39 St. Rep. 305 (1982), followed in Wagner v. Cutler, 232 M 332, 757 P2d 779, 45 St. Rep. 1092 (1988).

False Representations — Right to Rescind: The sellers of a business falsely represented the profitability of the business and its standing with suppliers and wholesalers to prospective buyers. The buyers relied on and had a right to rely on the truth of the representations and were induced to purchase the business because of the false representations. Upon learning of the falsity of the representations that had induced them to purchase the business, the purchasers had the right to rescind the contract for deed for the purchase of the business. Lumby v. Doetch, 183 M 427, 600 P2d 200 (1979).

Reliance on Alleged Representations After Independent Investigation: When it appears that a party who claims to have been deceived to his prejudice has investigated for himself or that the means were at hand to ascertain the truth of any representations made to him, his reliance on such representations made to him, however false they may have been, affords no ground of complaint. Van Ettinger v. Pappin, 180 M 1, 588 P2d 988 (1978), cited in Aetna Life Ins. Co. v. McElvain, 221 M 138, 717 P2d 1081, 43 St. Rep. 697 (1986). See also Fossen v. Fossen, 2013 MT 299, 372 Mont. 175, 311 P.3d 743.

Material Misrepresentations: Inaccurate statement by defendant's agent in mineral deed negotiations that nearest oil fields were 20 miles away did not constitute fraud under this section in the absence of fraudulent intent and where the misstatement arose from an honest misunderstanding between defendant and agent. Clough v. Jackson, 156 M 272, 479 P2d 266 (1971).

Puffing: Broker's statement that laundromat grossed $3,000 a month, was worth $37,000, and "looks like a real good deal" did not establish material misrepresentations constituting fraud and entitling purchaser to rescind sale contract in view of evidence that, although open less than 30 days a month, business did gross $100 a day and that seller had paid $30,000 for business and added $4,000 of improvements; in the absence of corroboration, buyer's claim that broker also told him business netted $1,000 a month was not basis for rescission. Young v. Handrow, 151 M 310, 443 P2d 9 (1968).

Representations in Stock Sale: False representation that an investment company would be ready for business within 2 months, made to induce the sale of stock, was a fraud. Buhler v. Loftus, 53 M 546, 165 P 601 (1917).

Deception: An owner of land is supposed to know its boundaries, and his vendee has a right to rely upon his representations as to them; such representations are regarded as those of fact, and, if false, the effect of them is to deceive the intending purchaser. Post v. Liberty, 45 M 1, 121 P 475 (1912).

PROMISES

Inducement to Purchase Property Based on Promise of Road Improvements — Directed Verdict Improper: Plaintiffs claimed they were fraudulently induced to enter contracts to purchase land when seller orally promised to improve access roads to county grade. The District Court granted defendants a directed verdict, relying on Kelly v. Ellis, 39 M 597, 104 P 873 (1909), in holding that when there was no allegation of failure to keep all promises made in the written agreement, the statute of frauds precluded admission of evidence of an oral promise directly related to the contents of the contract. However, plaintiffs relied on a certificate of survey that showed county grade easements, a letter from defendants' attorney agreeing to hold a title insurance company harmless from any claims arising from purchasers' access problems, and the representation by a realtor that roads would be upgraded to county road standards. These representations constituted a conflict in evidence precluding directed verdict, and the District Court erred in taking from the jury the issue of whether plaintiffs were fraudulently induced to enter the contracts. Dew v. Dower, 237 M 476, 774 P2d 989, 46 St. Rep. 981 (1989), following Majers v. Shining Mtn., 230 M 373, 750 P2d 449, 45 St. Rep. 283 (1988), Majers v. Shining Mtn., 219 M 366, 711 P2d 1375, 43 St. Rep. 16 (1986), Dodds v. Gibson Prod. Co., 181 M 373, 593 P2d 1022 (1979), and Goggans v. Winkley, 154 M 451, 465 P2d 326 (1970). Following a trial subsequent to Dew, infra., the District Court determined that defendant did fraudulently induce plaintiffs to purchase property by misrepresenting the quality of the road that she intended to build as access to the property and further awarded monetary damages to each plaintiff. On appeal, defendant contended, among other things, that the trial court erred in admitting, without first requiring plaintiffs to prove intent to defraud, parol evidence that defendant orally promised to improve the road and also erred in determining that defendant intended to defraud plaintiffs by inducing them to enter into contracts for deed. However, defendant waived the right to appeal the parol evidence question by failing to object at trial, and substantial evidence that defendant had no intention to perform the promises to improve the road was sufficient to prove defendant's intent to defraud. Dew v. Dower, 258 M 114, 852 P2d 549, 50 St. Rep. 454 (1993).

Failure to Keep Promise: Allegation that executive vice-president of bank promised to find purchaser for defendant's corporation did not support claim of fraud under this section since mere making of promise which promisor fails to keep is not actionable fraud. Gallatin Trust & Sav. Bank v. Henke, 154 M 170, 461 P2d 448 (1969).

Promise Made Without the Intent to Perform: Where an oral contract was made between two real estate brokers to divide a commission, the mere fact that a promise was not carried out is not proof that such promise was made with no intention to perform; fraud in failing to perform was not proved when there was a possibility the sale would not go through. Reilly v. Maw, 146 M 145, 405 P2d 440 (1965).

Indefinite Promise: Where plaintiff invested funds in mining operations of defendant, defendant's indefinite promise that "they were going to form a corporation as soon as possible" without setting any time or date for doing so was insufficient to establish fraud where corporation was not formed 4 months later. Marlin v. Drury, 124 M 576, 228 P2d 803 (1951).

Intention — Proof Required: One charging fraud by reason of making a promise without any intention of performing it must prove that the maker of it had no such intention when he made it, the mere showing that it was not performed being insufficient to prove fraud. Howe v. Messimer, 84 M 304, 275 P 281 (1929).

Change of Mind: When a promise was made in good faith at the time when made, there is no fraud, though the promisor subsequently changes his mind and fails to perform. Cuckovich v. Buckovich, 82 M 1, 264 P 930 (1928).

Good Faith Presumed: The law presumes good faith and that at the time one charged with making a fraudulent promise made it, he intended to perform it. It never presumes fraud, but the burden of proving fraud is on the party alleging it. Cuckovich v. Buckovich, 82 M 1, 264 P 930 (1928).

Intention: The mere making of a promise which the promisor fails to keep does not constitute actionable fraud, intention not to keep it when it was made being necessary to constitute the promisor's action fraudulent under this section. Int'l Harvester Co. v. Merry, 60 M 498, 199 P 704 (1921).

Inducement by Promise: Where a married man by a promise made to his dangerously sick wife to devise both his own and her property to their daughter and son induces her to convey her property to him instead of to the daughter as she proposes, he intending at the time either to repudiate the promise afterward or to do as he pleases with the property after once getting it into his hands, there is actual fraud in his act from its inception. Huffine v. Lincoln, 52 M 585, 160 P 820 (1916).

DAMAGES

Damages — Purchase of Farmlands: The measure of damages for fraud in inducing the purchase of farmlands is the difference between their actual value at the date of sale and the contract price. Healy v. Ginoff, 69 M 116, 220 P 539 (1923).

Crop Loss: Where a purchaser of land was aware, after the first year of his occupancy, that the representations by the seller as to the amount of water available for irrigation by reason of which he lost the first year's crop were false, his recovery of damages was limited to the amount represented by the loss of that crop, and he could not claim damages based upon four successive failures thereafter, he having planted the crops with knowledge that water could not be obtained for irrigation. Healy v. Ginoff, 69 M 116, 220 P 539 (1923).

Boundaries of Land: The representations made by a landowner to an intended purchaser as to the boundaries of his property were, in effect, warranties, the owner being presumed to know its location. Where, after the consummation of a sale, the statements of the vendor in this regard proved false, the result was a fraud within the meaning of this section, whether made in good or bad faith, and the vendee had the right to rescind or sue for damages. Post v. Liberty, 45 M 1, 121 P 475 (1912).

MISCELLANEOUS

Material Misrepresentation on Application for Credit Life and Disability Insurance — Denial of Coverage Warranted: Schlemmer applied to the North Central Life Insurance Company (North Central) for credit life and disability insurance but misrepresented his health history. If he had answered correctly on the application, he would have been ineligible for the insurance. Nevertheless, he averred by his signature that he understood the form and that his application statements were true, so the policy was issued. Schlemmer later filed a claim for disability payments. North Central investigated, found that Schlemmer had been treated within the previous 2 years for hypertension, chronic obstructive lung disease, and disease or disorder of the kidneys, contrary to his statements in the application, and denied the claim and refunded Schlemmer's premiums. Schlemmer sued for damages, claiming that the application and underwriting procedures used by North Central violated 33-18-201, commonly known as the unfair claims settlement practices law, breached the covenant of good faith and fair dealing, and constituted fraud. Schlemmer also maintained that the District Court erred in failing to rule on whether North Central's agent had knowledge of Schlemmer's condition, which might have created a question of material fact. The Supreme Court affirmed the District Court's rulings that: (1) Schlemmer's claim of ignorance of the contents of the written application could not prevail because the application language was clear and unambiguous and Schlemmer did not deny signing it; (2) Schlemmer materially misrepresented his health on the application; (3) the material misrepresentation was legally sufficient to allow North Central to deny coverage under the policy; and (4) Schlemmer's argument that North Central's agent knew or should have known about Schlemmer's health was mere speculation insufficient to create an issue of fact to defeat North Central's properly supported motion for summary judgment. Further, the Supreme Court declined to consider Schlemmer's argument that the misrepresentation could not serve as a basis to rescind the policy because he did not apply for benefits until more than 2 years after applying for the insurance, pursuant to 33-22-205, because Schlemmer never raised the issue at the District Court level. Schlemmer v. N. Cent. Life Ins. Co., 2001 MT 256, 307 M 203, 37 P3d 63 (2001).

Failure of Plaintiff to Appear at Trial or Present Evidence — Judgment for Defendant Proper: Objections by the plaintiff on appeal as to whether evidence was properly admitted at trial were waived because of plaintiff's failure to appear at trial, in person or by counsel, and to make a timely objection. Similarly, plaintiff's contention that the District Court should have found evidence of fraud failed because plaintiff failed to appear or present any evidence at trial to support the claim. Gibson v. Swanson, 239 M 380, 780 P2d 1137, 46 St. Rep. 1764 (1989).

Fraudulent Concealment of Wrongful Nature of Sexual Abuse — Discovery Doctrine Not Applicable: Plaintiff who was sexually abused as a child contended the discovery doctrine applied because her abuser fraudulently concealed the wrongful nature of the relationship. Plaintiff was not incompetent, did not psychologically repress the attacks, and was aware that child molestation was a wrongful act. Reliance upon a fraudulent representation must be reasonable, and the state of facts was sufficient to cause a reasonable person to inquire. E. & D.W. v. D.C.H., 231 M 481, 754 P2d 817, 45 St. Rep. 778 (1988).

Warranty Deed — Donative Intent — No Fraud or Lack of Consideration: Plaintiff filed an action to set aside a warranty deed to defendant transferring land that plaintiff had received originally as a tenant in common with defendant's father under the condition that they deed the land to defendant "when they were done with it". The District Court found that defendant was not guilty of deceit or false representation and that there was fair and adequate consideration for the transfer and refused to void the deed. The Supreme Court affirmed, holding that there was sufficient evidence to support the District Court's findings. Although the land was valued at $300,000 to $600,000 and the consideration for the transfer was $1, plaintiff's performance of the condition requiring transfer of the land to defendant, coupled with the payment of $1, constituted fair and adequate consideration in this case. Wright v. Blevins, 217 M 439, 705 P2d 113, 42 St. Rep. 1311 (1985).

No Fraud Found in Sale of Real Property — Theory of Negligent Misrepresentation Abandoned — Findings and Conclusions Not Clearly Erroneous: Where the plaintiffs agreed to purchase a bar and restaurant from the defendant seller and later brought an action for damages against the county and the county sanitarian, claiming that the sanitarian misrepresented the capacity of the sewer system and conditions of a county license, the findings and conclusions of the District Court were supported by substantial evidence and were not clearly erroneous. The District Court found that the plaintiffs failed to prove their claim of fraud and that the theory of negligent misrepresentation had been abandoned by the plaintiffs. The record contained conflicting evidence but showed that there could have been a misunderstanding between the parties, and a misunderstanding will not support a claim for fraud in the inducement. The statements made by the defendant may have been negligent, but the District Court properly concluded that by failing to argue the theory of negligent misrepresentation, the plaintiffs evidenced an intention to abandon that theory. Lacey v. Herndon, 205 M 379, 668 P2d 251, 40 St. Rep. 1375 (1983).

Reliance on Stockbroker's Representations: A customer has the right to rely on representations made by his stockbroker as the parties are not on equal footing and do not have equal means of knowing the truth. Brown v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 197 M 1, 640 P2d 453, 39 St. Rep. 305 (1982).

Faulty Execution of Quitclaim Deed: Although attorney was not qualified to notarize execution of client's quitclaim deed to himself, no question of fraud was raised as client admitted to signing execution. Matthews v. Berryman, 196 M 49, 637 P2d 822, 38 St. Rep. 2112 (1981).

Threat to Withdraw as Legal Counsel: Fraud was not present when attorney, minutes before he was to defend client on criminal charges, threatened to withdraw as counsel unless client executed security agreement and quitclaim deed as security for attorney's fee. Attorney had given the instruments to client weeks before trial, but client had failed to execute them. Matthews v. Berryman, 196 M 49, 637 P2d 822, 38 St. Rep. 2112 (1981).

Land Sale Contract: Summary judgment for seller was reversed as against buyer alleging fraud based upon misrepresentation. Bails v. Gar, 171 M 342, 558 P2d 458 (1976).

One Party in Superior Position: Record disclosing that buyer of real estate who was real estate broker and mineral dealer, knowledgeable in legal affairs, titles, and values of property and who handled drafting of contract, was in superior position as compared to seller who was almost illiterate, weakminded, and an irresponsible drinker who took no part in drafting contract, was sufficient to raise legal question of fraud on grounds of gross inadequacy of consideration and undue influence. Rock v. Birdwell, 149 M 449, 429 P2d 634 (1967).

Bad Faith: Where seller of land made representation that he had authority to sell his brother's land, which was adjoining, whereas in fact he did not have such authority, and where other evidence indicated that the seller made no effort to carry out other provisions of his contract for sale, the District Court was correct in finding him guilty of bad faith. Hart v. Honrud, 131 M 284, 309 P2d 329 (1957).

Fraud Defined: Fraud, in its generic sense, especially as used in courts of equity, comprises all acts, omissions, and concealments involving a legal or equitable duty which result in damages to another; it is any cunning or artifice used to cheat or deceive another. Bullard v. Zimmerman, 82 M 434, 268 P 512 (1928).

Sale of Stock: Representations made to a stockholder in a company by a broker that 100 shares of its capital stock had been turned back into its treasury by a subscriber unable to pay therefor and soliciting plaintiff to buy it "to help the company out" related to a material matter within the meaning of this section. Stillwell v. Rankin, 55 M 130, 174 P 186 (1918).

Effect on Parties Defrauding: A trust cannot result in one of two persons for the benefit of the other, if they intended and agreed to obtain land from the government unlawfully and fraudulently. The court, in such a case, in a suit between themselves as to the land, will leave the parties where it finds them. Keely v. Gregg, 33 M 216, 83 P 222 (1905).

28-2-406. What constitutes constructive fraud.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Elements of Fraud 155
Pleadings and Proof 161
General 164

ELEMENTS OF FRAUD

No Factual Basis Presented Disputing Essential Elements of Constructive Fraud — Summary Judgment Granting Dismissal of Constructive Fraud Claim Upheld. Drescher v. Malee, 2022 MT 200, 410 Mont. 305, 519 P.3d 17.

Tort Claims Not Precluded by Parties Contracting on Same Matter: The parties entered into an agreement for the defendant to purchase the plaintiff's home. After the defendant reneged on the agreement, the plaintiff filed an action for fraud, deceit, and negligence. The District Court dismissed the claims based on its conclusion that the plaintiff's injuries resulted from the defendant's breach of contract and therefore she was precluded from bringing any tort claims against him. The plaintiff appealed. The Supreme Court explained that tort claims are not prohibited simply because the parties have entered into a contract on the same matter. However, given that the plaintiff had offered only speculative statements regarding the fraud and deceit claims, the Supreme Court agreed with the District Court's grant of summary judgment on behalf of the defendant on those claims, but it remanded the matter to the District Court to allow the negligence claim to proceed. Dewey v. Stringer, 2014 MT 136, 375 Mont. 176, 325 P.3d 1236.

Constructive Fraud May Rely on Duty to Disclose: In a constructive fraud action concerning a bank providing loan customers with misleading information about the repayment status of their existing loan and modification application, the Supreme Court held that constructive fraud may rely on a duty to disclose if one party has special knowledge of material facts and acts to mislead the other party. Morrow v. Bank of America, N.A., 2014 MT 117, 375 Mont. 38, 324 P.3d 1167.

Contractor Who Built Home So Defective as Not to Be Salvageable Guilty of Constructive Fraud: The Whites entered into a construction contract with Longley for the construction of their home. After failing to perform under the terms of the contract, Longley persuaded the Whites to buy him out of the contract for $30,000 and to let him continue to build the home without a contract. Subsequently, Longley failed to build a house that could be occupied or salvaged. Longley argued that he had not committed constructive fraud because the Whites had failed to disclose everything that they had assumed from their dealings with him. The Supreme Court said there is no support for the contention that a party being defrauded has an obligation to inform the defrauder that the party is being defrauded. The Supreme Court went on to say that the record showed many intentional misrepresentations on Longley's part and that the trial court had correctly found that all the elements necessary to prove constructive fraud were present. White v. Longley, 2010 MT 254, 358 Mont. 268, 244 P.3d 753.

Fraud Substantiated in Attorney's Handling of Probate Case — Violation of Attorney's Duty of Truthfulness — Public Censure Warranted: Attorney Potts represented parties in a will contest. Two of the parties knew that some joint tenancy accounts were not included in the value of the estate and, in an attempt to secure the funds in the accounts, directed Potts to remain silent as to whether the settlement agreement prepared by Potts included the accounts. Potts failed to notify the court and counsel for the estate that one of his clients intended to obtain the jointly held property regardless of the outcome of any settlement. The Supreme Court subsequently determined in In re Estate of Stukey, 2004, MT 279, 323 M 241, 100 P3d 114 (2004), that the parties intended that the total estate value, including the joint tenancy accounts, be included in the settlement. A professional misconduct complaint was later filed against Potts, alleging that Potts engaged in or assisted in client fraud by failing to disclose material information to opposing counsel and that Potts breached the duty of candor to the tribunal by failing to disclose material information to the court. The Commission on Practice found that Potts knew that his clients were using Potts' services to perpetuate fraud in violation of Rules 1.2(d) and 3.3(a)(2) of the Montana Rules of Professional Conduct (MRPC), that Potts failed to fulfill his ethical obligation to inform the clients that he would not participate in the fraudulent conduct, a violation of Rule 1.2(d), MRPC, and that Potts violated the duty of candor to the tribunal in violation of Rule 3.3(a)(2), MRPC. The Commission recommended that Potts be publicly censured and suspended from the practice of law for 30 days. Potts appealed, raising issues of client confidentiality, asserting that his clients did not engage in fraud because the accounts passed to his client as a matter of law and thus could not have been included as part of the settlement basis, contending that he had no duty to correct opposing counsel's erroneous understanding of the settlement, and arguing that the Commission's proposed sanctions were inappropriate. The Supreme Court held that, by definition, Potts' clients were engaged in fraudulent conduct, that Potts assisted in the conduct by not disclosing the conduct to the court and to opposing counsel in violation of the duty of truthfulness and by drafting a stipulation stating that all disputes had been settled when he knew that the parties relied on a misrepresentation in drafting a settlement, and that Potts could have avoided the situation by withdrawing from representation. Potts' conduct resulted in considerable injury to the parties, requiring one District Court proceeding and two appeals to determine the meaning and scope of the stipulation. The Commission's findings were affirmed. However, the court reversed the suspension of Potts' practice in light of mitigating factors of Potts' history of compliance with the rules of professional conduct and his good character and reputation to this point and held that public censure sufficed to apprise Potts of the gravity of the misconduct. In re Potts, 2007 MT 81, 336 M 517, 158 P3d 418 (2007).

False Impression Establishing Duty to Disclose Deficiencies in Irrigation System and Underlying Land — Doctrine of "Implied Findings": When Kimble sold his property and irrigation system, he represented that: (1) the irrigation equipment was in working order; (2) all pivots could be operated at the same time; (3) the system provided sufficient water for the acreage; and (4) he knew of no irrigation system deficiencies. Kimble also neglected to mention the extent and cause of the erosion on pivot three, even though it could be impliedly found that he had knowledge of that risk. Plaintiffs later claimed that Kimble, as defendant's agent, had misrepresented the efficiency and effectiveness of the irrigation system and failed to disclose relevant facts regarding the backfilled acreage at pivot three. The District Court held that Kimble's actions constituted constructive fraud. On appeal, defendants argued that they had no duty to disclose the erosion risk at pivot three because there was no evidence that Kimble created a false impression regarding that risk and that the District Court had made no such finding. Plaintiffs pointed out that the court's conclusion that Kimble failed to disclose the extent and cause of the erosion was based on the factual predicate that defendants had knowledge of the risk of erosion. The Supreme Court affirmed, applying the doctrine of implied findings as set out in Poulsen v. Treasure St. Indus., Inc., 192 M 69, 626 P2d 822 (1981). Although no fiduciary duty existed between the parties, Kimble created a false impression by exaggerating the efficiency of the irrigation system that established a duty on the part of defendants to disclose the fact that the old river channel had been filled, thereby creating an increased risk of serious impairment to pivot three and an increased risk of erosion resulting from planting a field in an old river channel with no riprap to prevent the river from reclaiming the channel. These facts were sufficient to support the legal conclusion that defendants were liable for constructive fraud. H-D Irrigating, Inc. v. Kimble Properties, Inc., 2000 MT 212, 301 M 34, 8 P3d 95, 57 St. Rep. 832 (2000).

Ignorance of Defect Precluding Rescission: Houdashelts sold Lutes a business that had a sump system that was believed by Houdashelts to be legal and properly permitted. Lutes sought to rescind the contract because of constructive fraud, based on Houdashelts's failure to disclose the fact that the sump system did not have the proper permits. Houdashelts were excused from disclosure because of their own ignorance. Therefore, no constructive fraud existed and rescission was improper. Houdashelt v. Lutes, 282 M 435, 938 P2d 665, 54 St. Rep. 420 (1997).

Six Elements Required to Prove Negligent Misrepresentation — Exercise of Due Care Question for Jury: A real estate broker appealed a verdict finding that an employee had negligently misrepresented the boundary of property purchased by the Cechovics. The Supreme Court held that a plaintiff had to prove the following six elements in order to show negligent misrepresentation: (1) the defendant made a representation as to a past or existing fact; (2) the representation was untrue; (3) the defendant made the representation without any reasonable ground for believing it to be true; (4) the representation was made with the intent to induce the plaintiff to rely on it; (5) the plaintiff was unaware of the falsity of the representation and was justified in relying on it; and (6) the plaintiff was damaged as a result of relying on the representation. The Supreme Court also held that in addition to the six elements, the plaintiff had to show that the defendant failed to exercise due care in obtaining or communicating the information and that the question of whether the defendant had exercised due care was for the jury and would not be overturned on appeal so long as there was substantial evidence to support the jury's finding. Cechovic v. Hardin & Associates, Inc., 273 M 104, 902 P2d 520, 52 St. Rep. 854 (1995), followed in Walters v. Luloff, 2008 MT 17, 341 M 158, 176 P3d 1034 (2008). However, see Morrow v. Bank of America, N.A., 2014 MT 117, 375 Mont. 38, 324 P.3d 1167.

No Duty to Warn of Unjustified Construction Lien — No Constructive Fraud Found in Sale of Real Property: Hickingbothams agreed to purchase a part of tract 1-A (1-A-1) from Duncan. Later, Hickingbothams also negotiated for and purchased an additional adjoining tract (portion A of 1-A) from Duncan. At the same time, Duncan was constructing a house on a separate part of tract 1-A. Because of a dispute with the contractor over the value of work performed by the contractor, the contractor placed a construction lien against all of parcel 1-A, including that part owned by Hickingbothams. Hickingbothams sued Duncan, alleging that Duncan committed fraud by executing the receipt and agreement to sell and purchase portion A while knowing that a construction lien had been placed against the property. The Supreme Court held that despite Duncan's knowledge of the ongoing dispute with the contractor, the construction lien had not yet been placed against the property, including portion A of 1-A. The Supreme Court held that because Duncan had no duty to warn of the impending filing of an unjustified and unwarranted construction lien against the property and because no real advantage was gained by Duncan, he did not commit constructive fraud. Hickingbotham v. Duncan, 271 M 525, 898 P2d 1215, 52 St. Rep. 574 (1995).

Failure to Keep Promise to Pay Medical Bills if Injured Person Travels to Exam — No Fraud: The District Court properly granted the church summary judgment on issues of fraud and misrepresentation in an action arising after plaintiff fell and was injured on church property. Plaintiff claimed that the church agreed in writing to pay medical bills if plaintiff would travel to Salt Lake City for a medical exam. Plaintiff did so, and the church failed to pay. The promise to pay money in the future was not a representation, the first element of a prima facie case for fraud or misrepresentation. Davis v. Church of Jesus Christ of Latter Day Saints, 258 M 286, 852 P2d 640, 50 St. Rep. 535 (1993).

Alleged Representations Regarding Conditions of Loan Agreement — Failure of Fraud Claim Due to Admissions of Party: Debtor claimed actual or constructive fraud based on bank president's alleged representations that the due date on a note would not be enforced and that the note would only become due if the bank deemed itself insecure or if the debtor violated the agreement. However, debtor's statements and admissions directly conflicted with the claimed representations, and in light of debtor's subsequent violation of the agreement, the claim of fraud failed. Citizens First Nat'l Bank of Wolf Point v. Moe Motor Co., 248 M 495, 813 P2d 400, 48 St. Rep. 528 (1991).

Attempt by Corporate Director to Gain Negotiation Advantage Not Constructive Fraud: The District Court found that a corporate director's attempt to gain an unfair advantage over a stockholder through negotiation tactics constituted constructive fraud. The director's offer, however, was never accepted. Reversing, the Supreme Court found that the director's actions were more consistent with negotiation tactics than oppressive actions. There was no breach of fiduciary duty, and the director did not mislead the stockholder to his prejudice. Rejecting all the director's offers, the stockholder then failed to prove prejudice that would constitute constructive fraud. Daniels v. Thomas, Dean & Hoskins, Inc., 246 M 125, 804 P2d 359, 47 St. Rep. 2293 (1990).

Failure to Inform Claimant of Right to Attorney Not Constructive Fraud: The claimant argued that at the time he settled his claim, he was not informed that he could retain an attorney to handle his claim and that this failure constituted constructive fraud. The Supreme Court held that the lower court had not abused its discretion in finding that no constructive fraud existed because the claimant was articulate, had negotiated an earlier settlement with the State Fund, and was well aware of the significance of a sound economic future for himself and his family. Hartfield v. St. Comp. Ins. Fund, 246 M 259, 805 P2d 1293, 47 St. Rep. 2001 (1990).

Denying Opportunity to Discover Defects: The defendant argued that no constructive fraud existed on her part because the plaintiffs had ample time and the duty to discover all pertinent facts. The Supreme Court held that the defendant prevented the plaintiffs from examining the underlying contract despite their requests and that such an action by the defendant constituted constructive fraud. Lee v. Armstrong, 244 M 289, 798 P2d 84, 47 St. Rep. 1421 (1990).

No Evidence Alleged Fraud Benefit to Defendant: The plaintiff argued that the defendant bank's failure to disclose that certain escrow payments had not been applied by the bank as the plaintiff had been led to believe they would be applied constituted constructive fraud. The Supreme Court ruled that the evidence did not support the claim because the bank did not gain any advantage by the nondisclosure. Kitchen Krafters, Inc. v. Eastside Bank of Mont., 242 M 155, 789 P2d 567, 47 St. Rep. 602 (1990).

Fiduciary Relationship Between Insurer and Insured — Breach Constituting Constructive Fraud: Fiduciary duties are simply a statement of the kind of good faith duty owed by an insurer to an insured. An insurance company has to consider the interests of both itself and the insured, but failure to act in the highest good faith toward the insured may constitute constructive fraud. Tynes v. Bankers Life Co., 224 M 350, 730 P2d 1115, 43 St. Rep. 2243 (1986).

No Material Fact to Support Fraud Claims: Plaintiff brought action for fraud, both actual and constructive, as well as undue influence, arising out of a promise by his mother to compensate plaintiff, upon sale of the family corporation's assets, for a portion of value attributable to plaintiff's stock and partnership interest conveyed to corporation for cancellation of promissory note executed by plaintiff for a loan from the corporation. The respondent mother was granted summary judgment. The Supreme Court held that plaintiff failed to establish a fraud claim because of admissions that his mother did not intend to deceive him and that he never relied on his mother's promise to compensate. His claims were also barred by the Statute of Limitations. Fleming v. Fleming Farms, Inc., 221 M 237, 717 P2d 1103, 43 St. Rep. 776 (1986).

False Impression and Failure to Disclose Impairments — Constructive Fraud: The defendants made misleading general statements about the profitability of the business in addition to giving inaccurate figures in a prospectus and in financial statements. Plaintiffs claimed other facts were misrepresented as well. The Supreme Court, relying on Moschelle v. Hulse, 190 M 532, 622 P2d 155, 37 St. Rep. 1506 (1980), found that these facts created a "pattern of concealment" which contributed to the plaintiffs' inability to discover the true condition and profitability of the business, constituting constructive fraud. McGregor v. Cushman/Mommer, 220 M 98, 714 P2d 536, 43 St. Rep. 206 (1986). See also Drilcon, Inc. v. Roil Energy Corp., Inc., 230 M 166, 749 P2d 1058, 45 St. Rep. 114 (1988), Hobbs v. Pac. Hide & Fur Depot, 236 M 503, 771 P2d 125, 46 St. Rep. 544 (1989), and Mattingly v. First Bank of Lincoln, 285 M 209, 947 P2d 66, 54 St. Rep. 1116 (1997).

Sale of Ranch by Joint Venturer — No Conversion or Fraud as Against Other Joint Venturers: Respondent and appellants attempted to start a dairy operation on respondent's ranch. Respondent sold the ranch after concluding that the operation would not work because adequate financing could not be obtained. There was conflicting evidence concerning respondent's intentions and whether appellants knew the ranch was for sale. Respondent made his agreed contribution to the operation, paid other expenses in an effort to find financing, and used his best efforts to make the operation a success. Appellants used some of the ranch's equipment as collateral for a loan. There was substantial credible evidence for the lower court's finding that respondent was not liable for constructive fraud for failure to inform appellants that he was going to sell the ranch. Furthermore, since appellants knew respondent did not intend to transfer ownership of the equipment to any of the appellants, their claim for conversion of the equipment must also fail. Farmers St. Bank of Victor v. Imperial Cattle Co., 218 M 89, 708 P2d 223, 42 St. Rep. 1419 (1985).

Parol Evidence Rule — Constructive Fraud as Within the Exception: Defendant represented plaintiff in a civil action in federal court. The parties agreed that the case was originally handled on a 50% contingency fee basis. The case lasted almost 10 years. Plaintiff signed a formal authorization for defendant to settle. At the time of settlement, plaintiff contended the parties agreed to replace their 50% of net fee agreement with a percentage distribution of the gross settlement amount. At some point in time, the parties signed an agreement in defendant's handwriting providing for a 75%-25% split of the settlement. The agreement contained a clause stating the agreed sums had been paid in full. Plaintiff contended defendant had retained half the settlement. Defendant contended that the trial court erred in permitting plaintiff to testify concerning the agreement. On appeal, the Supreme Court held that the fraud exception to the parol evidence rule addresses both actual and constructive fraud. The court stated that constructive fraud often exists where the parties to a transaction have a special confidential or fiduciary relation which affords the power and means to one to take undue advantage of or exercise undue influence over the other. The attorney-client relationship is a fiduciary one. Evidence presented along with plaintiff's testimony established constructive fraud on defendant's part. The court held that plaintiff's claim of conduct against defendant, which constituted at least constructive fraud, fell within the ambit of the fraud exception of the parol evidence rule. Eaton v. Morse, 212 M 233, 687 P2d 1004, 41 St. Rep. 1708 (1984).

Bank's Fiduciary Duty to Customers It Gives Financial Advice — Real Estate Sales: Wife, whose husband had recently died, signed a contract for a deed to her ranch with Dittman, who signed as "trustee". There were two other purchasers, who did not sign: a person to whom, according to the evidence, wife would not have knowingly sold and the marketing officer of the bank used by the wife and husband for some 24 years. Wife was unfamiliar with real estate and financial affairs and relied upon the advice of various bank officers with regard to the sale of the ranch. This put the bank in a prima facie fiduciary relationship as to the wife. The relationship and its attendant duties extended to the advising officers in their dealings with the wife in regard to sale of the ranch. The marketing officer thus had a duty to fully inform the wife and protect her interests. This duty he breached, and the breach amounted to constructive fraud, where evidence showed that: (1) the contract price and terms were disadvantageous to the wife; (2) the true purchasers were not disclosed to her either by the contract or the marketing officer; (3) the purchasers intended to and began to subdivide and sell the ranch, though the marketing officer knew wife apparently did not wish this, having refused an earlier offer to purchase with right to subdivide; (4) the marketing officer had extensive financial interests involving loans to him from his bank, and an audit of the bank recommended that in view of this his lending authority should be eliminated or curtailed; and (5) the lower court was unimpressed with the way in which wife's attorney in the negotiations represented her interests. The lower court properly ordered the contract for deed rescinded. Deist v. Wachholz, 208 M 207, 678 P2d 188, 41 St. Rep. 286 (1984).

Negligent Misrepresentation by a Stockbroker: A stockbroker testified that what he told a customer regarding the risk of a transaction he believed to be true. The customer testified that he did not believe he had been deliberately misinformed by the broker. However, one who in the course of a transaction in which he has a pecuniary interest supplies information for the guidance of others in their transactions must exercise reasonable competence in obtaining or communicating the information. Negligent as well as intentional misrepresentation can be the basis of a tort action in fraud. Brown v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 197 M 1, 640 P2d 453, 39 St. Rep. 305 (1982), followed in Wagner v. Cutler, 232 M 332, 757 P2d 779, 45 St. Rep. 1092 (1988).

Reliance on Stockbroker's Representations: A customer has the right to rely on representations made by his stockbroker since the parties are not on equal footing and do not have equal means of knowing the truth. Brown v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 197 M 1, 640 P2d 453, 39 St. Rep. 305 (1982).

Constructive Fraud — Requirement of Breach of Duty: Plaintiffs and defendant entered an agreement whereby defendant would lease condominiums from the plaintiffs and would sell plaintiffs her home. The lease of one of the condominiums contained an option for defendant to purchase the unit by forgiving plaintiffs their obligation under the promissory note on the home. Plaintiffs discovered that the floors in the home slope north at a rate of 5½ inches over 30 feet. Plaintiffs sought to rescind the contract, and defendant sought specific performance. Plaintiffs contended that their consent to the contract was obtained through constructive fraud. Constructive fraud requires the breach of a duty. Defendant and several contractors who performed work on the house testified that they were unaware of the condition of the floors. Plaintiffs inspected the house twice, and their professional appraiser was unaware of the condition during his appraisal. Since defendant was unaware of the defect, she was under no duty to disclose. Because defendant had no duty that she could breach, there was no constructive fraud. Woodahl v. Matthews, 196 M 445, 639 P2d 1165, 39 St. Rep. 238 (1982), followed in Van Hook v. Baum, 245 M 407, 800 P2d 151, 47 St. Rep. 1883 (1990). See also Harris v. St. Vincent Healthcare, 2013 MT 207, 371 Mont. 133, 305 P.3d 852, holding that, pursuant to a contract, health care providers had no duty to charge automobile insurance companies at the reduced reimbursement rate of the victims' private health care insurance.

Threat to Withdraw as Legal Counsel: Constructive fraud was not present when attorney, minutes before he was to defend client on criminal charges, threatened to withdraw as counsel unless client executed quitclaim deed as security for attorney's fee. Demand for security for fees was not a breach of duty by the attorney; the attorney did not mislead his client, as he had every intention of withdrawing; and the client was not prejudiced by having to provide security for a debt for which he was legally responsible. Matthews v. Berryman, 196 M 49, 637 P2d 822, 38 St. Rep. 2112 (1981).

Breach of Duty to Disclose: Breach of duty to disclose material facts is an indispensable element of constructive fraud. Mends v. Dykstra, 195 M 440, 637 P2d 502, 38 St. Rep. 2010 (1981).

Affirmative Misrepresentation — Failure to Advise in Good Faith: Plaintiffs entered an agreement to purchase the Texaco distributorship in Bozeman. At the time of entering the agreement, plaintiffs contacted Texaco's agents in Billings to check rumors that Texaco was planning to withdraw from the Montana market. Plaintiffs followed up on this rumor several times prior to purchasing the distributorship. The agents checked with the New York and Los Angeles offices and received assurances that Texaco was not planning to withdraw from Montana. Shortly after plaintiffs purchased the distributorship, Texaco withdrew from Montana. The Supreme Court found that Texaco's actions in failing to advise plaintiffs of its plans or intentions and in making affirmative misrepresentations concerning its marketing plans or intentions to plaintiffs were in bad faith and done for Texaco's gain without consideration of the risk or harm to the plaintiffs. Texaco was found to have committed a constructive fraud, and since its actions were deliberate and in reckless disregard of the consequences, punitive damages were awarded. Alexander v. Texaco, Inc., 530 F. Supp. 864, 38 St. Rep. 724 (D.C. Mont. 1981).

Fraudulent Intent: Dishonesty of purpose or intent to deceive is not a requirement of this section. Moschelle v. Hulse, 190 M 532, 622 P2d 155, 37 St. Rep. 1506 (1980).

Rescission of Contract — Fraudulent Misrepresentation — Failure to Disclose: During the course of the sale of their bar, defendants were under a duty to make such disclosures as would erase the false impressions created in the minds of plaintiffs that repairs to the premises were not needed and that winter earnings were sufficient to the plaintiffs' needs. Since defendants failed to meet this duty, plaintiffs are entitled to rescission of the contract of sale. Moschelle v. Hulse, 190 M 532, 622 P2d 155, 37 St. Rep. 1506 (1980).

Concealment of Facts: Restaurant owner's withholding from potential buyers of information that she had received warning from State Board of Health concerning unsatisfactory condition of water supply and sewage disposal systems and that correction of difficulty was necessary to meet Board's standards was fraudulent, the concealment being in the nature of a constructive fraud. Russell v. Russell, 152 M 461, 452 P2d 77 (1969).

Deficiency in Amount of Land Sold: Sale of land later shown to consist of fewer acres than represented constituted constructive fraud, entitling buyer to rescission or damages under statute even though buyer, experienced in real estate transactions, failed to ascertain the true number of acres and even though the seller's representations were honest mistake, not intended to deceive anyone. Hardin v. Hill, 149 M 68, 423 P2d 309 (1967). However, see Turner v. Ferrin, 232 M 146, 757 P2d 335, 45 St. Rep. 946 (1988), in which a 6% acreage variation in a bulk real estate sale was held to be immaterial, and Cedar Lane Ranch, Inc. v. Lundberg, 1999 MT 299, 297 M 145, 991 P2d 440, 56 St. Rep. 1207 (1999), in which words of acreage estimation in a deed, combined with a negotiated lump-sum sale price and an absence of any reference to a price an acre, were determined to constitute a sale in gross.

PLEADINGS AND PROOF

Security Brokerage Contracts — Contract of Adhesion Rendering Arbitration Clause Unenforceable: Kloss opened a full-service brokerage account with defendant, which permitted Kloss to purchase securities and maintain a money market account and which included a living trust account. The account did well, and Kloss decided to set up a charitable trust with the bond proceeds. The initial account and the living trust agreement contained a mandatory arbitration clause, and the charitable trust incorporated the arbitration clause by reference. Kloss then had second thoughts about the charitable trust and petitioned to revoke it. Defendant moved to compel arbitration, and the District Court granted the motion, citing Chor v. Piper, Jaffray & Hopwood, 261 M 143, 862 P2d 26 (1993), and Iwen v. U.S. W. Direct, 1999 MT 63, 293 M 512, 977 P2d 989 (1999), for the holding that defendant had no obligation to explain the terms of the contract because it was within Kloss's reasonable expectations and that even if the contract was considered a contract of adhesion, it was not unenforceable because it was not unconscionable. Kloss appealed, arguing that the arbitration clause was part of a contract of adhesion and that waiver of the constitutional right to jury trial should not be presumed from the signing of a contract of adhesion. Defendant maintained that form contracts prepared by securities brokers are not contracts of adhesion dictated by one party to another who has no voice in its formulation, and that arbitration clauses contained in the contracts are not unconscionable. The Supreme Court examined Passage v. Prudential-Bache Sec., Inc., 223 M 60, 727 P2d 1298 (1986), for an explanation of contracts of adhesion in the securities context and the circumstances under which they are unenforceable. The court distinguished both Chor and Passage, finding that the contracts in this case were clearly contracts of adhesion because they were standardized forms containing terms that Kloss had no opportunity to negotiate if wishing to invest with defendant. Further, the arbitration clause by which Kloss waived the right to access to state courts, the right to jury trial, the right to reasonable discovery, the right to findings of fact based on the evidence, and the right to enforce the law by way of appeal was clearly not within Kloss's reasonable expectations. The arbitration clause was never explained by defendant, and Kloss was not aware of the arbitration provision in the contract. Thus, the District Court committed reversible error when it concluded that the arbitration clause was enforceable. Kloss v. Edward D. Jones & Co., 2002 MT 129, 310 M 123, 54 P3d 1 (2002), followed in Larsen v. W. St. Ins. Agency, Inc., 2007 MT 270, 339 M 407, 170 P3d 956 (2007), with regard to factors to be applied in determining a contract of adhesion.

District Court Jurisdiction to Decide Constructive Fraud Based on Pleadings and Final Pretrial Order: Plaintiffs filed a claim for misrepresentation and failure to disclose concerning the sale of an irrigation system. Defendants contended that plaintiffs did not notify them by pleadings or evidence at trial that plaintiffs were claiming that a false impression was created regarding the condition of the field at pivot three, arguing that the complaint concerned defects and misrepresentations related to the irrigation system, not to the land, and that the District Court thus lacked jurisdiction to enter judgment on the issue of the land rather than the irrigation system. A District Court does not have jurisdiction to grant relief outside of the issues presented by the pleadings unless the parties stipulate that other questions be considered or the pleadings are amended to conform to the proof. However, in this case, the pleadings and the final pretrial order, which cited misrepresentation of or failure to disclose problems with both the deficient irrigation system and the erosion of the river bank near pivot three, gave defendants sufficient notice of the disputed issues to vest the District Court with issue jurisdiction. H-D Irrigating, Inc. v. Kimble Properties, Inc., 2000 MT 212, 301 M 34, 8 P3d 95, 57 St. Rep. 832 (2000).

Alleged Failure to Disclose Easement in Real Estate Purchase — No Constructive Fraud Found: Garrison expressed an interest to Averill, a real estate broker, in purchasing real estate on Flathead Lake from Gainey. After Garrison made an offer on the property, Averill received a counteroffer from Gainey, who, at that time, told Averill about an easement on the property. Averill told Garrison of the easement, explaining that Garrison could back out of the deal because of it and that if Garrison chose to go ahead with the purchase, he would have an opportunity to review the language of the easement when title insurance was purchased. Later, Averill read the easement language to Garrison over the telephone, and when the two walked over the property, Averill had a copy of the easement language with him and told Garrison that, to his knowledge, the easement was not being used. After the closing, people who benefited from the easement informed Garrison of their intent to make use of the easement and Garrison sued Averill and

Gainey, alleging constructive fraud. The Supreme Court noted that even if there had been a plan by some persons holding the easement to make future use of the easement, that testimony was fully consistent with the testimony presented at trial concerning nonuse of the easement by present lot owners. The Supreme Court held that there was substantial credible evidence from which the District Court could find that the existence and scope of the easement and the fact of nonuse of the easement were fully disclosed to Garrison. Garrison v. Averill, 282 M 508, 938 P2d 702, 54 St. Rep. 454 (1997).

Constructive Fraud Pleading — "Inartful" Pleading Held Sufficient — Relationship Between Former Rules 8(a) and 9(b): Berg was sued by the State Fund in a complaint that pleaded constructive fraud in three paragraphs that incorporated previous counts of the complaint by reference. Berg alleged that the constructive fraud count did not comply with the requirements of former Rule 9(b), M.R.Civ.P. (now superseded), that all of the elements of the constructive fraud claim be pleaded with "particularity" because all of the elements of constructive fraud were not pleaded. The Supreme Court held that the "particularity" requirements of former Rule 9(b) do not negate, and must be read in conjunction with, the provisions of former Rule 8(a), M.R.Civ.P. (now superseded), requiring a short and plain statement. The Supreme Court noted that Berg was able to sufficiently understand the state's pleading, that he made a responsive pleading denying the allegation of constructive fraud, that the State Fund pleading must be understood in its context of the facts of the case, and that there were no contradictory statements or statements made "on information and belief" in any of the State Fund's statements in its complaint. State ex rel. St. Comp. Mut. Ins. Fund v. Berg, 279 M 161, 927 P2d 975, 53 St. Rep. 1098 (1996).

Sale of Home by Realtors — Negligent Misrepresentation, Actual and Constructive Fraud, and Real Estate Licensing and Consumer Protection Laws — Expert Witnesses Unnecessary to Prove Standard of Care: Durbins purchased a home through the seller's realtors. Contrary to the representations of the realtors, Durbins discovered that the property had no legal septic system, that the household water was unsafe to use for any purpose, and that the access road was located on the neighbor's property. Durbins brought an action against the realtors, alleging negligent misrepresentation, actual and constructive fraud, and statutory violations involving the Montana real estate licensing laws and the Montana Unfair Trade Practices and Consumer Protection Act of 1973. The defendants sought and achieved dismissal of the case on the grounds that Durbins failed to prove through expert testimony the applicable standard of care of the realtors. The Supreme Court held that because Durbins did not allege professional misrepresentation, the issues of whether the realtors negligently misrepresented the facts, were guilty of actual or constructive fraud, or were guilty of the statutory violations alleged by Durbins, were questions resolvable by common knowledge. The questions did not turn on a standard peculiarly within the knowledge of an expert witness, and scientific, technical, or other specialized knowledge was not necessary to assist the jury. The Supreme Court therefore held that Durbins were not required to provide expert standard of care testimony to establish any of the violations. Durbin v. Ross, 276 M 463, 916 P2d 758, 53 St. Rep. 471 (1996).

Allegation of Constructive Fraud Based on Concealment or Misleading Conduct — Failure of Proof: Bengala asserted constructive fraud based on a bank's failure to notify him on the progress of premises repairs for which the bank was obligated by lease agreement. Evidence showed that the bank attempted to resolve the repair problems, even though Bengala was not made aware of those efforts until he withheld his rent in protest. Despite the lack of notification, the trial court properly found a failure of proof of constructive fraud. Bengala v. Conservative Sav. Bank, 250 M 101, 818 P2d 371, 48 St. Rep. 880 (1991).

Allegations of Constructive Fraud and Visitation Interference Unsubstantiated by Fact — Summary Judgment Proper: Appellant alleged that a counselor's testimony at a dissolution hearing was a misrepresentation constituting constructive fraud and that her observations and professional opinions affected the outcome of the visitation order to the point of visitation interference. However, the allegations were based on appellant's own speculation and opinion rather than substantial objective evidence contained in the record. Absent any genuine issue of material fact, summary judgment on both questions was proper. Thomas v. Hale, 246 M 64, 802 P2d 1255, 47 St. Rep. 2261 (1990).

No Pattern of Repeated Concealment to Support Finding of Constructive Fraud: The parties entered into a contract for the sale of a marketing by mail business. The plaintiff argued that the defendant had concealed the true financial status of the business from him and that the customer list supplied to him was in reality only a mailing list. The Supreme Court affirmed the lower court's ruling that there had been no constructive fraud. The Supreme Court stated that although there was conflicting testimony, there was sufficient evidence to support the trial court's findings. Amundson v. Wortman, 238 M 207, 777 P2d 315, 46 St. Rep. 1207 (1989).

Bank's Fiduciary Duty in Arm's-Length Debtor/Creditor Relationship: Evidence indicated a longstanding relationship between First Bank and customer but did not show that First Bank had ever acted as financial adviser to customer. Without a showing that parties had other than an arm's-length relationship, it was error to submit a fiduciary duty instruction to the jury. First Bank-Billings v. Clark, 236 M 195, 771 P2d 84, 46 St. Rep. 291 (1989).

Corporate Fraud Not Shown With Particularity: Claim of plaintiff who asserted fraud in sale of his interest in a corporation was summarily dismissed upon his failure to produce documentation showing any misrepresentation or to allege fraud with particularity. Pipinich v. Battershell, 232 M 507, 759 P2d 148, 45 St. Rep. 1237 (1988).

Dual Prongs for Piercing Corporate Veil — Evidence of Fraud Sufficient: There are two prongs to piercing the corporate veil. First, the person purporting to represent the corporation must be found to be the corporate "alter ego". Second, there must be a showing that the corporate entity was used as a subterfuge to defeat public convenience, justify wrong, or perpetrate either actual or constructive fraud. Drilcon, Inc. v. Roil Energy Corp., Inc., 230 M 166, 749 P2d 1058, 45 St. Rep. 114 (1988), followed in Berlin v. Boedecker, 268 M 444, 887 P2d 1180, 51 St. Rep. 569 (1994).

Duty, Not Fiduciary Relationship, Required: This section does not require that plaintiff demonstrate a fiduciary relationship for a constructive fraud claim to lie; it merely requires the establishment of a duty. A sufficient duty arose in a commercial transaction where defendants had a duty to refrain from intentionally or negligently creating a false impression by words or conduct. McJunkin v. Kaufman, 229 M 432, 748 P2d 910, 44 St. Rep. 2111 (1987), citing Moschelle v. Hulse, 190 M 532, 622 P2d 155, 37 St. Rep. 1506 (1980), and distinguished in Chor v. Piper, Jaffray & Hopwood, 261 M 143, 862 P2d 26, 50 St. Rep. 1234 (1993). See also Cohen v. Wedbush, Noble, Cooke, Inc., 841 F2d 282 (9th Cir. 1988), Eissinger v. Mullin Trucking, Inc., 263 M 38, 865 P2d 300, 50 St. Rep. 1695 (1993), and Mattingly v. First Bank of Lincoln, 285 M 209, 947 P2d 66, 54 St. Rep. 1116 (1997).

Instruction Given on Constructive Fraud — Instruction on Bad Faith Superfluous: The District Court instructed the jury on constructive fraud but not on breach of the implied covenant of good faith and fair dealing, which plaintiff contended was error. The Supreme Court noted that the jury found no breach of duty under the instruction on constructive fraud, which does not require a showing of fraudulent intent. An instruction on bad faith would require plaintiff to prove intentional concealment. The court held that if plaintiff could not meet the burden of proof on constructive fraud, she could not meet the higher burden of proof on bad faith; thus, the instruction would have been superfluous. Bushnell v. Cook, 221 M 296, 718 P2d 665, 43 St. Rep. 825 (1986), partially overruled in Cechovic v. Hardin & Associates, Inc., 273 M 104, 902 P2d 520, 52 St. Rep. 854 (1995).

Instruction on Negligent Misrepresentation Not Given — Action for Fraud: There was no error when District Court instructed the jury on constructive fraud but not on negligent misrepresentation. In Montana, an action for negligent misrepresentation is an action for fraud, so the jury was adequately instructed. Bushnell v. Cook, 221 M 296, 718 P2d 665, 43 St. Rep. 825 (1986), partially overruled in Cechovic v. Hardin & Associates, Inc., 273 M 104, 902 P2d 520, 52 St. Rep. 854 (1995).

No Fraud When Implications Based on Opinion: A plaintiff's opinions alone do not provide a sufficient basis in fact to prove constructive fraud when there is no evidence of any breach of duty or of a fraudulent act or omission. Westlake v. Osborne, 220 M 91, 713 P2d 548, 43 St. Rep. 200 (1986).

Confidential Relationship Not Found as Basis for Constructive Fraud: The plaintiff, son of a deceased rancher, received 24½% of the surface rights to his father's ranch in accordance with the terms of an estate plan established for the benefit of the plaintiff and his brothers, the defendants. Upon leaving the ranch, plaintiff executed one quitclaim deed to his mineral interest in 1977 and one quitclaim deed to his surface interest in 1968 in exchange for a promise that the defendants would hold him harmless on a promissory note. The District Court did not err (in a subsequent challenge by the plaintiff to the validity of the quitclaim deeds) in declaring both deeds to be valid and denying the plaintiff any interest in the ranch. The plaintiff's argument that because of the confidential, familial relationship which existed between himself and the other family members he failed to obtain independent advice as to the signing of the quitclaim deeds was not supported by the findings of the District Court. The type of "confidential relationship" that will support a presumption of fraud must include an abuse of confidence. Here there was no evidence of abuse and no evidence that the plaintiff was in any way misled. Moreover, independent advice is not a prerequisite to the validity of a deed. Turley v. Turley, 199 M 265, 649 P2d 434, 39 St. Rep. 1336 (1982).

No Fraud When No Advantage Gained by Breach of Duty: A real estate broker discussed the listing agreement with seller, and seller testified that he was familiar with standard real estate listing agreements. Even if there were a breach of a fiduciary relationship, there was no evidence that the broker gained an advantage that could result in constructive fraud. Nardi v. Smalley, 197 M 321, 643 P2d 228, 39 St. Rep. 606 (1982).

Constructive Fraud in Execution of Contract for Deed — Failure to Disclose Violation of Law: Where the plaintiffs sued for damages caused by the defendants' fraud in the execution of a contract for deed for the sale of a shale and concrete block plant, alleging misrepresentations by the defendant company and its agents as to the plant's status of compliance with air and water pollution laws, the court did not err in finding the defendants guilty of constructive fraud. The record shows that the defendants were put on notice of the pollution problems by both the notice of violation of county and state regulations and by complaints and threat of a lawsuit from a neighboring landowner. Because the record is void of any evidence that these impairments of the plaintiffs' property were ever disclosed to the plaintiffs, there is substantial evidence to support the finding of constructive fraud. Poulsen v. Treasure St. Indus., Inc., 192 M 69, 626 P2d 822, 38 St. Rep. 218 (1981).

Valuation of Land: Proof of inadequacy of value of land as security for indebtedness against it is not alone sufficient to prove fraud, either actual or constructive. Duffy v. Hastings, 78 M 22, 252 P 316 (1926).

GENERAL

Sufficient Indica of Mutual Assent to Find Written Contract — Compensatory Damages — Constructive Fraud — Statute of Frauds — Statute of Limitations: The defendants sold a tract of land from their parents' estate despite the fact that the plaintiffs had an oral agreement with the parents for the purchase of a portion of the property. The District Court properly determined that the plaintiffs had an enforceable contract to buy the property under 70-20-102 and 30-11-111 based on (1) an unsigned land purchase agreement, (2) a land survey, (3) a check issued by one of the plaintiffs that was endorsed and deposited, and (4) a letter to a tax preparer referencing the check received as partial payment for the property at issue. Because the plaintiffs had an enforceable contract, the District Court properly determined that the plaintiffs suffered compensatory damages and that the personal representative's statements showed constructive fraud. The Supreme Court held that the District Court did not err in its conclusion that the limitations provided under 72-3-803 did not bar the plaintiffs' claim. Wood v. Anderson, 2017 MT 180, 388 Mont. 166, 399 P.3d 304.

Arbitration Provision in Adhesive Contract Enforceable — Noncompetition Clause Within Weaker Party's Reasonable Expectation: Larsen asserted that an employment contract containing a noncompetition clause was a contract of adhesion and that the arbitration clause in the contract was unenforceable. The Supreme Court applied the factors in Kloss v. Edward D. Jones & Co., 2002 MT 129, 310 M 123, 54 P3d 1 (2002), and determined that the contract was indeed adhesive. However, simply being adhesive does not render a contract invalid and unenforceable under Kloss. The contract must also either fall outside the weaker party's reasonable expectation or be unconscionable. In this case, Larsen had 20 years' experience in the insurance industry and had entered various similar employment agreements that contained arbitration clauses during those years, and the arbitration provision was stated in bold letters on the first page of the agreement. These facts constituted sufficient grounds to support the conclusion that the arbitration clause fell within Larsen's reasonable expectations and was therefore enforceable. However, once the District Court determined the validity of the arbitration clause, the court exceeded its authority in deciding additional substantive issues under the agreement that should have been decided by an arbitrator, so the case was remanded for arbitration. Larsen v. W. St. Ins. Agency, Inc., 2007 MT 270, 339 M 407, 170 P3d 956 (2007), following Martz v. Beneficial Mont., Inc., 2006 MT 94, 332 M 93, 135 P3d 790 (2006).

Validity of Voluntary Easement Affirmed: The Permanns requested that Urick grant an easement across Urick's property for the Permanns to go camping and move cattle, and Urick agreed. When Urick's sons discovered that the voluntary easement had been granted, they persuaded Urick to rescind the easement. Urick requested that the Permanns convey the easement back to her. They refused. Urick filed suit and then subsequently died. Urick's son Gliko, as trustee of Urick's estate, brought an action against the Permanns seeking to have the easement rescinded, citing mutual mistake, constructive fraud, undue influence, and lack of consideration. The District Court held that the easement was valid, and Gliko appealed. The Supreme Court considered each of Gliko's rescission arguments in turn. The language of the easement was simple and unambiguous, so there was no mutual mistake. Urick had testified by deposition that no misleading statements were made relating to the easement, so there was no constructive fraud. There was no confidential relationship between Urick and the Permanns, Urick was not possessed of weakness of mind, and no advantage was taken of Urick's necessities or distress, so there was no undue influence. Last, there was no evidence that consideration was meant to be given, so lack of consideration was not a valid ground for rescission. The District Court was affirmed. Gliko v. Permann, 2006 MT 30, 331 M 112, 130 P3d 155 (2006).

Constructive Fraud for Failure to Disclose Risk of Erosion to Field Planted in Old River Channel: The sellers of farm land and an irrigation system failed to disclose to the buyers that the field at pivot three was an old river bed that had been filled but not riprapped and that the field was subject to increased risk of erosion. The buyers spent $99,575 to fix the impairment and sued for damages. The District Court found that the sellers were liable for constructive fraud for failure to disclose, and the sellers contested the District Court findings. The Supreme Court affirmed. The District Court was capable of finding that a risk of increased erosion existed without the benefit of expert testimony. Further, the court's conclusion, that filling the old river bed and creating a greatly increased risk of erosion was a serious impairment, was not clearly erroneous. Moreover, the court did not err in holding that the buyers had no way of knowing of the increased risk, even though a conversation with the the sellers' employee who performed the backfill work would have revealed the problem. The buyers were not required to speak with the sellers' employees before purchasing, particularly given the fact that when the field at pivot three was cleared and leveled, it looked like any other field. The sellers also contended that the buyers had merely to ask their own consultant, who would have informed them of the origin and obvious condition of the field. However, the buyers' consultant did not inspect the fields until after closing of the sale and thus could not have provided the buyers with any knowledge. H-D Irrigating, Inc. v. Kimble Properties, Inc., 2000 MT 212, 301 M 34, 8 P3d 95, 57 St. Rep. 832 (2000).

Bank Loan for Purchase of Contaminated Real Property — Negligent Misrepresentation, Constructive Fraud, and Punitive Damages — Summary Judgment Reversed: After the Department of Health and Environmental Sciences (now Department of Environmental Quality) discovered that soil had been contaminated with gasoline leaking from Habets' and other service station gas tanks in violation of 75-10-715, Habets entered into a buy-sell agreement for sale of his service station to Mattingly. Mattingly then met with First Bank Vice President Joe Dolan to secure financing. Dolan conducted a physical inspection of the service station property in order to obtain an impression of the value of the property and to determine whether First Bank would be secure in its loan. At the time of his inspection, Dolan was aware of the contamination caused by the service station gas tanks. The loan was approved by the First Bank loan committee made up of Dolan, Susan Hemmer, the bank president, and John Mulcare, an owner of another service station, all three of whom were aware of the contamination but did not discuss it with Mattingly or the loan committee. Mattingly learned of the contamination much later when he tried to sell the station. He then brought an action against Habets, Habets' realtor, and First Bank, alleging constructive fraud, negligence, and negligent misrepresentation by First Bank and seeking punitive damages. The District Court granted summary judgment to First Bank on all issues. The Supreme Court, following Kitchen Krafters, Inc. v. Eastside Bank of Mont., 242 M 155, 789 P2d 567 (1990), which was overruled, with regard to the elements for a claim of negligent misrepresentation against a financial institution, in Morrow v. Bank of America, N.A., 2014 MT 117, 375 Mont. 38, 324 P.3d 1167, stated that a threshold issue in a claim of negligent misrepresentation is whether the defendant made a representation as to a past or existing material fact upon which the claim is based. The Supreme Court pointed out that except for some basic facts involving the existence of the contamination, Dolan's visit to the gas station, and the action of the loan committee, the parties disagreed over the nature, scope, and import of the valuation of the property; disagreed whether First Bank's appraisal of the property and approval of the Mattingly loan constituted a representation as to the value of the property; and, if it was a representation, disagreed over whether Mattingly relied upon that representation. Citing McGregor v. Cushman/Mommer, 220 M 98, 714 P2d 536 (1986), the Supreme Court also stated that special circumstances may support a claim for constructive fraud when a party makes misleading statements concerning the physical condition or commercial value of real estate and pointed out that a jury might find that representations by First Bank with regard to the property would constitute these "special circumstances". Concerning the requirement of this section that in a claim for constructive fraud one party must gain an advantage over the other, the Supreme Court cited the fact that upon closing the sale of the station to Mattingly, First Bank was able to pay off a loan for the property made to Habets and that in making the loan to Mattingly, First

Bank was able to collect interest income from the loan. Because there were facts in dispute as to the foregoing issues, the Supreme Court held that summary judgment was not appropriate and that the District Court erred in granting summary judgment in favor of First Bank. Because 27-1-221 allows punitive damages against a party guilty of actual fraud or malice, the Supreme Court also reversed the District Court on the issue of punitive damages. Mattingly v. First Bank of Lincoln, 285 M 209, 947 P2d 66, 54 St. Rep. 1116 (1997).

Contract Clause Requiring Independent Investigation Not Bar to Negligent Misrepresentation Action: A real estate broker appealed a verdict finding that an employee had negligently misrepresented the boundary of property purchased by the Cechovics. The basis for the appeal was that the contract between the parties contained a clause requiring the Cechovics to conduct an independent investigation, which the Cechovics had not conducted, and that therefore the Cechovics' reliance on the employee's representation was not justified. The Supreme Court held that an independent investigation clause does not preclude justifiable reliance by a buyer on misrepresentations made by the seller and that in the present case, the jury had found that such reliance existed. Cechovic v. Hardin & Associates, Inc., 273 M 104, 902 P2d 520, 52 St. Rep. 854 (1995), following Wagner v. Cutler, 232 M 332, 757 P2d 779 (1988).

Negligent Misrepresentation Governed by Three-Year Negligence Statute of Limitations — Tolls Until Plaintiff Suffers Damages: A real estate broker appealed a verdict finding that he was liable because of his employee's negligent misrepresentation of a boundary on land purchased by the plaintiffs. The basis for the appeal was that the applicable statute of limitations was the 2-year time limit governing actions for fraud and that the suit had not been timely filed. The Supreme Court held that negligent misrepresentation involves breach of a reasonable standard of care and therefore is couched in terms of negligence and as such is subject to the 3-year negligence statute of limitations. The Supreme Court further held that the statute did not begin to run until damages were suffered and that did not occur in the present case until the plaintiffs learned that their house had been built on another's property. Cechovic v. Hardin & Associates, Inc., 273 M 104, 902 P2d 520, 52 St. Rep. 854 (1995), partially overruling Bushnell v. Cook, 221 M 296, 718 P2d 665 (1986).

Prima Facie Fraud Not Shown — No Instruction Required: A party that failed to establish a prima facie case of constructive fraud by proving or even asserting the existence of any breach of duty or fraudulent act or omission was not entitled to an instruction on the subject of constructive fraud. Story v. Bozeman, 259 M 207, 856 P2d 202, 50 St. Rep. 761 (1993).

Relationship of Negligent Misrepresentation to Fraud and Negligence Liability: Depending on circumstances, negligent misrepresentation can give rise to a case of constructive fraud under this section. Yet under Restatement (Second) of Torts 552, a negligent misrepresentation may be insufficient to constitute actual or constructive fraud but nevertheless give rise to negligence liability under 27-1-701 through the want of ordinary care of the defendant in managing his property or person. In the latter case, the test of liability is the exercise of reasonable care and is subject to comparative negligence. Bottrell v. Am. Bank, 237 M 1, 773 P2d 694, 46 St. Rep. 561 (1989), followed in Mattingly v. First Bank of Lincoln, 285 M 209, 947 P2d 66, 54 St. Rep. 1116 (1997).

Fiduciary Relationship Basis for Constructive Fraud Cause of Action: Dealings or transactions between parties who have a fiduciary relationship provide a sufficient contract to support an action for constructive fraud. Local Union No. 400 v. Bosh, 220 M 304, 715 P2d 36, 43 St. Rep. 388 (1986). See also Luke v. Gager, 2000 MT 377, 303 M 474, 16 P3d 377, 57 St. Rep. 1599 (2000).

Constructive Fraud in Real Estate Brokerage Agreement: Where defendant agreed to pay commission for brokerage services rendered by out-of-state plaintiff not licensed in Montana and services were performed by plaintiff both within and without Montana, the court found the parties had entered into a fiduciary relationship whereby neither party may take advantage of the other. Therefore, the fact that recovery may not be had for services rendered in Montana because of the proscription of 37-51-401 does not prevent recovery for services rendered out of the state. Ryckman v. Wildwood, Inc., 197 M 154, 641 P2d 467, 39 St. Rep. 378 (1982).

Sale of House: The prospective buyer of a house should surely not be required to take the house apart board by board to determine its condition. Where the jury could have found the seller often gave buyers misleading information and half-truths, the seller admitted on cross-examination that he was aware of many serious flaws in the house and did not inform buyers, and many of the flaws were not obvious and required far more than a superficial inspection to find them, constructive fraud on the seller's part was a crucial and perhaps the crucial element of the buyers' suit for damages or rescission. There also being numerous facts in dispute, it was reversible error to refuse buyers' constructive fraud instructions (to give an instruction that if material facts are known to one party and not the other, failure to disclose them is not actionable fraud) and to refuse to allow mention of constructive fraud in closing argument. The fact that the parties had a contract and had neither a fiduciary nor a confidential relationship would not bar a jury from finding constructive fraud. Mends v. Dykstra, 195 M 440, 637 P2d 502, 38 St. Rep. 2010 (1981), followed in McGregor v. Cushman/Mommer, 220 M 98, 714 P2d 536, 43 St. Rep. 206 (1986).

Trustee Gaining Advantage Through Fraud: Plaintiff's husband and defendant were brothers and partners in a ranching operation, although each owned the land individually. Plaintiff's husband died and defendant was named executor. A corporation was formed on May 1, 1973, to operate the ranch. Both parties transferred all assets to the corporation. Defendant's family got 364 more shares than plaintiff, and defendant was named president of the corporation. Restrictions were placed on the valuation and transfer of stock. On May 29, 1975, plaintiff consulted her own attorney and for the first time fully realized her position. All corporate votes became deadlocked. On April 29, 1977, plaintiff filed suit to dissolve the corporation, alleging fraud and oppressive conduct by defendant and mistake at the formation. The court found that defendant occupied a position of trust and confidence in relation to plaintiff. He was executor of her husband's estate and partner to her husband at the date of death; that status imposed on defendant the duties of a trustee. Because the result of incorporation was to give defendant control over plaintiff's assets, the trustee statutes were clearly violated. Defendant used his position to gain an advantage over plaintiff without fully disclosing the consequences and was guilty of fraud. Skierka v. Skierka Bros., Inc., 192 M 505, 629 P2d 214, 38 St. Rep. 754 (1981).

Constructive Fraud — Failure of Plaintiffs to Investigate Misrepresentation: Where plaintiffs seek rescission of a contract for sale of a bar, defendants' contention that plaintiffs could have discovered, upon investigation, defects of the premises does not mitigate defendants' duty to erase false impressions, especially where, as here, defendants knew of the defects, investigation was made difficult by defendants, repairs were substantial, and plaintiffs were novices. Moschelle v. Hulse, 190 M 532, 622 P2d 155, 37 St. Rep. 1506 (1980), relied on in McGregor v. Cushman/Mommer, 220 M 98, 714 P2d 536, 43 St. Rep. 206 (1986).

Waiver of Right to Rescind: Plaintiffs do not waive their rights to rescind a contract for sale of a bar even if they wait 9 months after execution of the contract where defects in premises did not surface until the end of the 9-month period. Moschelle v. Hulse, 190 M 532, 622 P2d 155, 37 St. Rep. 1506 (1980).

Failure to Read Deed Carefully: Where plaintiff's principal reason for wishing to rescind mineral deed was her mistaken belief that she had granted a royalty interest, evidence that plaintiff was astute in negotiations and that consideration for the deed was fair and adequate but that plaintiff failed to read carefully the instrument she signed did not establish constructive fraud under this section. Clough v. Jackson, 156 M 272, 479 P2d 266 (1971).

Deed From Mother to Son: Constructive trust would not be imposed on lands deeded son by aged mother in absence of evidence to show that son gained land by accident, mistake, undue influence, violation of trust, or other wrongful act or by constructive fraud as defined in statute. Bodine v. Bodine, 149 M 29, 422 P2d 650 (1967).

28-2-407. What constitutes undue influence.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Premarital Agreement Enforceable — Premarital Agreement Between Father and Surrogate Mother Signed Voluntarily Without Undue Influence or Duress — Parent-Child Relationship Provision Not Equitably Unconscionable. Sayler v. Yan Sun, 2023 MT 175, 413 Mont. 303, 536 P.3d 399.

Settlement Agreement Properly Approved — Sibling Trustee Present and Represented by Counsel — Mediation's Key Terms Understood Despite COVID-19 Illness — Undue Influence Inapplicable — Doctrine of Laches Elements Established. Lindemulder v. Lindemulder, 2022 MT 119, 409 Mont. 69, 512 P.3d. 260.

Gift of Shares of Family Farm to Son — Undue Influence Not Proven by Other Son: The mother owned a family farm where one of her two sons worked as the full-time manager. The mother expressed interest in preserving the farm and she gifted her controlling shares to the manager son. After taking the mother to Billings for medical evaluations and facilitating a gift of a convertible to himself, the other son filed suit alleging undue influence. The District Court found that the mother's gift of shares to the manager son was not the result of undue influence, that the other son failed to meet his burden of proving undue influence, that the gift of shares without condition became irrevocable upon acceptance, and that the essential elements of an irrevocable gift inter vivos were satisfied. Larson v. Larson, 2017 MT 299, 389 Mont. 458, 406 P.3d 925.

Two Contested Wills and Trusts — Appointment of Neutral Representative — Undue Influence, Fraud, or Duress: The decedent executed a will and trust in 2010 leaving the majority of her estate to her niece, with whom she shared a close relationship. In 2012, the decedent executed a new will leaving a sizable portion of her estate to her housekeeper and handyman. The decedent died a year later. The housekeeper petitioned for probate of the 2012 will, and the niece objected and cross-petitioned for probate of the 2010 will. The District Court appointed a neutral personal representative to serve as a special fiduciary to the decedent's trust. A jury found that the 2012 will was procured by undue influence, fraud, or duress. However, the District Court rejected the niece's requests to receive fees and costs and to admit the 2010 will and trust because the special verdict form did not ask the jury to make any findings on the 2010 will or trust. On appeal by both parties, the Supreme Court affirmed in part, upholding the District Court's appointment of a neutral personal representative and special fiduciary, admission of settlement document evidence because one party opened the door to the line of questioning, and suppression of testimony by the decedent's attorneys relating to her dispositional intentions. The Supreme Court also found that while the District Court erred in precluding testimony because a party violated a sequestration order, numerous professional witnesses and friends of the decedent provided similar testimony. The Supreme Court held that the will contestants have the burden of establishing undue influence, fraud, or duress and that the jury properly found that the 2012 will was procured in this manner. However, the Supreme Court found that the District Court erred in refusing to admit the 2010 will to probate and in finding that the niece was statutorily barred from recovering attorney fees. In re Estate of Edwards, 2017 MT 93, 387 Mont. 274, 393 P.3d 639.

Allegation of Undue Influence When Testator Is Taking Heavy Medication at Time Will Is Executed — No Evidence of Specific Acts of Undue Influence Presented — Summary Judgment Proper: After the testator's death, one of his daughters claimed that her father had been under undue influence at the time he executed the will. The daughter argued that her father was taking heavy medication at the time the will was executed; however, she did not point to specific acts of undue influence and the District Court granted summary judgment against the daughter. She appealed the decision to the Supreme Court, which affirmed the District Court ruling. The court agreed that summary judgment was proper because the daughter's suspicion of undue influence was not supported by any admissible evidence of specific acts of undue influence outlined in this section. In re Estate of Mead, 2014 MT 264, 376 Mont. 386, 336 P.3d 362.

Substantial Circumstantial Evidence of Undue Influence in Order to Acquire Parent's Assets: A son and a daughter both sought probate of different wills signed by their mother. The District Court found that the decedent was subject to undue influence at the time she transferred certain property to the son, so probate was denied, resulting in intestacy. The son appealed, but the Supreme Court affirmed. There was substantial circumstantial evidence that the son took advantage of the mother's physical and mental weakness when she transferred the property to the son. Based on the nature and timing of the transfer, the District Court did not err in concluding that the transfer was the result of undue influence by the son. In re Estate of Lightfield, 2009 MT 244, 351 M 426, 213 P3d 468 (2009).

Sufficient Finding of Undue Influence Over Parent — Constructive Trusts Properly Imposed and Damages Awarded: When Josephine became too ill to manage herself and her affairs, her daughter Melissa agreed to move in with Josephine and care for her. In the process, as Josephine's health steadily declined, Melissa used her confidential relationship with Josephine to manipulate Josephine and her finances, controlling Josephine's checking account, mail, and payment of bills and expenses. By the time Josephine died, Melissa had obtained title to all of Josephine's real property, sold Josephine's property in Ovando and Florida, encumbered the remaining property with over $175,000 in loans taken out in Josephine's name, used part of the loan proceeds to buy property in Missoula and Las Vegas, exhausted all cash in Josephine's house, repeatedly overdrawn Josephine's checking account, fraudulently cashed one of Josephine's certificates of deposit by forging Josephine's name to it, used and obtained credit cards in Josephine's name and charged the account to the credit limit, exhausted all of Josephine's savings, Social Security, retirement, and annuity income, retained rental income from Josephine's rental units without accounting for it, destroyed years of Josephine's financial records while keeping very few records after assuming control of Josephine's affairs, fabricated lease documents and forged signatures on them to obtain loans in Josephine's name, used Josephine's money to pay all personal bills and obligations, never informed her siblings or provided an accounting of expenditures of Josephine's income and assets, and refused to provide a copy of Josephine's will, answer questions, or provide any other information. Melissa's brother Robert obtained a copy of the will and commenced an action to recover assets of Josephine's estate from Melissa. The District Court held Melissa accountable for a money judgment of $177,000 and for other items, totaling nearly $400,000. The court imposed a constructive trust on all real property that Melissa had obtained from Josephine or purchased with loan proceeds obtained in Josephine's name and awarded Robert costs and attorney fees. Melissa appealed. The Supreme Court applied the criteria in In re Estate of Bradshaw, 2001 MT 92, 305 M 178, 24 P3d 211 (2001), and determined that Melissa had exercised undue influence over Josephine. It concluded that there were ample reasons for imposition of the constructive trusts because the properties were obtained through undue influence and would have unjustly enriched Melissa if she were allowed to retain title to the properties. The damage award was based on substantial evidence and did not constitute error. The award of attorney fees and costs was within the equitable powers of the District Court based on the extraordinary efforts by Melissa to conceal her use of Josephine's property and money, which required Robert to make substantial efforts to successfully uncover and prove Melissa's wrongful conduct. The District Court was affirmed on all issues. Monroe v. Marsden, 2009 MT 137, 350 M 327, 207 P3d 320 (2009).

Summary Judgment Proper Absent Proof of Undue Influence: Stanton sued for distribution of trust proceeds that were bequeathed to him in Barker's will. Defendants asserted that Stanton had exerted undue influence over Barker, invalidating the will, and that a prior version of the will should be followed, which included defendants as beneficiaries. The District Court found that defendants did not prove undue influence and granted summary judgment to Stanton. On appeal, the Supreme Court applied the criteria in In re Estate of Bradshaw, 2001 MT 92, 305 M 178, 24 P3d 211 (2001), to determine whether Stanton had exerted undue influence, noting that the defendants bore the burden of proof. Stanton admitted a confidential relationship with Barker, but that fact was insufficient in itself to prove undue influence. Because of the relationship, Stanton had the opportunity to exercise undue influence. However, opportunity alone is not sufficient to prove undue influence and invalidate a will. Barker's physical and mental condition and the naturalness of the disposition were not at issue. Defendants failed to prove undue influence, and summary judgment for Stanton was affirmed. Stanton v. Wells Fargo Bank Mont., N.A., 2007 MT 22, 335 M 384, 152 P3d 115 (2007). See also In re Estate of Mead, 2014 MT 264, 376 Mont. 386, 336 P.3d 362.

No Finding of Undue Influence Under Bradshaw Criteria: Contestants to their father's will asserted that their father was unduly influenced by one of his sons. The District Court found no undue influence, and on appeal, the Supreme Court examined each of the criteria in In re Estate of Bradshaw, 2001 MT 92, 305 M 178, 24 P3d 211 (2001), and affirmed. All of the children had confidential relationships with their father at certain points in their lives, but the mere opportunity to exercise influence on a testator is not sufficient to prove undue influence. Although the contestants may have suspected that the father was unduly influenced, they did not meet their burden of proving that fact. Also, the District Court made the requisite findings regarding the father's physical and mental capacity and condition, the possibility of unnaturalness of the disposition, and the timing and circumstances surrounding the demands and importunities that may have affected the father's ability to withstand any possible influence, and the findings were supported by credible evidence. In re Estate of Harms, 2006 MT 320, 335 M 66, 149 P3d 557 (2006).

Validity of Promissory Note Executed to Satisfy Charge-Back Liability in Nigerian Scam: Hughes executed a promissory note to satisfy a charge-back liability necessitated by Hughes' participation in a Nigerian scam. Hughes made the first payment on the note, but failed to make any more payments, and the bank that issued the note initiated an action for judicial foreclosure. The District Court granted summary judgment to the bank on the promissory note, and Hughes appealed. The Supreme Court considered Hughes' arguments regarding lack of consideration, menace, and undue influence. Hughes became liable under 30-4-212 for satisfying the entire charge-back debt, so the note did not fail for lack of consideration. Hughes' first quarterly payment comprised a ratification of the contract, so the note did not fail for consent because of menace. Whatever influence the bank employee exerted over Hughes, it did not rise to the level of substituting the employee's will for that of Hughes, nor was there any indication that Hughes was in a mentally or physically weak state or in a confidential relationship with the employee, so the note did not fail for lack of consent as a result of undue influence. Based on the claims made and the facts asserted, summary judgment for the bank was affirmed. Valley Bank of Ronan v.

Hughes, 2006 MT 285, 334 M 335, 147 P3d 185 (2006), following Averill Mach. Co. v. Taylor, 70 M 70, 223 P 918 (1924), and Heintz v. Vestal, 185 M 233, 605 P2d 606 (1980).

Validity of Voluntary Easement Affirmed: The Permanns requested that Urick grant an easement across Urick's property for the Permanns to go camping and move cattle, and Urick agreed. When Urick's sons discovered that the voluntary easement had been granted, they persuaded Urick to rescind the easement. Urick requested that the Permanns convey the easement back to her. They refused. Urick filed suit and then subsequently died. Urick's son Gliko, as trustee of Urick's estate, brought an action against the Permanns seeking to have the easement rescinded, citing mutual mistake, constructive fraud, undue influence, and lack of consideration. The District Court held that the easement was valid, and Gliko appealed. The Supreme Court considered each of Gliko's rescission arguments in turn. The language of the easement was simple and unambiguous, so there was no mutual mistake. Urick had testified by deposition that no misleading statements were made relating to the easement, so there was no constructive fraud. There was no confidential relationship between Urick and the Permanns, Urick was not possessed of weakness of mind, and no advantage was taken of Urick's necessities or distress, so there was no undue influence. Last, there was no evidence that consideration was meant to be given, so lack of consideration was not a valid ground for rescission. The District Court was affirmed. Gliko v. Permann, 2006 MT 30, 331 M 112, 130 P3d 155 (2006).

No Requirement That All Five Statutory Criteria Be Proved to Show Undue Influence — Return to Discretionary Standard and Line of Cases Requiring That All Criteria Must Be Satisfied Overruled: This section sets forth the statutory definition of undue influence. In 1965, in In re Maricich, 145 M 146, 400 P2d 873 (1965), the Supreme Court set forth five criteria as factors that a court may consider in determining a question of undue influence: (1) any confidential relationship between the person alleged to be exercising undue influence and the donor; (2) the physical condition of the donor as it may affect the donor's ability to withstand influence; (3) the mental condition of the donor as it *may* affect the donor's ability to withstand influence; (4) the unnaturalness of the disposition as it relates to showing an unbalanced mind or a mind easily susceptible to undue influence; and (5) demands and importunities as they may affect the donor, taking into account the time, place, and surrounding circumstances. The court continued this discretionary approach in Cameron v. Cameron, 179 M 219, 587 P2d 939 (1978). Then, beginning with In re Estate of Aageson, 217 M 78, 702 P2d 338 (1985), the court strayed from that approach and held that a court *must* consider the five criteria and set a standard for their consideration in which a proponent of an undue influence theory must satisfy each of the statutory criteria. In the present case, the Supreme Court was asked to consider whether the District Court incorrectly determined that a person's status as a beneficiary was the result of undue influence. The District Court found all five factors to be present, but the presence of four of the five factors was challenged on appeal. The court noted that the standard requiring a finding of all five statutory criteria was not supported by any authority and did not square with the alternative statutory definitions of undue influence in this section. Therefore, the court returned to the Cameron standard and overruled subsequent cases holding to the contrary, stating that a court *may* consider the five criteria in determining the existence of undue influence but that the five criteria need not all be proved to show undue influence in any given case. The statutory requirements control, and the five criteria are simply nonexclusive considerations available to guide the District Court in its application of the requirements. In the present case, the District Court correctly determined that each of the criterion for establishing a claim of undue influence had been established. In re Estate of Bradshaw, 2001 MT 92, 305 M 178, 24 P3d 211 (2001), overruling Christensen v. Britton, 240 M 393, 784 P2d 908 (1989), In re Estate of Luger, 244 M 301, 797 P2d 229 (1990), Taylor v. Koslosky, 249 M 215, 814 P2d 985 (1991), In re Estate of Jochems, 252 M 24, 826 P2d 534 (1992), Flikkema v. Kimm, 255 M 34, 839 P2d 1239 (1992), In re Estate of Lien, 270 M 295, 892 P2d 530 (1995), In re Estate of DeCock, 278 M 437, 925 P2d 488 (1996), In re Estate of Lande, 1999 MT 162, 295 M 160, 983 P2d 308 (1999), and Luke v. Gager, 2000 MT 377, 303 M 474, 16 P3d 377 (2000), and followed in In re Estate of Wittman, 2001 MT 109, 305 M 290, 27 P3d 35 (2001), Pense v. Lindsey, 2003 MT 182, 316 M 429, 73 P3d 168 (2003), and In re Estate of Harms, 2006 MT 320, 335 M 66, 149 P3d 557 (2006).

Inappropriate Control, Advanced Age of Donor, and Unnatural Disposition of Donor's Property as Sufficient Evidence of Undue Influence: Mowrer, a 104-year-old woman, was physically weak when the Eddies arrived at her home in Kansas, moved into her home, immediately secured several hundred thousand dollars of her money, and then moved her to Montana away from family and long-time friends, keeping her isolated in their home even though she was mentally competent. In determining whether Mowrer had exercised free will in transferring property to the Eddies, consideration was given to the nature of the relationship between the parties, Mowrer's susceptibility to undue influence, and the reasonableness of the transfers in light of existing circumstances. In this case, the evidence supported the determination that: (1) Mowrer was under the Eddies' absolute and inappropriate control; (2) Mowrer was susceptible to undue influence because of advanced age and physical infirmity; and (3) the Eddies took advantage of Mowrer's weakness and their control over her to secure an unnatural disposition of essentially all her property to them. The gift was the result of fraud, duress, or undue influence and was properly set aside. In re Guardianship of Mowrer, 1999 MT 73, 294 M 35, 979 P2d 156, 56 St. Rep. 300 (1999).

Leaving Bulk of Estate to One Child Not of Itself an Unnatural Disposition: Shodin brought an action to block having her mother's will admitted to probate, alleging that the will was a product of undue influence asserted by her sister over their mother. The Supreme Court held that the fact that a parent leaves the majority of assets to just one child is not, by itself, evidence that the transfer was an unnatural disposition. In re Estate of Tipp, 281 M 120, 933 P2d 182, 54 St. Rep. 90 (1997), following In re Estate of Lien, 270 M 295, 892 P2d 530 (1995).

Charitable Immunity Rejected: Montana has never adopted the doctrine of charitable immunity, and the District Court properly declined to allow the defense in a church member's action against a church for breach of fiduciary duty. Davis v. Church of Jesus Christ of Latter Day Saints, 258 M 286, 852 P2d 640, 50 St. Rep. 535 (1993).

Fiduciary Duty Between Church and Member: In an action by a church member injured during a fall on church property, the existence of a fiduciary duty depended upon the satisfactory proof of a special relationship. The lower court's finding of existence of the duty was not appropriate for determination on a summary judgment motion, but the lower court properly refused the church summary judgment on the member's claim that the church breached its fiduciary duty. Whether the duty existed, whether the member's reliance on the duty was reasonable, and whether her reliance on the duty could be justified after a certain point in time could not be resolved by summary judgment. The member contended that the church plays a major role in all aspects of a member's life, that member had contributed over $75,000 to the church over a 10-year span and had contributed much time and effort to the church, and that the church provides a member with an extended family and a vast network of support for all financial and other problems. Davis v. Church of Jesus Christ of Latter Day Saints, 258 M 286, 852 P2d 640, 50 St. Rep. 535 (1993), overruled, to the extent that the issue of whether a fiduciary duty or a special relationship exists between two parties is a question of law, not fact, in Gliko v. Permann, 2006 MT 30, 331 M 112, 130 P3d 155 (2006).

Suit for Breach of Fiduciary Duty After Suing for Negligence — Res Judicata: A church member who successfully sued in a negligence action for damages resulting from a fall on church property later sued for breach of fiduciary duty, claiming physical and mental pain and suffering arising from the breach. Recovery for emotional distress on a breach of fiduciary duty claim must be supported by tortious conduct that results in a substantial invasion of a legally protected interest and causes a significant impact upon the plaintiff. The suffering alleged in this action is alleged to have arisen from defendants' conduct after the injury and is not related to the suffering from the injury itself. Damages for invasion of a legally protected interest were not barred by res judicata. Davis v. Church of Jesus Christ of Latter Day Saints, 258 M 286, 852 P2d 640, 50 St. Rep. 535 (1993), overruled, to the extent that the issue of whether a fiduciary duty or a special relationship exists between two parties is a question of law, not fact, in Gliko v. Permann, 2006 MT 30, 331 M 112, 130 P3d 155 (2006).

Termination Agreement — No Undue Influence or Economic Duress: Employee who signed an employment termination agreement contended that his wife's illness created emotional distress and increased financial demands, enhanced his need to remain in the community, increased his demand on the company group health insurance plan, and enhanced the need to avoid further stress on his family, all of which imposed undue influence on him to sign the agreement. The undue influence claim necessarily included an argument of economic duress. After considering the facts, including claimant's voluntary signing of the agreement by his free will and after reading and understanding the terms of the agreement, his claims were insufficient to meet the tests of undue influence or economic duress. Somersille v. Columbia Falls Aluminum Co., 255 M 101, 841 P2d 483, 49 St. Rep. 904 (1992), following Horgan v. Indus. Design Corp., 657 P2d 751 (Utah 1982), and Hoven v. First Bank (N.A.)-Billings, 244 M 229, 797 P2d 915 (1990).

Contested Trust — Summary Judgment Appropriate: Summary judgment in a case contesting a trust agreement was proper when Taylor failed to demonstrate a material fact issue regarding the naturalness of the disposition. Mere allegation that because her brother was acting as the decedent's fiduciary and that because of alleged animosity between her and her brother, he exercised undue influence over the decedent to have her left out of the will was insufficient to meet her burden of showing disputed material facts regarding whether the disposition was unnatural. Taylor v. Koslosky, 249 M 215, 814 P2d 985, 48 St. Rep. 649 (1991), followed in In re Estate of Eggebrecht, 1998 MT 249, 291 M 174, 967 P2d 388, 55 St. Rep. 1028 (1998), and overruled, to the extent that a court is not required to but may consider the criteria in Cameron v. Cameron, 179 M 219, 587 P2d 939 (1978), in determining the existence of undue influence, but the five criteria need not all be proved to show undue influence in any given case, in In re Estate of Bradshaw, 2001 MT 92, 305 M 178, 24 P3d 211 (2001).

Undue Influence Not Contingent Upon Showing of Incompetence: The lower court found that an elderly man's giving of all his personal and real property to the defendants was fair and regular because the man was competent. The Supreme Court reversed and remanded the case, directing the lower court to determine the amount of damages the man's estate was entitled to recover. The court held that although the evidence indicated that the man was competent and knew what he was doing, his competence had nothing to do with the issue of undue influence. The court ruled that there was overwhelming evidence of undue influence and that the lower court had abused its discretion in not finding for the plaintiff. Christensen v. Britton, 240 M 393, 784 P2d 908, 46 St. Rep. 2223 (1989).

Economic Duress Not Established: Economic duress is not established merely by proof that consent was secured by the pressure of financial circumstances or by the fact that one party insisted upon a legal right and the other party yielded to such insistence. Where plaintiffs were forced to continue to refinance because of inability to pay their loans and consequent threat of bank foreclosure, there is no "economic duress" that will void the loan contract. Shiplet v. First Sec. Bank of Livingston, Inc., 234 M 166, 762 P2d 242, 45 St. Rep. 1816 (1988).

No Question of Fiduciary Duty When Judgment Based Only on Good Faith and Fair Dealing: Appellant argued that District Court prejudiced its interests by improperly instructing the jury that, as franchisor, appellant owed a fiduciary duty to respondents as franchisees. The Supreme Court noted that a franchise relationship is inherently a business relationship rather than a fiduciary relationship. However, the questioned jury instruction was found to be primarily definitional; therefore, the Supreme Court found it unnecessary to rule on whether the special facts of the case gave rise to a fiduciary duty since the District Court only held appellant to the responsibility of acting in good faith and fair dealing with respondents. Dunfee v. Baskin-Robbins, Inc., 221 M 447, 720 P2d 1148, 43 St. Rep. 964 (1986).

No Undue Influence When Implications Based on Opinions: A plaintiff's opinions alone do not provide a sufficient basis in fact to prove undue influence when there is no evidence of abuse of confidence or of grossly oppressive or unfair advantage. Westlake v. Osborne, 220 M 91, 713 P2d 548, 43 St. Rep. 200 (1986).

Undue Influence on Testator Making Will: Undue influence was present when testator made 1980 wills at urging of three of his four children when at time of making the wills testator was 91 years old, confined to a rest home, hard of hearing, and suffering from a brain disorder, and the wills disinherited the fourth child, whose interests testator's actions since 1948 had been directed toward protecting. The Supreme Court held there was substantial credible evidence to support the District Court's determination that there was undue influence and dismissal of petition for probate of the 1980 wills. In re Estate of Aageson, 217 M 78, 702 P2d 338, 42 St. Rep. 1038 (1985).

Incompetence and Undue Influence Never Presumed — Presumption of More Satisfactory Evidence Not Error: Although incompetence or undue influence is never presumed and it is clearly the burden of the plaintiff to prove such matters, when the defendant failed to engage in the usual practice of calling upon doctors and nurses from the confining hospital to clearly show mental capacity at the time the instrument was signed, it was not error for the District Court to rely on the presumption in 26-1-602 that provides that more satisfactory evidence would be adverse if weaker and less satisfactory evidence is offered and it is within the pertinent party's power to produce more satisfactory evidence. That presumption relates only to the type and lack of evidence of the defendant, not to the plaintiff's burden of proof. Adams v. Allen, 209 M 149, 679 P2d 1232, 41 St. Rep. 610 (1984).

Will Versus Deed — Test for Undue Influence Different: Plaintiff obtained a power of attorney from his sick and elderly aunt and then brought her to Montana to live with him. The aunt later executed a new will leaving her estate to the plaintiff and deeded a ranch to plaintiff. It was alleged that plaintiff exercised undue influence over his aunt in the execution of the deed, the will, and the power of attorney. The court employed 28-2-407 in concluding that plaintiff had exercised undue influence in the execution of the deed. A different test is employed when establishing undue influence in the execution of a will. A will may not be defeated on grounds of undue influence unless the testator is induced to execute an instrument which is in form and appearance his will but in reality expresses testamentary dispositions which he would not have voluntarily made. In this case the will was drafted by the lawyer the testator had used for many years, and there is no evidence that plaintiff participated in the preparation of the will or that he dictated the will's terms. The will should therefore not have been set aside. Dybvik v. Dybvik, 201 M 389, 654 P2d 989, 39 St. Rep. 2184 (1982).

Voidance of Quitclaim Deeds Properly Denied — Family Relationship Not Found as Basis for Undue Influence: The plaintiff, son of a deceased rancher, received 24½% of the surface rights to his father's ranch in accordance with the terms of an estate plan established for the benefit of the plaintiff and his brothers, the defendants. Upon leaving the ranch, plaintiff executed one quitclaim deed to his mineral interest in 1977 and one quitclaim deed to his surface interest in 1968 in exchange for a promise that the defendants would hold him harmless on a promissory note. The District Court did not err (in a subsequent challenge by the plaintiff to the validity of the quitclaim deeds) in declaring both deeds to be valid and denying the plaintiff any interest in the ranch. The District Court found that the facts of the case did not satisfy the stated statutory requisites, and the Supreme Court will not substitute its judgment for the judgment of the trial court. Turley v. Turley, 199 M 265, 649 P2d 434, 39 St. Rep. 1336 (1982).

Threat to Withdraw as Legal Counsel: Undue influence was not present when attorney, long after initiation of attorney-client relationship but only minutes before he was to defend client on criminal charges, threatened to withdraw as counsel unless client executed security agreement and quitclaim deed as security for attorney's fee. The security arrangement was fair and equitable. The per hour charge for attorney's services was established by earlier agreement; papers executed on day of trial simply established method of payment. Matthews v. Berryman, 196 M 49, 637 P2d 822, 38 St. Rep. 2112 (1981).

Promissory Note — Undue Influence in Making: A promissory note was executed to appellant by the deceased, with whom he had a close confidential relationship. The decedent's age caused her to rely quite heavily on appellant in running her farm and made her more susceptible to his influence. The amount of the note was also quite large in relation to the alleged consideration. Under the five-factor test enumerated in Cameron v. Cameron, 179 M 219, 587 P2d 939 (1978), there was substantial evidence to support a finding of undue influence in the creation of the note. Heintz v. Vestal, 185 M 233, 605 P2d 606 (1980).

Elements Constituting Undue Influence: In determining the issue of undue influence, the court may consider the confidential relationship of the person attempting to influence the donor, the physical and mental conditions of the donor as they affect his ability to withstand the influence, the unnaturalness of the disposition as it relates to showing an unbalanced mind or a mind easily susceptible to undue influence, and demands and importunities as they may affect the particular donor, taking into consideration the time, place, and all surrounding circumstances. Cameron v. Cameron, 179 M 219, 587 P2d 939 (1978), followed in In re Estate of Bradshaw, 2001 MT 92, 305 M 178, 24 P3d 211 (2001), and In re Estate of Wittman, 2001 MT 109, 305 M 290, 27 P3d 35 (2001). See also Christensen v. Britton, 240 M 393, 784 P2d 908, 46 St. Rep. 2223 (1989), In re Estate of Luger, 244 M 301, 797 P2d 229, 47 St. Rep. 1642 (1990), In re Estate of Jochems, 252 M 24, 826 P2d 534, 49 St. Rep. 116 (1992), Flikkema v. Kimm, 255 M 34, 839 P2d 1239, 49 St. Rep. 880 (1992), In re Estate of DeCock, 278 M 437, 925 P2d 488, 53 St. Rep. 992 (1996), In re Estate of Tipp, 281 M 120, 933 P2d 182, 54 St. Rep. 90 (1997), Hauck v. Seright, 1998 MT 198, 290 M 309, 964 P2d 749, 55 St. Rep. 838 (1998), In re Guardianship of Mowrer, 1999 MT 73, 294 M 35, 979 P2d 156, 56 St. Rep. 300 (1999), and In re Estate of Lande, 1999 MT 162, 295 M 160, 983 P2d 308, 56 St. Rep. 642 (1999). Christensen was followed in Luke v. Gager, 2000 MT 377, 303 M 474, 16 P3d 377, 57 St. Rep. 1599 (2000). Christensen, Estate of Luger, Estate of Jochems, Flikkema, Estate of DeCock, and Estate of Lande, as well as Taylor v. Koslosky, 249 M 215, 814 P2d 985 (1991), In re Estate of Lien, 270 M 295, 892 P2d 530 (1995), and Luke v. Gager, 2000 MT 377, 303 M 474, 16 P3d 377 (2000), were overruled, to the extent that a court is not required to but *may* consider the five criteria in Cameron v. Cameron, 179 M 219, 587 P2d 939 (1978), in determining the existence of undue influence, but the five criteria need not all be proved to show undue influence in any given case, in In re Estate of Bradshaw, 2001 MT 92, 305 M 178, 24 P3d 211 (2001).

Testimony of Attorney: Although testatrix was 85 and had infirmities associated with old age at the time her will was executed, testimony of her attorney, that due to her age and failing eyesight and her desire to make unequal distribution of her property he had made a special effort to assure himself of her competence before preparing her will and deeds, was sufficient to overcome allegations of contestants. Blackmer v. Blackmer, 165 M 69, 525 P2d 559 (1974).

Failure to Read Instrument Carefully: Where plaintiff's principal reason for wishing to rescind mineral deed was her mistaken belief that she had granted a royalty interest, evidence that plaintiff was astute in negotiations and that consideration for the deed was fair and adequate but that plaintiff failed to read carefully the instrument she signed did not establish undue influence under this section. Clough v. Jackson, 156 M 272, 479 P2d 266 (1971).

Burden of Proof:

In cases involving undue influence, contestant has the burden of proof and must produce substantial evidence to prove undue influence. In re Maricich's Estate, 145 M 146, 400 P2d 873 (1965).

The burden of proving undue influence upon testator in making his will is upon the contestant, and in order to establish it as a fact it must be shown by proof that it was exercised upon the mind of the testator directly to procure its execution. Mere suspicion that by reason of the close relation between the testator and the beneficiary the latter may have had opportunity to ingratiate himself in the former's favor and thus exercise influence over him is insufficient. Hale v. Smith, 73 M 481, 237 P 214 (1925).

Sufficiency of Evidence to Support Undue Influence:

Facts that beneficiary under a second will was never close to his alleged godfather until discovery that latter had bank account, the poor physical condition of the testator, the unnaturalness of the disposition, and importunities made upon the testator by telling him his friends were going to put him in an insane asylum constituted substantial evidence to support a verdict setting aside second will. In re Maricich's Estate, 145 M 146, 400 P2d 873 (1965).

Evidence in an action to set aside a will on the ground of undue influence alleged to have been exercised by a testator's niece, who was made the principal beneficiary under the will, who for the last 9 years of the life of deceased had cared for him, and whom he had treated as his own daughter showed an entire absence of proof of undue influence and therefore was insufficient to warrant its setting aside on that ground. Hale v. Smith, 73 M 481, 237 P 214 (1925).

Facts Tending to Prove or Disprove Undue Influence:

Facts to be considered in proving whether undue influence was exercised are: confidential relationship of person attempting to influence testator, the testator's physical and mental condition, unnaturalness of the disposition, and the demands and importunities as they affected testator. In re Maricich's Estate, 145 M 146, 400 P2d 873 (1965), followed in In re Estate of Hogan, 218 M 428, 708 P2d 1018, 42 St. Rep. 1711 (1985), In re Estate of Lien, 270 M 295, 892 P2d 530, 52 St. Rep. 190 (1995), In re Estate of Eggebrecht, 1998 MT 249, 291 M 174, 967 P2d 388, 55 St. Rep. 1028 (1998), In re Estate of Bradshaw, 2001 MT 92, 305 M 178, 24 P3d 211 (2001), and In re Estate of Wittman, 2001 MT 109, 305 M 290, 27 P3d 35 (2001). Estate of Lien was distinguished in In re Estate of Lande, 1999 MT 162, 295 M 160, 983 P2d 308, 56 St. Rep. 642 (1999), and Estate of Lien and Estate of Lande were overruled, to the extent that a court is not required to but may consider the criteria in determining the existence of undue influence, but the five criteria need not all be proved to show undue influence in any given case, in In re Estate of Bradshaw, 2001 MT 92, 305 M 178, 24 P3d 211 (2001). See also Pense v. Lindsey, 2003 MT 182, 316 M 429, 73 P3d 168 (2003).

One influenced by love and affection and gratitude for services performed is not acting under undue influence. In re Maricich's Estate, 145 M 146, 400 P2d 873 (1965).

Where no fiduciary relations existed between mortgagor and mortgagee and they dealt at arm's length, each being represented by counsel when the mortgage was executed, there was no undue influence exerted toward securing its execution, within the meaning of subsection (1) of this section, defining "undue influence" as abuse of a confidence or authority reposed in one for the purpose of obtaining an unfair advantage over another. Pederson v. Thoeny, 88 M 569, 295 P 250 (1930).

Undue influence sufficient to invalidate a will must be such as to control the mental operations of the testator, overcome his power of resistance, and thus cause him to adopt the will of another in the disposition of his property which he would not have made if left freely to act in accordance with his own pleasure. Hale v. Smith, 73 M 481, 237 P 214 (1925).

Relationship of the Parties:

In a will contest where the jury found undue influence, trial judge did not abuse discretion in granting proponents a new trial on the question of influence that the jury found to exist with respect to proponents' mother where the will was executed without the knowledge of the beneficiaries, it was drafted by an attorney chosen by the testatrix, and testatrix did not change the will for 20 months before her death. In re Cocanougher's Estate, 141 M 16, 375 P2d 1009 (1962).

To meet the requirement of this definition, the one party to the negotiations must occupy a superior position with reference to the other by reason of a real or apparent authority he holds over him, arising out of preexisting relations, or assumes at the time because of the weakness of mind or distress or necessities of the other, by reason of which he knowingly gains an advantage, which in contemplation of law is unconscionable. Emerson-Brantingham Implement Co. v. Anderson, 58 M 617, 194 P 160 (1920).

Sufficiency of Pleading: Answer in an action on a promissory note stating facts that defendant was afflicted with a diseased and resultant weak mind, that he reposed special confidence in plaintiff (his brother), and that the latter, taking advantage of this confidence, unduly influenced defendant to make the note was sufficient to constitute a plea of undue influence under this section. Stagg v. Stagg, 96 M 573, 32 P2d 856 (1934).

Demands and Importunities May Amount to Undue Influence: Demands and importunities may amount to undue influence, without being coupled with fraud, threats, or misrepresentation; whether they do or not depends upon what they were, how persistently and under what circumstances they were employed, and whether the mind of the testator was so infirm as to be overpowered by them. Murphy v. Nett, 47 M 38, 130 P 451 (1913).

Theory: The theory underlying the doctrine of undue influence is that the testator is induced, by the means employed, to execute an instrument in form and appearance his will but in reality expressing testamentary dispositions which he would not have voluntarily made. Murphy v. Nett, 47 M 38, 130 P 451 (1913).

Law Review Articles

Consumer Contracts in Action, Furth-Matzkin, 82 Mont. L. Rev. 97 (2021).

Blackmer v. Blackmer: The Presumption of Undue Influence in Montana, Swartley, 37 Mont. L. Rev. 250 (1976).

28-2-408. Kinds of mistake.

Case Notes

Sufficient Evidence for Rescission of Workers' Compensation Settlement Agreement Based on Mutual Mistake of Material Fact Not Discovered Until After Settlement: Gamble was injured on the job, the parties entered a settlement agreement, and the employer began paying benefits based on a medical diagnosis, yet Gamble's condition worsened. Finally, Gamble went to a specialist who ran additional tests and discovered that Gamble had suffered an odontoid fracture of the spine that was consistent with the job injury but that had been unnoticed at the time of the settlement. Gamble's request for additional medical benefits was denied by the employer because payment for the fracture was not part of the settlement. The Workers' Compensation Court held that the fracture was compensable, and the employer appealed, but the Supreme Court affirmed. If Gamble's fracture existed at the time of settlement, the parties were mutually mistaken regarding the material fact concerning the nature of Gamble's injury, requiring that the agreement be rescinded. The Supreme Court reviewed the findings and found that substantial credible evidence supported the facts that: (1) the fracture was consistent with and caused by the on-the-job injury; (2) Gamble's symptoms were consistent with the injury; (3) there was a basis for ruling out other potential causes of injury; and (4) there was an explanation as to why the injury was not diagnosed at the time of settlement. Because the mutual mistake of fact existed, the settlement agreement was properly rescinded. Gamble v. Sears, 2007 MT 131, 337 M 354, 160 P3d 537 (2007).

Contract Based Upon Mutual Mistake as to Workers' Compensation Law on Subrogation Rights of Insurer: Brown entered into a settlement agreement with the State Fund for $52,329.17, less $18,666.67 characterized as the "subrogation due the State Fund". Brown then pursued a third-party claim and settled for less than the policy limits. After the Supreme Court's decision in Zacher v. Am. Ins. Co., 243 M 226, 794 P2d 335 (1990), holding that an insurer is not entitled to subrogation unless the claimant is fully compensated for the injury, Brown sued to recover the money withheld by the State Fund. The Supreme Court held that Brown was entitled to rescind the agreement because the parties had made a mutual mistake as to state law that pertains to subrogation rights. However, the Supreme Court refused to award Brown the money retained by the State Fund on the basis that the whole agreement was void and that the lower court would have to determine the amount of money that Brown was entitled to receive. Brown v. Richard A. Murphy, Inc., 261 M 275, 862 P2d 406, 50 St. Rep. 1330 (1993).

Authority of Workers' Compensation Court to Reopen Final Compromise Settlement Agreement Based on Mutual Mistake: Settlement agreements for workers' compensation benefits, like other agreements, are subject to the law of contracts. A Montana court that is not otherwise limited by statute, including the Workers' Compensation Court, has the authority to set those contracts aside based upon a mutual mistake regarding the nature and extent of a claimant's injuries even when express language in the settlement agreement purports to prohibit setting the agreement aside. Wolfe v. Webb, 251 M 217, 824 P2d 240, 49 St. Rep. 1 (1992), distinguishing Bowen v. Anaconda Co., 220 M 185, 714 P2d 142 (1986), and Hutchinson v. Pierce Packing Co., 219 M 18, 710 P2d 64 (1985), and followed in Gamble v. Sears, 2007 MT 131, 337 M 354, 160 P3d 537 (2007).

Workers' Compensation Settlement — Lack of Foresight of Future Symptoms Not Basis for Rescission: Claimant entered a final settlement agreement on September 8, 1981, and on December 27, 1982, petitioned the Workers' Compensation Court for rescission of the agreement. The District Court rescinded the agreement and awarded permanent total disability benefits on the ground of mistake. The Supreme Court reversed and stated that a mistake justifying rescission must be a mistake made in unconscious ignorance of a past or present fact and that because speculation as to later symptoms is a conscious ignorance of future fact, an error of foresight cannot justify a finding of rescission for mistake. The Supreme Court found claimant's reported symptoms were not credible evidence of past or present disability or a change in disability and distinguished Kienas v. Peterson, 191 M 325, 624 P2d 1, 37 St. Rep. 1747 (1980), in which medical evidence became available later as to true extent of injury at time of settlement. Supreme Court also held that claimant did not suffer economic duress in freely accepting offer of settlement. Claimant must rely on statutory scheme of award modification despite fact that he entered into settlement only months before Supreme Court ruling making tender of value of an undisputed impairment rating mandatory. Claimant could not claim detrimental reliance on "good cause" clause in agreement when agreement was a standard form prepared by the Workers' Compensation Division and not the insurer. When there was no medical evidence in record that claimant's disability had changed, the Workers' Compensation Court was statutorily without power to reopen the settlement. Veterans' Administration (federal veterans') disability ratings are irrelevant under Montana workers' compensation laws. Hutchinson v. Pierce Packing Co., 219 M 18, 710 P2d 64, 42 St. Rep. 1810 (1985).

28-2-409. What constitutes mistake of fact.

Case Notes

No Posttrial Relief Based on Surprise or Mistake of Fact — Surprise Issue Not Preserved for Appeal — District Court Considered Best Available Information at Time of Trial: The uninsured employers' fund (UEF) breached a contract and the District Court awarded consequential damages to the prevailing party. Subsequently, UEF moved for posttrial relief on two grounds. First, UEF claimed the District Court should have set aside the judgment due to surprise because consequential damages were not sought in the complaint. Second, UEF claimed the District Court should have set aside the judgment based on a mistake of fact because the party that was awarded damages continued to keep a franchise despite a finding by the District Court that the franchise would be terminated. On appeal, the Supreme Court determined that UEF did not preserve the surprise defense based on a failure to object at trial and that the District Court did not make a mistake of fact since it relied on the best available information regarding the franchise at the time of trial. Elk Mtn. Motor Sports, Inc. v. Dept. of Labor and Industry, 2012 MT 261, 367 Mont. 36, 289 P.3d 165.

Incorrect Burden of Proof Imposed — Possibility of Reliance on Misdiagnosis Sufficient for Reversal and Remand: After suffering a workplace injury, Keller saw numerous health care providers in attempting to gain a correct diagnosis of her back pain. At least one of those providers raised the possibility of long thoracic nerve injury and scapular winging, although most of the providers diagnosed Keller's condition as occurring from another cause. Keller settled her case based upon the latter diagnoses but continued to see health care providers until several concluded that her pain was caused by long thoracic nerve injury. Keller attempted to open up the settlement agreements based upon mutual mistake but the Workers' Compensation Court refused, holding that Keller must show that the insurer had no knowledge that long thoracic nerve injury or scapular winging might be the cause of her pain. The Supreme Court reversed, holding that the Workers' Compensation Court imposed an incorrect burden of proof. Citing Weldele v. Medley Dev., 227 Mont. 257, 738 P.2d 1281 (1987), the Supreme Court held that since the evidence showed it was possible that the parties relied upon a misdiagnosis in settling the case, even though they knew of the existence of the possibility of different sources of Keller's pain, the imposition of the stricter burden of proof was sufficient error for remanding the case to the lower court because of a mistake of fact. Keller v. Liberty NW., Inc., 2010 MT 279, 358 Mont. 448, 246 P.3d 434.

Error in Rescinding Workers' Compensation Settlement Agreement Based on Mutual Mistake of Fact: In 2004, some 16 years after Kruzich suffered a traumatic brain injury in an industrial accident, Kruzich began developing signs of Parkinson's disease, which was determined was likely a result of the brain injury. Kruzich had entered a settlement agreement with the insurer in 1994 that expressly closed all present and future domiciliary care benefits while reserving medical and hospital benefits. When Parkinson's disease developed, Kruzich petitioned the Workers' Compensation Court to rescind the settlement agreement and reopen the claim, which the court did, on grounds that a material mutual mistake of fact had occurred regarding the nature of Kruzich's injuries. The insurer appealed, and the Supreme Court reversed. Under contract law, parties make a mutual mistake of fact only if they are unconsciously ignorant or forgetful of a fact that existed prior to or at the time of settlement, but ignorance of a future event does not constitute a mistake of fact. In this case, there was no evidence that at the time that the settlement agreement was executed, Kruzich suffered an injury of Parkinson's disease or that Kruzich would develop the disease 16 years later. The parties could not have been mutually mistaken about a fact that did not exist prior to or at the time of settlement, so the Workers' Compensation Court erred in reopening Kruzich's case based on mutual mistake of fact. Kruzich v. Old Republic Ins. Co., 2008 MT 205, 344 M 126, 188 P3d 983 (2008).

Validity of Voluntary Easement Affirmed: The Permanns requested that Urick grant an easement across Urick's property for the Permanns to go camping and move cattle, and Urick agreed. When Urick's sons discovered that the voluntary easement had been granted, they persuaded Urick to rescind the easement. Urick requested that the Permanns convey the easement back to her. They refused. Urick filed suit and then subsequently died. Urick's son Gliko, as trustee of Urick's estate, brought an action against the Permanns seeking to have the easement rescinded, citing mutual mistake, constructive fraud, undue influence, and lack of consideration. The District Court held that the easement was valid, and Gliko appealed. The Supreme Court considered each of Gliko's rescission arguments in turn. The language of the easement was simple and unambiguous, so there was no mutual mistake. Urick had testified by deposition that no misleading statements were made relating to the easement, so there was no constructive fraud. There was no confidential relationship between Urick and the Permanns, Urick was not possessed of weakness of mind, and no advantage was taken of Urick's necessities or distress, so there was no undue influence. Last, there was no evidence that consideration was meant to be given, so lack of consideration was not a valid ground for rescission. The District Court was affirmed. Gliko v. Permann, 2006 MT 30, 331 M 112, 130 P3d 155 (2006).

Public Contracts Subject to Fundamental Contract Analysis — Public Bidding and Contract Modification Statutes Not Inherently Inconsistent: Public contracts are not necessarily exempt from fundamental contract analysis because competitive bidding statutes were established for the benefit of the public rather than to establish the rights of bidders. Nothing in the competitive bidding statutes places public contracts out of reach of remedies at law or the equitable relief provided under 28-2-1611 if a party is otherwise qualified for relief under the terms of the statute. Further, public bidding statutes and contract modification statutes are not inherently inconsistent, so 28-2-1611 may be applied to public contracts. E.H. Oftedal & Sons, Inc. v. St., 2002 MT 1, 308 M 50, 40 P3d 349 (2002).

Unenforceability of Buy-Sell Agreement on Grounds of Impossibility or Impracticality of Performance — Requiring Performance of Contract With Potential for Environmental Degradation Unconstitutional: Cape-France Enterprises (Cape-France) entered a buy-sell agreement with Peed (now deceased) and Moore to purchase some property near Bozeman for a subdivision. Before the subdivision could be completed, water needed to be procured for the site. According to the agreement, as buyers, Peed and Moore were responsible to bring water to the property, but because city water was not available, a well needed to be drilled. However, the presence of a pollution plume was discovered near the land. After the subdivision process was commenced, the Department of Environmental Quality notified Cape-France that: (1) the plume may have advanced under the property; (2) a subdivision would not be approved unless a well was drilled and tested; (3) a well could be drilled, but if testing showed pollution in the water, treatment would be extensive; and (4) if drilling or pumping of the water caused expansion of the pollution, then Cape-France, as owner of the property, would be held liable for cleanup costs. On cross-motions for summary judgment, the District Court held that the buy-sell agreement could be rescinded on the basis of mutual mistake of fact and impossibility or impracticality of performance and that specific performance would not be granted. The Supreme Court affirmed. A court may determine that an act is impossible in legal contemplation when it is not practicable, when the act can be done only at an excessive, unreasonable, and unbargained-for cost. The doctrine of impossibility or impracticability is applied when, aside from the object of a contract being unlawful, the public policy underlying the strict performance of the contract is outweighed by the senselessness of requiring performance. The doctrine is not limited to cases of literal impossibility but may also be applied in cases that present a potential for substantial and unbargained-for damages. In this case, requiring Cape-France to go forward with the performance of the contract when there was a very real possibility of substantial environmental degradation and resultant financial liability for cleanup was not in the public interest or in the interests of the contracting parties and was not in accord with the guarantee of a clean and healthful environment in Art. II, sec. 3, Mont. Const., or the mandate to maintain and improve a clean and healthful environment for present and future generations in Art. IX, sec. 1, Mont. Const. Thus, rescission of the contract was proper. Cape-France Enterprises v. Estate of Peed, 2001 MT 139, 305 M 513, 29 P3d 1011 (2001). See also Smith v. Zepp, 173 M 358, 567 P2d 923 (1977), and Mont. Envtl. Information Center v. Dept. of Environmental Quality, 1999 MT 248, 296 M 207, 988 P2d 1236 (1999).

Defaulting Buyer Under Unambiguous Written Contract Cannot Rely Upon Expectations Not Covered by Contract to Avoid Contract — Disposition of Downpayment Amounts Paid and Due — County Not Liable for Negligent Misrepresentation as to Recordability of Deeds and Seller's Title Insurer Not Liable for Loss in Marketability: Documents for the sale and purchase of two sections of land unambiguously showed, and it was undisputed, that the resale of 20-acre parcels by the buyer, the immediate acceptance by the county of 20-acre resale deeds of a type that would make subdivision review unnecessary, and the ability to resell without having to undergo subdivision review were not parts of the bargain. The parties knew that these things were contemplated, but the documents did not refer to them or make them a part of the contract. Before the contract was made, the county indicated that it would accept the 20-acre resale deeds. The deal fell through when the county changed its position after the contract was signed. The buyer failed to pay the whole downpayment, and the seller terminated the contract and kept the paid portion of the downpayment. Precontract discussions on the matter must be disregarded as parol evidence because the documents were unambiguous and did not refer to the matter. The buyer was not entitled to rescind the contract and have the paid portion of the downpayment returned based on mutual mistake or failure of consideration. There was no mutual mistake because the parties knew that it was not a certainty that the county would accept the deeds. There was no failure of consideration because the resale, county acceptance of the deeds, and avoidance of subdivision review were not part of the written contract. In addition, the need for a subdivision review would not make the land unmarketable; at most, its market value decreased and it would take longer to sell it. Furthermore, a party in default is not entitled to rescission. The seller was entitled to terminate the contract. The seller was also entitled to keep an amount of the paid portion of the downpayment equal to the amount by which the contract price for the land exceeded the market value of the land at the time of the breach. The seller was not entitled to keep the remainder of the paid portion of the downpayment or to a judgment for the unpaid portion of the downpayment because the contract did not provide for that remedy. The county was not liable in tort to the seller for negligent misrepresentation, and the buyer's title insurance company was not liable to the seller for the loss in the marketability of the land caused by the need for subdivision review. Yellowstone II Dev. Group, Inc. v. First Am. Title Ins. Co., 2001 MT 41, 304 M 223, 20 P3d 755 (2001), overruled in Mary J. Baker Revocable Trust v. Cenex Harvest St., Cooperatives, Inc., 2007 MT 159, 338 M 41, 164 P3d 851 (2007), to the extent that Yellowstone II held that the determination of whether a term in a contract is ambiguous is not a question involving parol evidence.

Authority of Workers' Compensation Court to Reopen Final Compromise Settlement Agreement Based on Mutual Mistake: Settlement agreements for workers' compensation benefits, like other agreements, are subject to the law of contracts. A Montana court that is not otherwise limited by statute, including the Workers' Compensation Court, has the authority to set those contracts aside based upon a mutual mistake regarding the nature and extent of a claimant's injuries even when express language in the settlement agreement purports to prohibit setting the agreement aside. Wolfe v. Webb, 251 M 217, 824 P2d 240, 49 St. Rep. 1 (1992), distinguishing Bowen v. Anaconda Co., 220 M 185, 714 P2d 142 (1986), and Hutchinson v. Pierce Packing Co., 219 M 18, 710 P2d 64 (1985).

Reopening Workers' Compensation Settlement for Mutual Mistake — Statute of Limitations: Workers' compensation claimant was held to have discovered in October 1986 that back surgery was a possibility when at that time his doctor discussed with claimant the possibility of surgery and advised claimant to consider it. Furthermore, in that month, claimant's attorney for a social security disability claim notified the administrative law judge of the doctor's conclusion, and the judge's decision in claimant's favor was based in part on a possibility of surgery. Therefore, the 2-year statute of limitations for a claim based on mutual mistake (assuming that there was one) expired in October 1988 because a full and final compromise settlement approved by the Workers' Compensation Court was made without knowledge that surgery might well be necessary. The claim was barred because claimant's petition to reopen the compromise settlement was filed in July 1990. Rath v. St. Labre Indian School, 249 M 433, 816 P2d 1061, 48 St. Rep. 758 (1991).

No Mutual Mistake in Workers' Compensation Settlement: Claimant sought to have his workers' compensation settlement reopened on grounds of mutual mistake. The Supreme Court affirmed the District Court's denial of the request after finding: (1) claimant was capable of understanding the terms of the settlement agreement; (2) although claimant may have experienced an increased level of pain, there was no evidence to indicate the parties were mutually mistaken about the condition of claimant's back at the time of settlement; (3) there was no evidence to link claimant's personality disorder to his back injury; and (4) the claim was barred by the statute of limitations. Whitcher v. Pac. Employers Ins. Co., 236 M 289, 769 P2d 1215, 46 St. Rep. 367 (1989). See also Giles v. Bozeman Pub. Schools, 257 M 289, 849 P2d 180, 50 St. Rep. 273 (1993).

Ignorance of Contract Contents Not Grounds for Relief From Liability: One who executes a written contract is presumed to know its contents and to assent to them. Ignorance of the contents is not grounds for relief from liability. Johnson v. Estate of Shelton, 232 M 85, 754 P2d 828, 45 St. Rep. 887 (1988), citing Quinn v. Briggs, 172 M 468, 565 P2d 297 (1977).

No Mistake as to Subdivisibility of Land: Buyer breached a buy-sell agreement, claiming there was a mutual mistake of fact as to the subdivisibility of certain real property covered by the contract. The court found there was not mistake of fact because the buyer has not proven the land cannot be subdivided. The buyer was an experienced businessman who was aware of certain obstacles to subdividing the land when he executed the buy-sell agreement. He was under a duty to execute the agreement with the prudence and care of a reasonable, cautious businessman. Hillstrom v. O'Neil, 226 M 452, 736 P2d 126, 44 St. Rep. 795 (1987).

Mutual Mistake Regarding Zoning Ordinance — Rescission Proper: When both parties believed, at the time a contract for deed was executed, that a business was in compliance with a zoning ordinance but the business was later found not to comply, it constituted a mutual mistake of fact under 28-2-409 and rescission was therefore proper under 28-2-1711. Carey v. Wallner, 223 M 260, 725 P2d 557, 43 St. Rep. 1706 (1986), affirmed, 229 M 57, 744 P2d 881, 44 St. Rep. 1778 (1987), and followed in Mitchell v. Boyer, 237 M 434, 774 P2d 384, 46 St. Rep. 928 (1989).

Res Judicata Inapplicable — Issues Not Same: Plaintiff suffered a back injury in October 1980, underwent surgery, and was judged to have reached a stationary state. Plaintiff was given an impairment rating of 25% and in August 1981 entered a final settlement for 125 weeks of permanent and partial disability benefits. In June 1981, while employed by a different employer, plaintiff experienced a sexual incident which she characterized as a sexual assault. In September 1981, while employed by a third employer, plaintiff suffered an industrial accident. In March 1984, the Workers' Compensation Court determined that the sexual incident did not constitute a compensable injury and that plaintiff as of that date was entitled to temporary total disability benefits by reason of the September 1981 injury. The benefits were to continue until the disability ceased. In October 1984, plaintiff sought to have the settlement entered in August 1981 set aside, claiming mutual mistake of fact. The Workers' Compensation Court held that its March 1984 decision barred this issue as res judicata. On appeal, the Supreme Court held that the issues were not identical so that res judicata was inapplicable. In the first case, the question was basically one of amount. In the second case, the question went to the validity of the settlement itself. The mistake plaintiff alleged was her total disability by reason of the second industrial accident. No ruling in the first case addressed whether the settlement had to be reopened in light of the Supreme Court's decision in Holton v. F.H. Stoltze Land & Lumber Co., 195 M 263, 637 P2d 10, 38 St. Rep. 1835 (1981). The court also noted that the question of mutual mistake of fact could not have been raised in the first case. The case was reversed and remanded with directions to hear the petition on its merits. Phelan v. St. Paul Mercury Ins. Co. 220 M 296, 716 P2d 601, 43 St. Rep. 381 (1986).

Workers' Compensation Settlement — Lack of Foresight of Future Symptoms Not Basis for Rescission: Claimant entered a final settlement agreement on September 8, 1981, and on December 27, 1982, petitioned the Workers' Compensation Court for rescission of the agreement. The District Court rescinded the agreement and awarded permanent total disability benefits on the ground of mistake. The Supreme Court reversed and stated that a mistake justifying rescission must be a mistake made in unconscious ignorance of a past or present fact and that because speculation as to later symptoms is a conscious ignorance of future fact, an error of foresight cannot justify a finding of rescission for mistake. The Supreme Court found claimant's reported symptoms were not credible evidence of past or present disability or a change in disability and distinguished Kienas v. Peterson, 191 M 325, 624 P2d 1, 37 St. Rep. 1747 (1980), in which medical evidence became available later as to true extent of injury at time of settlement. Supreme Court also held that claimant did not suffer economic duress in freely accepting offer of settlement. Claimant must rely on statutory scheme of award modification despite fact that he entered into settlement only months before Supreme Court ruling making tender of value of an undisputed impairment rating mandatory. Claimant could not claim detrimental reliance on "good cause" clause in agreement when agreement was a standard form prepared by the Workers' Compensation Division and not the insurer. When there was no medical evidence in record that claimant's disability had changed, the Workers' Compensation Court was statutorily without power to reopen the settlement. Veterans' Administration (federal veterans') disability ratings are irrelevant under Montana workers' compensation laws. Hutchinson v. Pierce Packing Co., 219 M 18, 710 P2d 64, 42 St. Rep. 1810 (1985).

Purchase Money Mortgages — Reformation: The bank prepared a mortgage from the buyer to the sellers and a deed of trust from the buyer to the bank as a service to and at the request of the buyer and the sellers. The bank inadvertently inserted the term "no exceptions" into the mortgage through a typographical error. Upon default of the buyer, the sellers filed an action for declaratory ruling that their purchase money mortgage was prior in time and right to the bank's deed of trust. The trial court reformed the sellers' mortgage to delete the term "no exceptions" and held that the bank's deed of trust was prior in time and right to the mortgage. The Supreme Court affirmed. The bank's mistake, while negligent, did not amount to neglect of a legal duty that would preclude reformation. The mistake was mutual because the mortgage as written did not reflect the mutual intentions of the parties which, the evidence indicated, were for the bank to receive a first mortgage and the sellers to receive a second mortgage. Pulse v. N. Am. Land Title Co. of Mont., 218 M 275, 707 P2d 1105, 42 St. Rep. 1578 (1985).

No Mutual Mistake of Fact — Insurance Compromise Settlement: The Workers' Compensation Court concluded that claimant had testified that his back was in much the same condition in 1982 as it had been on the date of his insurance compromise settlement in 1979. Accordingly, the parties to the settlement were not laboring under a mutual mistake of fact as to the nature and extent of injuries when they entered into a full and final compromise. This case was distinguished from Kienas v. Peterson, 191 M 325, 624 P2d 1, 37 St. Rep. 1747 (1980), in which it was held that the lack of knowledge that the industrial accident possibly aggravated preexisting cerebral palsy, leading to a worsening condition, was a mutual mistake of fact. The court reiterated in this instant case that 39-71-204 and 39-71-2908 (now repealed) preclude reopening of workers' compensation settlements. Sollie v. Travelers Indem. Co., 212 M 197, 686 P2d 920, 41 St. Rep. 1684 (1984).

Contract Not Voidable for Mistake: A party to a contract who did not read the contract carefully and who did not understand it is bound by the contract nonetheless when there has been no misrepresentation and no ambiguity in the terms of the contract, and where the other party acts in good faith and has no notice of the first party's mistake. Robertson v. Hughes, 204 M 515, 668 P2d 1025, 40 St. Rep. 1041 (1983).

Mutual Mistake to Defeat Object of Contract: Plaintiffs and defendant entered an agreement whereby defendant would lease condominiums from the plaintiffs and would sell plaintiffs her home. The lease of one of the condominiums contained an option for defendant to purchase the unit by forgiving plaintiffs their obligation under the promissory note on the home. Plaintiffs discovered that the floors in the home sloped north at a rate of 5½ inches over 30 feet. Plaintiffs sought to rescind the contract, and defendant sought specific performance. Plaintiffs contended mutual mistake in the making of the contract. The District Court found that the object of the contract was to furnish plaintiffs with a home to live in. This purpose was not frustrated by the unlevel condition, as defendant's family had lived in the house for 10 years. In order for mutual mistake to warrant rescission of a contract, the mistake must be so substantial and fundamental as to defeat the object of the parties in making the contract. Here, the mistake did not affect the object of the parties and rescission did not lie. Woodahl v. Matthews, 196 M 445, 639 P2d 1165, 39 St. Rep. 238 (1982), followed in Van Hook v. Baum, 245 M 407, 800 P2d 151, 47 St. Rep. 1883 (1990). See also Halcro v. Moon, 226 M 121, 733 P2d 1305, 44 St. Rep. 504 (1987).

Mutual Mistake — Basis for Rescission: Defendants purchased an irregular tract of land and commenced construction of a commercial building. They were contacted by plaintiff concerning purchase of the building. They consulted an attorney and discussed condominiumizing the building. He suggested as a tax matter that defendant should hold the property long enough to qualify for long-term capital gain treatment. An option to purchase with contract for deed was entered. The deeds and contract were not completed, as a survey was needed for a legal description of the property. The contract contained a provision that defendants provide and pave parking lots north and south of the building. The survey was completed and showed that the building encroached on state and county rights-of-way to the north and south. Plaintiffs then sought to rescind the contract and recover their money. The Supreme Court held that the providing of parking lots was material to the contract and that mutual mistake of fact as to the parking lots was an adequate basis for rescinding the contract. It also held that any findings not made could be implied to support the trial court's decision. Berry v. Romain, 194 M 400, 632 P2d 1127, 38 St. Rep. 1434 (1981).

Reliance on Trustee — Creation of Corporation: Plaintiff's husband and defendant were brothers and partners in a ranching operation, although each owned the land individually. Plaintiff's husband died and defendant was named executor. A corporation was formed to operate the ranch on May 1, 1973. Both parties transferred all assets to the corporation. Defendant's family got 364 more shares than plaintiff, and defendant was named president of the corporation. Restrictions were placed on the valuation and transfer of stock. On May 29, 1975, plaintiff consulted her own attorney and for the first time fully realized her position. All corporate votes became deadlocked. On April 29, 1977, plaintiff filed suit to dissolve the corporation, alleging fraud and oppressive conduct by defendant and mistake at the formation. The court found that defendant occupied a position of trust and confidence in relation to plaintiff. He was executor of her husband's estate and partner to her husband at the date of death; that status imposed on defendant the duties of a trustee. At the time of incorporation, the unequal stock division was not believed to be of any particular legal or practical significance, so that the parties were mistaken as to legal effect. Defendant claimed no mistake could be claimed because plaintiff failed in her duty to fully read the documents before signing. However, the duty was not so much on plaintiff to discover as on defendant as trustee to fully disclose. In view of the fact that no disclosure was made, the mistake under which the parties were acting was evident. Skierka v. Skierka Bros., Inc., 192 M 505, 629 P2d 214, 38 St. Rep. 754 (1981).

Finality of Workers' Compensation Decision — Grounds for Overturning: A full and final compromise settlement agreement between an injured worker and the Workers' Compensation State Fund was set aside because of mutual mistake of material fact by both parties. Kienas v. Peterson, 191 M 325, 624 P2d 1, 37 St. Rep. 1747 (1980), distinguished in Sollie v. Travelers Indem. Co., 212 M 197, 686 P2d 920, 41 St. Rep. 1684 (1984). A petition for rehearing was filed. The Supreme Court reaffirmed the decision. The petitioner argued the Workers' Compensation Court had no power to alter or rescind the agreement 4 years after its execution. The Supreme Court pointed out that it, not the Workers' Compensation Court, set aside the agreement. It noted the scope of its appellate power and also the code provision on lack of consent through mutual mistake of material fact. The Supreme Court was not broadening the possibilities of reopening such settlements; it merely found that no contract existed initially. Kienas v. Peterson, 38 St. Rep. 320 (1981) (apparently not reported in Montana Reports or Pacific 2d Reporter).

Workers' Compensation Settlement — Mutual Mistake: Plaintiff injured his back when he fell in the restaurant where he worked and a rack of dishes fell on him. He submitted his claim to the Workers' Compensation Division but was not represented by an attorney. He was examined by physicians who found him to be 5% disabled. Plaintiff entered into a full and final compromise settlement. Later examinations by physicians showed that plaintiff's fall had aggravated his preexisting cerebral palsy condition. This information was not available to either party at the time the settlement was entered into. Both parties were mistaken as to a fact material to the contract. The court found that the need to fairly compensate the injured worker is the intent and purpose of the Workers' Compensation Act. The full and final compromise settlement was set aside for mutual mistake of a material fact as to the nature and extent of the injury caused by claimant's accident. The case was remanded to the Workers' Compensation Court to determine the extent of claimant's disability. Kienas v. Peterson, 191 M 325, 624 P2d 1, 37 St. Rep. 1747 (1980), followed in Kimes v. Pac. Employers Ins. Co., 233 M 175, 759 P2d 986, 45 St. Rep. 1402 (1988), Weldele v. Medley Dev., 227 M 257, 738 P2d 1281, 44 St. Rep. 1062 (1987), and Keller v. Liberty NW., Inc., 2010 MT 279, 358 Mont. 448, 246 P.3d 434.

Rescission of Sale Agreement: In an action for rescission of a contract, plaintiff was under a legal duty to execute the sale agreement with the prudence and care of a reasonable and cautious businessman. When the evidence showed a failure to exercise such care, plaintiff could not obtain relief from a court of equity on the ground of unilateral mistake of fact. Quinn v. Briggs, 172 M 468, 565 P2d 297 (1977), followed in Silva v. McGuinness, 189 M 252, 615 P2d 879, 37 St. Rep. 1401 (1980).

Reformation of Instruments Because of Mistakes: Before equity will intervene to correct an alleged mutual mistake in a written instrument, the evidence of the mistake must be clear, convincing, and satisfactory. Humble v. St. John, 72 M 519, 234 P 475 (1925).

Failure to Read Instrument:

The complaint alleged that plaintiff had agreed to sell and defendant to buy a parcel of land and that plaintiff had accurately described the land to an attorney who undertook to reduce the terms of the agreement to writing. It further alleged that in doing so the attorney included more land than was intended to be conveyed and that, relying upon and having confidence in the attorney's integrity and ability, plaintiff failed to observe the inaccuracy, as did also the defendant, or made no mention of it if observing it. The contract was completed in this faulty condition. The complaint was sufficient to state a case for reformation on the ground of mutual mistake of the parties. Cox v. Hall, 54 M 154, 168 P 519 (1917).

One is guilty of negligence in failing to read a promissory note before signing it. Parchen v. Chessman, 49 M 326, 142 P 631 (1914), distinguished in Comerford v. USF&G Co., 59 M 243, 196 P 984 (1921).

Where the parties entrust the duty of formulating a writing embodying their agreement to an attorney or scrivener, and he, by his own mistake or fraud, embodies in it stipulations and conditions other than those agreed upon, the party against whom it is sought to be enforced may have it reformed, though it was signed by him and delivered to the other party, without reading. Parchen v. Chessman, 49 M 326, 142 P 631 (1914), overruling Hennessy v. Holmes, 46 M 89, 125 P 132 (1912).

28-2-410. What constitutes mistake of law.

Case Notes

No Unilateral Mistake of Law if Other Party Unaware of Misapprehension: The claimant argued that he had entered into the settlement believing that he was not entitled to receive benefits after age 65. The Supreme Court ruled that there can be no relief for a unilateral mistake of law unless it can be shown that the other party knew of the misapprehension. Hartfield v. St. Comp. Ins. Fund, 246 M 259, 805 P2d 1293, 47 St. Rep. 2001 (1990).

Rescission of Sale Agreement: A misunderstanding by the plaintiff of tax consequences attendant to a sale agreement is not ground for rescission as a mistake of law when the other party is not aware of or under the same misapprehension. Quinn v. Briggs, 172 M 468, 565 P2d 297 (1977).

Bank Unlawfully Pledging Note to County: Prior to amendment of the National Banking Act of 1930, national banks were prohibited from pledging any of their assets to secure deposits; hence, where in 1924, a depositor executed his note to a bank which unlawfully pledged it to a county as security for its funds then on deposit in the bank, which soon thereafter became insolvent, the county was without right to enforce payment of the note because it was not the owner or rightful holder thereof. The receiver's sending the dividend check for funds of the depositor to the County Treasurer was immaterial because it was a mistake. McFarland v. Stillwater County, 109 M 544, 98 P2d 321 (1940).

Justification of Mistake: The complaint of a County Surveyor in an action to recover from the county the difference between $7 and $8 per day compensation during 4 years of service, on the ground that owing to the mutual mistake of himself and the Board of County Commissioners he was allowed and accepted the smaller amount whereas under the law he was entitled to the larger one, stated a cause of action (as against the assertion that mistake of what the law allowed him was not a proper basis for relief), it being apparent from an inspection of various statutes relating to the compensation of the County Surveyor that there was ample justification for laymen, such as plaintiff and the Board, to fall into the mutual mistake as to the amount he was entitled by law to receive. Hicks v. Stillwater County, 84 M 38, 274 P 296 (1929).

Affecting Contract Obligations: Every person is charged with knowledge of the law, and generally speaking a mistake of law is not an adequate ground for relieving one from a contract obligation, more especially so where the mistake was not mutual, but the party relying thereon not only knew of his legal rights and asserted them, but nevertheless agreed to monthly settlements for several years, constituting accounts stated, accepting less than he was legally entitled to; under such conditions he may not thereafter be permitted to surcharge the accounts and recover the difference. Norum v. Ohio Oil Co., 83 M 353, 272 P 534 (1928).

Sufficiency of Complaint Based on Mistake of Law:

Where a fraud is alleged in the alternative in an action or the reformation of one and the cancellation of another instrument because executed under the influence of mutual mistake, it does not render the plea of mutual mistake ineffective. Brundy v. Canby, 50 M 454, 148 P 315 (1915).

Where plaintiff in a suit to recover an overpayment made on a repurchase of property sold under foreclosure, under a mistake of law, induced by defendant, alleges a cause of action under subsection (2) of this section, and the proof adduced brings it within subsection (1), there is a fatal variance, and recovery cannot be had by reason of a mistake of law. Bottego v. Carroll, 31 M 122, 77 P 430 (1904). See Brundy v. Canby, 50 M 454, 148 P 315 (1915).

28-2-411. Mistake of foreign laws — mistake of fact.

Case Notes

Nonresident Seeking Foreclosure in Montana: The rule that mistakes of foreign law are mistakes of fact was not available to nonresident bringing foreclosure proceedings in Montana through a local attorney where the nonresident failed to advise attorney of a payment that kept the debt alive in the belief the law here was the same as in his state, and attorney entered into an agreed statement of facts upon the trial of which the court found that the debt was outlawed. Rieckhoff v. Woodhull, 106 M 22, 75 P2d 56 (1937).

Part 5
Communication of Consent — Revocation of Proposal

Part Case Notes

Blank Security Agreement Signed by Borrower and Filled Out by Bank: Borrower signed a blank security agreement that bank then filled out and mailed to her. The record shows that she had the agreement in her possession in December 1985; thus, she had the means to discover the fraud that she alleged bank committed in setting the agreement's terms. Because she did not file a claim until December 1988, her claim was barred by the 2-year statute of limitations. Richland Nat'l Bank & Trust v. Swenson, 249 M 410, 816 P2d 1045, 48 St. Rep. 730 (1991).

Valid Release of Insurance Claims as Binding: Plaintiff injured in an automobile accident received $4,362.85 for medical expenses, lost wages, car rental costs, headaches, and inconvenience. In return for the settlement payments, the adjuster obtained a general liability release discharging the insurance company "from all claims, demands, damages, actions, causes of action or suits of any kind or nature whatsoever . . . [for] all injuries, known or unknown". Plaintiff sent a thank you note to the adjuster to express her pleasure with the "settlement and prompt service" but also retained an attorney on the case who attempted to obtain rescission of the release after receiving a copy of plaintiff's medical report. Rescission was denied upon a finding that plaintiff executed a valid release of all claims and that the terms of the agreement and release were clear and unambiguous. Plaintiff was bound by the settlement terms. Hanson v. Oljar, 231 M 272, 752 P2d 187, 45 St. Rep. 602 (1988), followed in Hetherington v. Ford Motor Co., 257 M 395, 849 P2d 1039, 50 St. Rep. 325 (1993), which was distinguished in Murphy v. The Home Depot, 2012 MT 23, 364 Mont. 27, 270 P.3d 72.

28-2-501. How consent is communicated.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Letters of Offer and Acceptance on Real Property Sale Exchanged — Terms of Response Immaterial — Contract for Sale Enforced by Specific Performance: Two sisters owned 78 acres as tenants in common. The defendant sister, who held a majority interest, sent a letter to the plaintiff sister, offering to sell her the majority interest or to purchase the minority interest. The letter set a deadline for a response and requested it be sent to a specified third party. Before the deadline expired, the plaintiff sister wrote back directly to her sister and agreed to purchase the majority interest. However, the defendant sister claimed she had decided to sell the property to their brother. The plaintiff sister sued, seeking specific performance of the contract. The defendant sister argued that the plaintiff had not accepted the original offer because she had not responded to the third party as requested. The District Court concluded that, as phrased in the letter, the request to direct the response to the third party was not a condition precedent to acceptance. On appeal, the Supreme Court agreed that the letters exchanged by the sisters formed a contract and that the mode of acceptance was not a condition precedent. The court affirmed the District Court's grant of specific performance ordering the defendant sister to sell her majority interest to the plaintiff. Olsen v. Johnston, 2013 MT 25, 368 Mont. 347, 301 P.3d 791.

Acceptance of Performance — Contract Established: In a construction contract dispute, substantial credible evidence supported the District Court's conclusion that the general contractor accepted the subcontractor's offer although the general contractor crossed out portions of the offer and added additional language. The general contractor's representative signed the offer, and the general contractor, who controlled access to the site, allowed the subcontractor to begin work without any other agreement in place. Assuming the general contractor's interlineations created a counteroffer, a meeting of the minds occurred when the subcontractor started performing its contractual obligations. AAA Constr. of Missoula, LLC v. Choice Land Corp., 2011 MT 262, 362 Mont. 264, 264 P.3d 709.

Attorney's Agreement to Settle Disputed Claim Binding Client Despite Attorney's Receipt of Funds or Filing With District Court — Estate of Goick Overruled: Following protracted litigation, the parties' attorneys agreed by telephone to settle a disputed claim, specifying a dollar amount and the preparation of a general release. Defendant's counsel prepared and faxed a release to plaintiff's counsel, who in turn replied by letter that the settlement terms were accepted. Defendant's counsel then prepared and signed a stipulation to dismiss the action and ordered a settlement check. About 2 weeks later, plaintiff's counsel advised that plaintiff refused to settle. Defendant's counsel moved to compel settlement, and the District Court granted the motion on the basis that plaintiff had agreed to the terms of the settlement. Plaintiff appealed, arguing that the settlement statement was only an attempt by counsel to reach an agreement that would then be forwarded to plaintiff for final agreement. However, plaintiff presented no evidence that counsel was not authorized to enter a settlement. Plaintiff also relied on 37-61-401(1) and on In re Estate of Goick, 275 M 13, 909 P2d 1165 (1996), for the proposition that he was not bound by the settlement because the agreement was not filed with the Clerk of Court or entered in the court's minutes. The Supreme Court affirmed. The literal interpretation of 37-61-401(1)(a) in Goick was inconsistent with prior case law and would preclude an attorney from binding a client to a settlement agreement, although 37-61-401(1)(b) would allow an attorney to discharge a claim or acknowledge satisfaction of judgment once the attorney received money. Precluding an attorney from binding a client to a settlement unless the attorney received funds does not make sense and is an absurd result. The Supreme Court therefore overruled that portion of Goick stating that a client is not bound to a settlement agreement unless the agreement is filed with the District Court or entered in the court's minutes. Lockhead v. Weinstein, 2003 MT 360, 319 M 62, 81 P3d 1284 (2003), following Hetherington v. Ford Motor Co., 257 M 395, 849 P2d 1039 (1993), which was distinguished in Murphy v. The Home Depot, 2012 MT 23, 364 Mont. 27, 270 P.3d 72.

Silence as Grounds for Estopping Party From Denying Existence of Contract: A manufacturing company received a government contract to produce combat helmets. Farmers State Bank supplied a letter to the Department of Defense stating that Farmers Bank and First National Bank of Missoula would provide the necessary financing. Neither bank provided funds, and the company sued under tort and contract law. The Supreme Court found that Farmers Bank was not an agent of First National solely on the basis of statements made by Farmers Bank in its letter to the Department of Defense. The court also held that First National's silence in not denying that it agreed to finance the company did not amount to a representation or concealment of material facts estopping it from claiming that there was no agreement on its part to fund the project. NW. Polymeric, Inc. v. Farmers St. Bank, 236 M 175, 768 P2d 873, 46 St. Rep. 275 (1989).

Obligation to Refund Payment for Gas Field Option: Plaintiff corporation rescinded a gas field option upon which it had paid $50,000 to defendant. After defendant failed to refund money due, plaintiff filed suit and was granted summary judgment for $71,320.55. On appeal, the Supreme Court held that, based upon the exhibits, affidavits, and briefs before the lower court, there was no evidence of a genuine issue of material fact. The escrow agreement and release based upon plaintiff's rescission were supported by adequate consideration since release from contract obligations and forbearance to sue are both adequate consideration. Ayers Oil and Gas, Inc., was a party to both the option and the release agreements as evidenced by Ayers' signature as president. Devon Oil & Gas Co., Inc. v. Ayers, 218 M 223, 707 P2d 523, 42 St. Rep. 1536 (1985).

Oral Contract for Purchase of House — Part Performance — Statute of Frauds Inapplicable — No Refund to Purchasers on Default: Defendant agreed to sell home to friends upon a $10,000 downpayment and assumption of defendant's loan. Plaintiffs did not qualify for assumption, so defendant prepared lease for plaintiffs' signature. They refused to sign because it was not a contract for deed. Defendant allowed plaintiffs to take occupancy, and they made sporadic payments for 4 years. Defendant's patience waned when the bank exercised acceleration provision for delinquencies. Plaintiffs sued for refund of payments. The court found an oral contract for deed. The Statute of Frauds was inapplicable because defendant was, at all times, willing to effect sale and transfer of the home. He was not required to refund plaintiffs' payments. Since no lease was ever signed and no rental relationship created, landlord and tenant law was inapplicable. Hayes v. Hartelius, 215 M 391, 697 P2d 1349, 42 St. Rep. 457 (1985).

Offer Followed by Suggested Changes, Passage of Time, and Acceptance: Following oral modification of written lease to allow lessee to use additional space for additional rent, lessor sent lessee a new lease that incorporated the modification and was essentially the same as the current lease. Lessee's attorney suggested changes not accepted by lessor. Lessor did not revoke his offer of the new lease, and a few months later lessee told lessor on the phone that her attorney's changes were not important to her and she would sign and deliver the lease, which she did the next month. The attorney's suggested changes were not a rejection, the time between the suggestions and the delivery of the signed lease by lessee was not unreasonable under the circumstances and did not work a revocation of the offer of the new lease, and the new lease was executed when lessee signed and delivered it. Lemley v. Allen, 203 M 37, 659 P2d 262, 40 St. Rep. 279 (1983).

28-2-502. When consent is considered fully communicated.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

28-2-503. Implied acceptance.

Case Notes

Acceptance of Performance — Contract Established: In a construction contract dispute, substantial credible evidence supported the District Court's conclusion that the general contractor accepted the subcontractor's offer although the general contractor crossed out portions of the offer and added additional language. The general contractor's representative signed the offer, and the general contractor, who controlled access to the site, allowed the subcontractor to begin work without any other agreement in place. Assuming the general contractor's interlineations created a counteroffer, a meeting of the minds occurred when the subcontractor started performing its contractual obligations. AAA Constr. of Missoula, LLC v. Choice Land Corp., 2011 MT 262, 362 Mont. 264, 264 P.3d 709.

No Error in Finding of No Unjust Enrichment: Plaintiff contended that defendant company was unjustly enriched when a promissory note was unilaterally entered into by one of the owners of defendant business without the knowledge or authorization of the other owners. The District Court held that the company was not unjustly enriched, and on appeal the Supreme Court affirmed. The company had no knowledge of the speculative transaction between plaintiff and the owner until shortly before suit was filed, so plaintiff could show no misconduct or fault on the company's part, nor was the owner authorized to engage in entering promissory notes on the company's behalf. Thus, the District Court did not err in holding that the company was not unjustly enriched. Estate of Pruyn v. Axmen Propane, Inc., 2009 MT 448, 354 M 208, 223 P3d 845 (2009). See also Maxted v. Barrett, 198 M 81, 643 P2d 1161 (1982).

City Resolution Allowing Implied Consent to Annexation Upon Continued Use of Utility Services Affirmed: The city of Whitefish adopted a municipal resolution requiring that property owners consent to annexation in order to continue to receive city utility services and allowing the city to imply consent to annexation from property owners that continued to receive the services after they received notice requiring them to disconnect from the utilities. Property owners contended that the resolution was invalid, but the District Court held the resolution valid, and the Supreme Court affirmed. The Attorney General held in 46 A.G. Op. 12 (1995), that a municipality may establish a rule requiring consent to annexation as a condition for continued receipt of services, and that opinion is in accord with 69-7-201. Further, the utility rule in this case put the burden on the property owner to arrange to disconnect from services if protesting annexation, so once proper notice was given, under 7-2-4710 and this section, the city's procedure to imply consent was a proper method to determine if a property owner wished to continue to receive city services or to protest annexation. Gregg v. Whitefish City Council, 2004 MT 262, 323 M 109, 99 P3d 151 (2004).

No Meeting of Minds Concerning Stock Transfer: Wife offered to convey shares of stock to husband to satisfy a dissolution judgment, but husband did not accept her offer; he merely agreed to consider it. Husband subsequently rejected wife's offer because of negative tax consequences associated with the transfer. There can be no binding contract without the mutual consent of the parties, and consent is established if there has been an offer and an acceptance of that offer. In re Marriage of Dalley, 237 M 287, 773 P2d 295, 46 St. Rep. 808 (1989).

Oral Contract for Purchase of House — Part Performance — Statute of Frauds Inapplicable — No Refund to Purchasers on Default: Defendant agreed to sell home to friends upon a $10,000 downpayment and assumption of defendant's loan. Plaintiffs did not qualify for assumption, so defendant prepared lease for plaintiffs' signature. They refused to sign because it was not a contract for deed. Defendant allowed plaintiffs to take occupancy, and they made sporadic payments for 4 years. Defendant's patience waned when the bank exercised acceleration provision for delinquencies. Plaintiffs sued for refund of payments. The court found an oral contract for deed. The Statute of Frauds was inapplicable because defendant was, at all times, willing to effect sale and transfer of the home. He was not required to refund plaintiffs' payments. Since no lease was ever signed and no rental relationship created, landlord and tenant law was inapplicable. Hayes v. Hartelius, 215 M 391, 697 P2d 1349, 42 St. Rep. 457 (1985).

No Implied Acceptance — Contract Governs: This section does not apply if the terms of a valid contract govern the transaction. Hence, city of Billings failed in its contention that Grays, by accepting benefits of subdivision improvement agreement and waiver of protest to creation of SID, are bound to the terms of the agreement by implied acceptance. If the terms of the agreement are disputed and no enforceable contract exists, the city's remedy lies in this section's quasi-contractual, restitutionary relief. "The theory of unjust enrichment and restitution is brought into play when no contract between the parties exists and the court implies a contract in law." (Maxted v. Barrett, 198 M 81, 643 P2d 1161 (1982).) Gray v. Billings, 213 M 6, 689 P2d 268, 41 St. Rep. 1910 (1984).

Obligations Arising Out of Lawful Contract Not to Be Repudiated: A contract between two interstate trucking firms under which the appellant was to provide workers' compensation coverage for his employees and agreed to save appellee's carrier harmless from any liability arising from any relationship between the appellant and his employees did not violate rules of the Interstate Commerce Commission, and appellee was entitled to be indemnified for an amount paid in settlement of a workers' compensation claim. Indus. Indem. Co. v. McIntosh, 185 M 158, 604 P2d 1233 (1980).

Estoppel by Acquiescence — Direct or Implied: If a party seeking reformation of a contract on the ground of mistake in its execution, after becoming aware of the mistake or the circumstances are such that he will be presumed to have known of it, acquiesces in the instrument, he loses his right to reformation; acquiescence may be implied from an unreasonable delay in applying for redress after getting notice of the mistake. Cook-Reynolds Co. v. Beyer, 107 M 1, 79 P2d 658 (1938).

Waiver of Fraud: Plaintiff, shortly after entering into a contract with defendant agreeing to trade his farm for that of the latter, discovered that he had been defrauded and gave notice of his intention to rescind, but continued in possession of the land acquired by him for nearly 14 months and for a period of 6 months after he commenced action for rescission. Plaintiff continued to use it as his own, paying an installment of taxes after knowledge of the fraud and 6 months after the deal assured defendant that he would attend to the payment of a mortgage assumed by him on the trade. Under these circumstances, plaintiff waived the fraud and ratified the contract by his conduct. Beebe v. James, 91 M 403, 8 P2d 803 (1932).

Notice of Facts: Under 28-10-604 plaintiff corporation must be deemed to have had notice of the facts known to its manager in entering into an agreement whereby its debtor was released from liabilities by his assignment for the benefit of creditors, and its voluntary acceptance of the benefits of the transaction was equivalent to a consent to it. Stone-Ordean-Wells Co. v. Anderson, 66 M 64, 212 P 853 (1923).

28-2-504. Acceptance to be absolute.

Case Notes

Acceptance of Sale of Real Property With New Terms, Including Foregoing Attorney Fees — Constituted Release: The husband had been ordered to pay his wife's attorney fees in the parties' divorce proceeding. After the divorce, the wife sought to purchase real estate in which the husband had an interest. The husband's attorney responded to the wife's offer with a letter containing several modifications to the wife's offer and also a request that the attorney fees owed by the husband be waived. The Supreme Court ruled that when the wife purchased the property pursuant to the modified terms, she also released the husband from paying the fees owed. The sale of the real estate was adequate consideration for the release. In re Marriage of Lyman, 240 M 336, 783 P2d 1362, 46 St. Rep. 2174 (1989).

Contract Part Oral, Part Written — Bid Not Contract — Parol Evidence Rule Inapplicable — Time of Essence by Oral Agreement: The plaintiff in a breach of contract case obtained a bid on a job building a basement. The defendant contractors on appeal argued: (1) that their bid constituted a contract and therefore the parol evidence rule barred testimony concerning a completion date not contained in the writing; and (2) time was not of the essence unless expressly provided in the writing. The Supreme Court said that the bid was an offer and that a purported acceptance which varied or added to the terms of the offer was not an acceptance but a counteroffer. The trial court's finding that the parties had agreed orally to a specific completion date was not clearly erroneous. The contract was partially written and partially oral. Because there was not a final, complete written document intended by the parties to contain all of the terms of the contract, the parol evidence rule did not apply. By agreeing to the completion date with the knowledge that the plaintiff considered the date essential because of approaching cold weather, the defendants agreed that time was of the essence. Therefore, the defendants were in substantial breach on the agreed date. Carriger v. Ballenger, 192 M 479, 628 P2d 1106, 38 St. Rep. 864 (1981), distinguishing Higby v. Hooper, 124 M 331, 221 P2d 1043 (1950).

Insurance Contract: Where a renewal policy was sent to an insured, the sending of policy constituted an offer and offer by insured to take the policy for as long as $10 would pay the premium was a new proposal, requiring acceptance by the insurer. Kudrna v. Great N. Ins. Co., 175 F. Supp. 783 (D.C. Mont. 1959).

Acceptance to Conform to Offer: To conclude an agreement the acceptance of the offer must be unconditional and must in every respect meet and correspond with the terms of the offer. State ex rel. Henderson v. Bd. of St. Prison Comm'rs, 37 M 378, 96 P 736 (1908), the principle being applied in this case to a contract with the Board of State Prison Commissioners for the care of inmates of the prison.

28-2-511. When proposal may be revoked.

Case Notes

Corporation Considered Real Party in Interest on Claim for Lost Corporate Profits — No Exception for S. Corporations: Gullett paid $10,000 earnest money for the purchase of real property. The money was drawn on the account of Gullett's corporation. When defendants refused to return the money after the purchase agreement failed, Gullett filed a complaint for return of the money and for profits allegedly suffered by the corporation's business through lack of the funds. Although the money was ultimately repaid to Gullett, the District Court summarily dismissed the claim for lost business profits on grounds that the corporation, not Gullett, was the real party in interest. On appeal, the Supreme Court affirmed. The cause of action for recovery of lost business profits belonged to the corporation, not to a shareholder. Gullett's argument that he should not be barred from the claim because the corporation was an S. corporation also failed because even though an S. corporation is treated differently for taxation purposes, it remains a corporation in all other ways, and the corporation and its shareholders remain separate entities. Gullett v. Van Dyke Constr. Co., 2005 MT 105, 327 M 30, 111 P3d 220 (2005), following Richland Nat'l Bank & Trust v. Swenson, 249 M 410, 816 P2d 1045 (1991), and followed in Cleveland v. Ward, 2016 MT 10, 382 Mont. 118, 364 P.3d 1250. See also Smith Setzer & Sons, Inc. v. S.C. Procurement Review Panel, 20 F3d 1311 (4th Cir. 1994).

Summary Judgment on Breach of Contract Affirmed — Wrongful Discharge Claim Reversed for Determination of Whether Claimant Was Employee or Independent Contractor: Tvedt brought a claim for breach of contract, wrongful termination, and indemnification of expenses, alleging that defendant group had breached the covenant of good faith and fair dealing, waived the at-will clauses in their employment agreement, and mischaracterized Tvedt as an independent contractor, rather than an employee. Defendant group moved for summary judgment and filed a contingent counterclaim stating that in the event that Tvedt was found to be defendant group's employee, then defendant group's obligation to pay Tvedt the contract value should cease and all payments made to Tvedt should be returned. The District Court determined that Tvedt was not an employee and granted summary judgment to defendant group on all claims, and Tvedt appealed. The Supreme Court affirmed summary judgment on the breach of covenant issue because Tvedt was given adequate notice of termination, defendant group was exercising the specific language of the at-will termination provision of the contract, and Tvedt did not demonstrate that defendant group had waived the right to enforce that provision. However, the court reversed summary judgment on the wrongful discharge claim because the District Court incorrectly applied defendant group's novation argument and because genuine issues of fact remained whether Tvedt was an employee or independent contractor and whether a manager's agreement that recognized Tvedt individually was in effect at the time of termination. Remand was ordered because the District Court never considered whether Tvedt was entitled to relief for wrongful discharge as a matter of law and, if so, whether the claim for indemnification was appropriate. Tvedt v. Farmers Ins. Group of Co., 2004 MT 125, 321 M 263, 91 P3d 1 (2004).

Offer Followed by Suggested Changes, Passage of Time, and Acceptance: Following oral modification of written lease to allow lessee to use additional space for additional rent, lessor sent lessee a new lease that incorporated the modification and was essentially the same as the current lease. Lessee's attorney suggested changes not accepted by lessor. Lessor did not revoke his offer of the new lease, and a few months later lessee told lessor on the phone that her attorney's changes were not important to her and she would sign and deliver the lease, which she did the next month. The attorney's suggested changes were not a rejection, the time between the suggestions and the delivery of the signed lease by lessee was not unreasonable under the circumstances and did not work a revocation of the offer of the new lease, and the new lease was executed when lessee signed and delivered it. Lemley v. Allen, 203 M 37, 659 P2d 262, 40 St. Rep. 279 (1983).

Revocation of Offer Contained in Letter of Intent to Contract: An offer may only be revoked prior to its acceptance. Sawyer-Adecor Int'l, Inc. v. Anglin, 198 M 440, 646 P2d 1194, 39 St. Rep. 1118 (1982).

Acceptance of Offer:

Where there was an agreement between an optionee and a prospective purchaser that "it will have to be first man up with the money" who could take up an option for the purchase of an interest in a block of real estate leases, and the prospective purchaser notified the optionee that the money had been raised, the purchaser's action constituted an acceptance and the optionee could not then revoke the offer. Aasheim v. Hoven, 137 M 179, 350 P2d 1025 (1960).

A contract is not created by a mere offer, even though kept open for nearly 2 months, which is revoked before acceptance. Donlan v. Arnold, 48 M 416, 138 P 775 (1914).

Resignation of Professor: A tender of resignation by a professor of the state university was, under the facts presented, a mere offer to resign, i.e., an offer to terminate his contract of employment, and as such could be withdrawn by him at any time before its acceptance by the State Board of Education. State ex rel. Phillips v. Ford, 116 M 190, 151 P2d 171 (1944).

Deposit in Bank for Inspection — Failure to Act: Where the owner of oil land transmitted a lease to a bank with draft to be paid before delivery of the lease, and no payment was made, the lessee requesting and being granted additional time within which to examine the title, and no acceptance of the offer to lease was communicated to the owner after expiration of the time for acceptance, the owner had a right to revoke his offer by requesting a return of the lease and draft. Nadeau v. Tex. Co., 104 M 558, 69 P2d 586 (1937).

Oil and Gas Lease: In the absence of a consideration, a written offer to lease oil and gas lands was revocable by the offeror at any time prior to the creation of a contract by acceptance, even though the time specified in which acceptance could be made had not expired, and withdrawal of the instrument by the offeror from the bank in which it had been deposited and notification of the fact to the offeree by the bank was a revocation, formal notice not having been necessary. Sunburst Oil & Gas Co. v. Neville, 79 M 550, 257 P 1016 (1927).

28-2-512. How proposal revoked.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Revocation of Offer: To be effective, revocation of an offer must be communicated to the offeree. Sawyer-Adecor Int'l, Inc. v. Anglin, 198 M 440, 646 P2d 1194, 39 St. Rep. 1118 (1982).

Part 6
Object of a Contract

28-2-601. Object of contract defined.

Case Notes

Contract for Sale of Illegal Slot Machines Void and Unenforceable: In December 1984, MPH Company (MPH) contracted to purchase 24 "Poker All Keno" electronic gambling machine kits. The kits were delivered in March 1985, but by May and June 1985 had proved to be inoperable. MPH sued the manufacturer for breach of contract, breach of warranty, fraud, and bad faith. In lieu of trial, the parties stipulated that the machines contained design defects rendering them commercially unacceptable and constituting a breach of contract. The District Court awarded MPH $193,663, representing funds expended in satisfaction of the contract, plus $79,354 in prejudgment interest. The Supreme Court reversed after finding that at the time the parties entered into the contract, the machines were not authorized under Montana gambling law and were at best illegal slot machines. Because the machines were unlawful, the entire contract was void. A party to an illegal contract may not use the courts of this state to enforce the agreement. MPH Co. & Tropic Indus. v. Imagineering, Inc., 243 M 342, 792 P2d 1081, 47 St. Rep. 947 (1990).

Novation of Lease — New Lessee's Obligation Not Affected by His Ownership Rights: Franchisor took possession of franchise after franchisee indicated a desire to sell the franchise. To make the franchise more attractive to prospective purchasers, franchisor agreed with Godwin, who had leased equipment to the franchise, to make the rental payments on the equipment if Godwin would forgo repossession of the equipment. In a proceeding involving right to possession of the equipment and recovery of rental payments, although franchisor claimed a right under the Uniform Commercial Code to possession of the equipment under its security agreement with franchisee, the lower court correctly found franchisor liable for rent. That franchisor may have been entitled to possession did not preclude it from making a binding agreement with Godwin to take over franchisee's rental payments. Taylor Rental Corp. v. Ted Godwin Leasing, Inc., 209 M 124, 681 P2d 691, 41 St. Rep. 594 (1984).

Unlawful Agreement to Transfer Radio Station: The plaintiff and defendant entered into a lease and sales right agreement for a radio station. Because the agreement contemplated a de facto transfer of the station without the consent of the Federal Communications Commission, it was unlawful. Because the transfer of the station was the single object of the agreement and because the object was unlawful, the agreement was void. McPartlin v. Fransen, 199 M 143, 648 P2d 729, 39 St. Rep. 1220 (1982).

Certainty of Option Contract — Specific Performance of Reformed Contract: Where the plaintiff and defendant entered into an option contract giving the plaintiff an option to purchase certain real estate but the parties failed to specify the interest which would be retained by the defendant in certain improvements and failed to specify the dates upon which the downpayment and annual payments would be made and the date upon which interest would accrue, the contract was nonetheless sufficiently definite to allow its enforcement by specific performance. At trial, the court took testimony of the parties and reformed the contract so as to make it sufficiently definite as to the defendant's retained interest to allow specific performance. The fact that certain dates were not specified is not fatal to the contract, as it need not be absolutely certain in every detail, and where a time of performance is not specified, a reasonable time will be implied. Keaster v. Bozik, 191 M 293, 623 P2d 1376, 38 St. Rep. 194 (1981).

28-2-602. Essential characteristics of object.

Case Notes

Validity of Forum Selection Language in Employment Contract: A clause in an employment contract provided that in case of disputes, venue for enforcement of the contract would be in the state District Courts of Lewis and Clark County, Montana, or in the district of choice set by the independent contractor. A dispute arose, and plaintiff independent contractor sought to enforce the contract in Lewis and Clark County. Defendant moved to dismiss for lack of personal jurisdiction, and the motion was granted on grounds that the contract's forum clause did not give the court personal jurisdiction over defendant, a resident of Illinois. Plaintiff appealed, and the Supreme Court reversed. As held in May v. Figgins, 186 M 383, 607 P2d 1132 (1980), parties to a contract may agree in advance to submit to the jurisdiction of a given court, and as such, forum selection clauses are prima facie valid and should be enforced unless the resisting party shows that the agreement was not deliberately and understandably made and that the contractual language did not clearly, unequivocally, and unambiguously express a waiver of personal jurisdiction. In this case, the parties knowingly consented to personal jurisdiction in Montana and the forum selection clause was clear and unambiguous. The case was remanded for further proceedings in the Montana court. Milanovich v. Schnibben, 2007 MT 128, 337 M 334, 160 P3d 562 (2007).

Timely Exercise of Third-Party Option to Purchase Real Property — No Breach of Buy-Sell Agreement: A provision in a buy-sell agreement between Palmer and Bahm allowed a third party 72 hours after the Palmer-Bahm agreement was signed to decide whether to purchase a strip of land from Bahm that was contained in the parcel covered by the agreement. Although the third party did not complete the transaction or enter into a separate buy-sell agreement within 72 hours, the buy-sell agreement required only that a purchase decision be made within 72 hours. Uncontroverted evidence showed that the third party made a timely decision to purchase the strip and communicated that decision to Bahm, so Bahm did not violate the agreement with Palmer or break the covenant of good faith and fair dealing by selling the strip to the third party. Palmer v. Bahm, 2006 MT 29, 331 M 105, 128 P3d 1031 (2006).

General Scheme Unlawful — Contract Unenforceable: When the general scheme of contracting parties is to bring about unlawful results, the contract is unenforceable. (See 15 Williston on Contracts 1752, 1755 (3rd Ed. 1972).) MPH Co. & Tropic Indus. v. Imagineering, Inc., 243 M 342, 792 P2d 1081, 47 St. Rep. 947 (1990).

Summary Judgment Proper on Question of Existence of Employment Relationship: A quarrel developed between a store employee and the prospective new store owner over dress policy. The employee walked out and later filed wrongful discharge allegations. The charges were summarily dismissed on the grounds that no employment relationship existed at the time of termination after it was determined that: (1) the prospective owner did not own or control the store on the day of termination; (2) the employee's wages were paid for that day by the former owner; and (3) the employee refused to give the store keys to the prospective owner, claiming they still belonged to the former owner. Janz v. Quenzer, 232 M 439, 756 P2d 1174, 45 St. Rep. 1178 (1988).

Certainty as to Terms of Contract Required — Summary Judgment: In suit for breach of alleged oral contract between law partners to find "a place" in the law firm for any of their children who might wish to become lawyers, District Court granted defendant's motion for summary judgment. Supreme Court affirmed and held that the contract was unenforceable for lack of certainty as to its terms. Defendant's daughter's work for the firm as a law clerk did not perfect the alleged agreement. Plaintiff failed to raise a genuine issue of material fact to preclude entry of summary judgment. Bishop v. Hendrickson, 215 M 158, 695 P2d 1313, 42 St. Rep. 259 (1985). See also Janz v. Quenzer, 232 M 439, 756 P2d 1174, 45 St. Rep. 1178 (1988).

When Contract Impossible or Void — Failure to Act on Defense as Harmless Error: A seller argued on appeal from a verdict for a purchaser in a breach of contract action that the cattle sales contract was void because he did not own the calves at the time of execution of the contract. The seller claimed the contract was wholly impossible and unlawful under 28-2-603. The Supreme Court said that the mere fact that a party contracts to sell something he does not own did not raise the defense of impossibility. The burden of proving impossibility rested on the party asserting it, and he had to show he took virtually every action within his powers to perform his duties under the contract. Here, the seller offered no evidence why it was impossible for him to obtain his wife's consent to the sale or to buy her out. The object of a contract had to be lawful when the contract was made and possible by the time the contract was to be performed. The District Court's failure to rule on the seller's motion for summary judgment on this ground was harmless error because the motion should have been denied. Miller v. Titeca, 192 M 357, 628 P2d 670, 38 St. Rep. 853 (1981).

Requirements of an Escrow — Improper Delivery: In this case concerning a contract for deed, an issue on appeal was whether a warranty deed was delivered improperly by the escrow bank. The Supreme Court noted the caveat of this section that the object of an escrow must be lawful when the contract is made and possible and ascertainable by the time the contract is to be performed. To constitute an instrument in escrow, it must be deposited with the intention that it take effect upon the performance of an express condition or the happening of a certain event. When the instruments here were deposited on condition of payment of a promissory note, it was foreordained that the warranty deed be delivered to the seller. This was not the arrangement at the time of the escrow deposit, according to the testimony of the parties in this case. The escrow deposit was not made until after the time for performance of the condition. The warranty deed thus was delivered to the seller improperly. Stoddard v. Grokin, 191 M 495, 625 P2d 529, 38 St. Rep. 326 (1981).

Real Estate Listing — Vagueness to Be Raised at Trial Level: Plaintiff and defendant entered into a real estate listing agreement. Defendant was a cotenant with her husband. Defendant contended that the listing contained an erroneous asking price, did not adequately describe the property, and was signed only by the defendant. Defendant contended the contract should be declared void due to vagueness. Defendant participated in the contract throughout its entire existence without any objection of vagueness and did not raise the issue at trial. The surrounding circumstances and positions of the parties clearly indicate their intent to enter into and perform an agreement. When reviewing a conflict in testimony regarding ambiguity, the trier of fact is entitled to determine the meaning of the contract in its own right. The reviewing court looks only to determine whether there is substantial credible evidence supporting the verdict. The vagueness issue was not raised in the District Court, thus it could not be considered on appeal. Barrett v. Ballard, 191 M 39, 622 P2d 180, 37 St. Rep. 2038 (1980).

Certainty of Description — Preemptive Right to Purchase Land: Where an agreement stipulated that the plaintiffs were to have the right of first refusal on "any additional tracts seller may offer", that preemptive right agreement was fatally defective because it was impossible to determine the description of the property to which the right applied with accuracy, even though resorting to extrinsic evidence. Klien v. Brodie, 167 M 47, 534 P2d 1251 (1975).

Purpose Ascertainable: A contract relating to the sale of mining property which could be construed as either authorizing plaintiff to secure a purchaser or to purchase the property himself was sufficiently clear to be enforceable. Smith v. Jack Pot Min. Co., 109 M 445, 97 P2d 368 (1939).

28-2-603. When contract wholly void.

Case Notes

Challenge to Contract or to Arbitration Clause — When Arbitration Appropriate: Plaintiffs defaulted on a loan with defendant, and nonjudicial foreclosure proceedings were begun. The loan contract contained an arbitration clause, but plaintiffs challenged the validity of the contract as a whole, not the validity of the arbitration clause. On defendant's motion, the District Court ordered arbitration, and plaintiffs appealed. The Supreme Court held that under federal law, when a complaint specifically challenges a contract arbitration clause, the doctrine of severability set out in Prima Paint Corp. v. Flood & Conklin Mfg. Co., 388 US 395 (1967), in conjunction with the Federal Arbitration Act, allows a court to hear the challenge. However, when, as here, a complaint challenges a contract as a whole, Prima Paint and Buckeye Check Cashing, Inc. v. Cardegna, 546 US 440 (2006), require a court to grant a motion to compel arbitration if the contract contains an arbitration provision. Thus, despite plaintiffs' contention that the contract itself was void ab initio, the District Court was affirmed. Martz v. Beneficial Mont., Inc., 2006 MT 94, 332 M 93, 135 P3d 790 (2006). However, see Thompson v. Lithia Chrysler Jeep Dodge of Great Falls, 2008 MT 175, 343 M 392, 185 P3d 332 (2008), in which a narrow exception to the Martz rule established that when a party challenges a contract containing an arbitration clause on the ground that the parties never entered a contract, the court, not arbitration, is the appropriate forum to decide whether a contract existed, prior to compelling arbitration.

Unenforceability of Buy-Sell Agreement on Grounds of Impossibility or Impracticality of Performance — Requiring Performance of Contract With Potential for Environmental Degradation Unconstitutional: Cape-France Enterprises (Cape-France) entered a buy-sell agreement with Peed (now deceased) and Moore to purchase some property near Bozeman for a subdivision. Before the subdivision could be completed, water needed to be procured for the site. According to the agreement, as buyers, Peed and Moore were responsible to bring water to the property, but because city water was not available, a well needed to be drilled. However, the presence of a pollution plume was discovered near the land. After the subdivision process was commenced, the Department of Environmental Quality notified Cape-France that: (1) the plume may have advanced under the property; (2) a subdivision would not be approved unless a well was drilled and tested; (3) a well could be drilled, but if testing showed pollution in the water, treatment would be extensive; and (4) if drilling or pumping of the water caused expansion of the pollution, then Cape-France, as owner of the property, would be held liable for cleanup costs. On cross-motions for summary judgment, the District Court held that the buy-sell agreement could be rescinded on the basis of mutual mistake of fact and impossibility or impracticality of performance and that specific performance would not be granted. The Supreme Court affirmed. A court may determine that an act is impossible in legal contemplation when it is not practicable, when the act can be done only at an excessive, unreasonable, and unbargained-for cost. The doctrine of impossibility or impracticability is applied when, aside from the object of a contract being unlawful, the public policy underlying the strict performance of the contract is outweighed by the senselessness of requiring performance. The doctrine is not limited to cases of literal impossibility but may also be applied in cases that present a potential for substantial and unbargained-for damages. In this case, requiring Cape-France to go forward with the performance of the contract when there was a very real possibility of substantial environmental degradation and resultant financial liability for cleanup was not in the public interest or in the interests of the contracting parties and was not in accord with the guarantee of a clean and healthful environment in Art. II, sec. 3, Mont. Const., or the mandate to maintain and improve a clean and healthful environment for present and future generations in Art. IX, sec. 1, Mont. Const. Thus, rescission of the contract was proper. Cape-France Enterprises v. Estate of Peed, 2001 MT 139, 305 M 513, 29 P3d 1011 (2001). See also Smith v. Zepp, 173 M 358, 567 P2d 923 (1977), and Mont. Envtl. Information Center v. Dept. of Environmental Quality, 1999 MT 248, 296 M 207, 988 P2d 1236 (1999).

Questions as to Buyer's Intent and Seller's Impossibility of Performance — Summary Judgment Improper: Seller sold 20 acres with a separate option agreement to reacquire 15 of the acres. The option agreement stated that if the option was not exercised within a year, buyer was to retain the 15 acres and the option was void. The buyer's affidavit stated that it was his intent to purchase 20 acres, subject to the option, and to retain all 20 acres if the option was not exercised in accordance with its terms. Because of a conflict between the local government master plan (now growth policy) and zoning map for the area, which was not resolved within the year of the option, the option could not be exercised. The District Court granted seller summary judgment in the seller's action for declaratory relief, ruling that it was impossible for seller to comply with the option because of the master plan (now growth policy)-zoning map conflict and that equity and good conscience required that seller be given reasonable additional time to comply with the option conditions. The language of the option agreement and the buyer's affidavit showed a genuine issue of material fact with regard to the parties' intent. In addition, the buyer's contention that seller was dilatory in exercising the option and that the delay caused the option to expire raised a genuine issue of material fact as to the question of impossibility of performance. Therefore, the grant of summary judgment was error. Furthermore, the District Court exceeded its authority in granting equitable modification of the express terms of the option contract to give seller additional time to perform. 360 Ranch Corp. v. R&D Holding, 278 M 487, 926 P2d 260, 53 St. Rep. 1038 (1996).

Employment Contract for Performance of Embryo Transfers by Nonveterinarian Void for Illegal Purpose: Employment contracts entered into in 1980 by an embryonics corporation and two persons who were not veterinarians, for the performance of bovine embryo transfers in Montana, were contracts for the illegal purpose of unauthorized practice of veterinary medicine and were therefore void. Actions arising from alleged breach of the contracts were unenforceable. Portable Embryonics, Inc. v. J.P. Genetics, Inc., 248 M 242, 810 P2d 1197, 48 St. Rep. 415 (1991).

Contract for Sale of Illegal Slot Machines Void and Unenforceable: In December 1984, MPH Company (MPH) contracted to purchase 24 "Poker All Keno" electronic gambling machine kits. The kits were delivered in March 1985, but by May and June 1985 had proved to be inoperable. MPH sued the manufacturer for breach of contract, breach of warranty, fraud, and bad faith. In lieu of trial, the parties stipulated that the machines contained design defects rendering them commercially unacceptable and constituting a breach of contract. The District Court awarded MPH $193,663, representing funds expended in satisfaction of the contract, plus $79,354 in prejudgment interest. The Supreme Court reversed after finding that at the time the parties entered into the contract, the machines were not authorized under Montana gambling law and were at best illegal slot machines. Because the machines were unlawful, the entire contract was void. A party to an illegal contract may not use the courts of this state to enforce the agreement. MPH Co. & Tropic Indus. v. Imagineering, Inc., 243 M 342, 792 P2d 1081, 47 St. Rep. 947 (1990).

Illegal Loan Agreement — Bar to Counterclaim: The Supreme Court upheld a District Court's grant of summary judgment, ruling that counterclaims arising out of an illegal loan agreement are barred. Powder River County Bank v. Arness-McGriffin Coal Co., 225 M 358, 732 P2d 1326, 44 St. Rep. 300 (1987).

Release and Subrogation as Single, Nonseverable Contract: Plaintiff was severely burned after a truck driven by an employee of H. Pierce Manufacturing Co. ran into the rear of her 1970 Ford Mustang, which caught fire. Plaintiff retained James Reno to represent her. Reno began negotiations with Pierce's insurer, St. Paul Fire and Marine Co. At the time Pierce was insured with St. Paul for up to $100,000 and with an excess carrier, Atlantic Co., for up to $2 million. Reno did not inquire as to what the excess carrier's coverage limits were. Reno and the adjuster agreed to a settlement entered by plaintiff for $300,000. Two separate documents consisting of the combined release and indemnification agreements and a subrogation agreement were executed. Reno agreed with the insurers to also pursue their interests against Ford. The insurers later retained independent counsel, and Reno filed an action against Ford. Ford sought to have the subrogation provision declared invalid. The release and subrogation agreements were so indivisible as to prevent enforcing one without the other, since both were offered in consideration of the settlement, and there was no way to allocate the settlement among the release, indemnification, and subrogation portions of the contract. Voiding the subrogation agreement requires voiding the entire release agreement. Abell v. Ford Motor Co., 39 St. Rep. 1347 (D.C. Mont. 1982) (apparently not reported in Federal Supplement).

Money Owed Under Unlawful Agreement to Transfer Radio Station: The plaintiff buyer and the defendant seller entered into a lease and sales right agreement for a radio station. Because the agreement contemplated a de facto transfer of the station without the consent of the Federal Communications Commission, it was unlawful and void. Because parties to an illegal contract cannot come into a court of law to have its illegal objects carried out, the defendant may keep the plaintiff's downpayment, the plaintiff may keep the accounts receivable he collected that were owned by the defendant, and the plaintiff need not pay unpaid rent owing to the defendant. McPartlin v. Fransen, 199 M 143, 648 P2d 729, 39 St. Rep. 1220 (1982).

Contract Provisions Ascertainable by Conduct of Parties: Where electrical contractor submitted a bid on a job based not on written specifications but on a previous similar job and the previous pattern of conduct between the parties indicated that both parties contemplated the rendering of particular services and materials, contract was not so ambiguous as to render its object wholly unascertainable. Mathis v. Daines, 196 M 252, 639 P2d 503, 39 St. Rep. 73 (1982).

When Contract Impossible or Void — Failure to Act on Defense as Harmless Error: A seller argued on appeal from a verdict for a purchaser in a breach of contract action that the cattle sales contract was void because he did not own the calves at the time of execution of the contract. The seller claimed the contract was wholly impossible and unlawful under this section. The Supreme Court said that the mere fact that a party contracts to sell something he does not own did not raise the defense of impossibility. The burden of proving impossibility rested on the party asserting it, and he had to show he took virtually every action within his powers to perform his duties under the contract. Here, the seller offered no evidence why it was impossible for him to obtain his wife's consent to the sale or to buy her out. The object of a contract had to be lawful when the contract was made and possible by the time the contract was to be performed. The District Court's failure to rule on the seller's motion for summary judgment on this ground was harmless error because the motion should have been denied. Miller v. Titeca, 192 M 357, 628 P2d 670, 38 St. Rep. 853 (1981).

Contract Establishing Life Estate Not Void: A claim that under this section a contract for the sale of an apartment building which contains a provision reserving a life estate to appellant is impossible because appellant did not hold title to the property and thus could not reserve a life estate to herself cannot stand given the terms of the contract, which clearly indicate the agreed intention on the part of the titleholders that appellant be entitled to remain in possession of the property for the rest of her life. A reservation need not be implied on the part of the appellant. Harbeck v. Orr, 192 M 243, 627 P2d 1217, 38 St. Rep. 668 (1981).

Real Estate Listing — Capability of Performance — Sale by Cotenant: Plaintiff and defendant entered into a real estate listing agreement. Defendant was a cotenant in the property with her husband. The defendant contended that listing contained an erroneous asking price, did not adequately describe the property to be sold, and was signed only by the defendant. A cotenant in a joint tenancy has a right and ability to sell her interest. Defendant was free to act and capable of acting without her husband, even though the husband knew at all times that she had put the property up for sale. Because she was capable of entering and performing contracts and was legally responsible for her acts, the contract was fully capable of being performed. Barrett v. Ballard, 191 M 39, 622 P2d 180, 37 St. Rep. 2038 (1980).

Impossibility of Performance: A Montana contract for construction of a complete operating oil refinery to process Oregon Basin crude oil so as to yield 60% gasoline containing not more than 10% sulphur had but a single object and was void under 1-1-108, 1-1-109, 1-2-103, 28-2-601, this section, and section 10704, R.C.M. 1935 (since repealed), where it was impossible to obtain such a yield of gasoline, whether or not contractor knew or should have known of such impossibility, and contractor was entitled to a recovery on the quantum meruit. His bond did not permit recovery of damages, a collateral promise in the contract consisting of warranty was invalid and would not support action for breach of warranty, and contractor's lien was supported by the implied contract. Smith Eng'r Co. v. Rice, 102 F2d 492 (9th Cir. 1938).

Void When Prohibited by Statute: A contract expressly prohibited by a valid statute is void, and courts may not disregard such prohibition. Johnson v. Kaiser, 104 M 261, 65 P2d 1179 (1937), overruled on another point in Aitken v. Lane, 108 M 368, 92 P2d 628 (1939).

Wagering or Gambling Transactions — Grain Market: In order to invalidate a contract as a wagering or gambling transaction (instant case grain market transaction) both parties must have intended that instead of delivery of the article there should be a mere payment of the difference between the contract price and the market price, i.e., a settlement of the difference, and burden of proof is on the party assailing the transaction. H. Earl Clack Co. v. Oltesvig, 104 M 255, 68 P2d 586 (1937).

When Uncertainty Makes Contracts Void:

Agreement that is so vague and indefinite that it is impossible to collect from it the full intention of parties is void, since neither court nor jury can make agreement for parties. Schwartz v. Inspiration Gold Min. Co., 15 F. Supp. 1030 (D.C. Mont. 1936).

In an action to quiet title to an interest in a ditch and water right, based upon conversations had by plaintiff with defendant, for work done on the ditch by him, evidence of plaintiff as to the alleged contract was so indefinite and uncertain under this section as not to constitute an enforceable agreement, it not appearing therefrom what amount of work plaintiff was to perform or in which one of several ditches he was to have an interest. Thrasher v. Schreiber, 77 M 221, 250 P 600 (1926).

A covenant in a lease of a building which required the lessee to complete the upstairs portion thereof without any specifications as to how it was to be completed, whether for office, living room, or storage purposes, or as to the kinds of materials to be used, etc., was so vague and uncertain as to be incapable of enforcement and therefore void under this section. Alderson v. Republican-Courier Co., 69 M 271, 221 P 544 (1923).

A lease of agricultural lands which did not impose upon either party the work of preparing them for crops or provide who should furnish seed, bear the expense of harvesting, extra help, etc., was not void for uncertainty, it being implied under 28-3-702 from the fact that the lessees were to have possession for the purpose of producing crops, that they were to do these things. McDonald v. McNinch, 63 M 308, 206 P 1096 (1922).

In an action for damages for breach of a lease of farm lands by the lessors, the lease was not void for uncertainty for failing minutely to describe a building site and right-of-way reserved by the lessors, where it was apparent therefrom that the burden of selecting them within a reasonable time was upon the lessors and that they themselves had caused the uncertainty to exist. McDonald v. McNinch, 63 M 308, 206 P 1096 (1922).

In an action by a lessor to recover his share of grain, alleged to have been raised by the defendant under a contract of lease of agricultural land, the only definite portion of which was that which secured to defendant, without naming a consideration, the possession of the land for a specified time but which did not bind him to do anything or raise any grain, the contract was void for uncertainty. Schwab v. McVey, 54 M 422, 171 P 277 (1918).

Where it could not be determined from a printed order blank containing many pages and covering a large variety of jewelry how many articles of a particular kind and price had been ordered, the memorandum of sale was so indefinite and uncertain as to make it unenforceable at law. Price v. Stipek, 39 M 426, 104 P 195 (1909).

Duty of Parties in Contracting:

The parties to a contract must express themselves in terms direct and explicit enough to enable their full intention to be ascertained to a reasonable degree of certainty. Evankovich v. Howard Pierce, Inc., 91 M 344, 8 P2d 653 (1932).

In order that a contract may be enforceable, the parties must express themselves in terms direct and explicit enough to enable their full intention to be ascertained to a reasonable degree of certainty. Schwab v. McVey, 54 M 422, 171 P 277 (1918).

28-2-604. When contract partially void.

Case Notes

Unenforceability of Part of Noncompetition Covenant: The District Court found that part of a noncompetition covenant was void. Tucker argued that the District Court erred in not ruling that an entire noncompetition covenant was void and that he was entitled to a refund for the full amount paid for the covenant. The Supreme Court held that the District Court had properly applied the "blue pencil approach" in limiting the covenant to the contiguous counties and, in so doing, did not void the covenant in its entirety. Dumont v. Tucker, 250 M 417, 822 P2d 96, 48 St. Rep. 996 (1991).

Limitation on Tax-Free Exchange Clause: Defendants contacted plaintiff to sell their ranch. The agreement allowed for a multiple listing. An interested buyer was found. Later a tax-free property exchange clause was inserted in the contract. Defendants located property in Arizona, but the buyer would not purchase it for exchange because of a defect in defendants' title. The Arizona property was sold before defendants cleared their title. Defendants eventually sold their property to the buyer. Defendants refused to pay the realtor commission, and a suit was filed. Defendants counterclaimed against the buyer for refusing to purchase the Arizona property pursuant to the exchange clause. The District Court refused defendants' offered instructions on alleged breach of the exchange clause. On appeal, the Supreme Court upheld the District Court, saying that as drafted the exchange clause placed an unreasonable burden on the buyer. The buyer could have been forced to exchange for an unmerchantable title. The court held the exchange clause in the contract invalid. The court did not reject the use of exchange clauses in real estate contracts but said they should be conditioned so as to require merchantability to be proven before the buyer must obligate himself to purchase exchange property. Adams v. Cheney, 203 M 187, 661 P2d 434, 40 St. Rep. 383 (1983).

Part 7
Illegal Objects and Provisions

Part Case Notes

Shared Well Agreement Valid Despite Subdivision Requirement for Individual Wells When Approved by State and County Regulators: Despite conditions in the subdivision certificate that called for individual water wells on each tract, the predecessors in interest to the Williamses and the Schwagers entered a shared water well agreement that endured between the tract owners for about 20 years. The subdivision certificate was approved by both the state and county. A disagreement arose between the Williamses and the Schwagers regarding use of the shared well, and the Williamses sought to enjoin the Schwagers from interfering with the well. The Schwagers responded that the well was in violation of the subdivision certificate and that the shared water well agreement was thus void. The District Court concluded that the agreement was valid and enforceable, and granted the Williamses' injunction. The Schwagers appealed, but the Supreme Court affirmed. The agreement was not void ab initio because the subdivision certificate was approved as required prior to installation of the water system, nor was the agreement illegal per se, because a county health department official testified that the parties could still obtain approval for a shared well, which was encouraged by the county in cases in which sufficient water existed, despite the requirement in the subdivision certificate that called for individual water systems. Further, the Schwagers could not attempt to benefit from repudiating the contract after previously accepting the benefits of the agreement in the form of water fees from the Williamses, and the District Court did not err in enforcing the agreement. Williams v. Schwager, 2002 MT 107, 309 M 455, 47 P3d 839 (2002).

Validity of Alleged Forfeiture Upheld — Necessity of Right in Property: Where the plaintiff and defendant entered into a commission contract providing that the defendant would not pay any commission to the plaintiff unless the purchaser of the defendant's property fulfilled its duties under a contract for deed, the Supreme Court held that the failure of the defendant to pay a portion of the plaintiff's commission did not constitute an unlawful forfeiture. In order for there to be a forfeiture, the plaintiff in this case must, under the rationale of Ridgeway v. City of Akron, 42 NE2d 724 (Ohio Ct. App., 1940), have a right in the commission. No such right could arise as the condition precedent had not been satisfied, and there was therefore no forfeiture. Martin v. Community Gas & Oil Co., 205 M 394, 668 P2d 243, 40 St. Rep. 1385 (1983).

Medical Payment Subrogation Clauses in Insurance Policies — Invalid: Welton was insured by Allstate when she was injured in an accident caused by Reitler. Allstate paid Welton $2,000 for the medical expenses she incurred as a result of the accident. Welton also received a $9,500 settlement from Reitler. Allstate then brought suit against Reitler to recover the $2,000 it paid Welton under a subrogation clause in its policy with Welton. The Supreme Court held that medical payment subrogation clauses are invalid and unenforceable. Allstate Ins. Co. v. Reitler, 192 M 351, 628 P2d 667, 38 St. Rep. 821 (1981), clarified in Youngblood v. Am. St. Ins. Co., 262 M 391, 866 P2d 203, 50 St. Rep. 1601 (1993). See also Farmers Ins. Exch. v. Christenson, 211 M 250, 683 P2d 1319, 41 St. Rep. 1342 (1984). However, see Scheafer v. Safeco Ins. Co., 2014 MT 73, 374 Mont. 278, 320 P.3d 967, holding that a requirement that primary coverage be exhausted before secondary insurance coverage is triggered is not subrogation.

Third Party May Not Question Legality: While either party to an agreement may raise the question of its illegality, it may not be invoked by a third party. Owens v. Davenport, 39 M 555, 104 P 682 (1909).

28-2-701. What is unlawful.

Case Notes

Violation of Statute 196
Violation of Public Policy 197
Violation of Morals 200
Miscellaneous 200

VIOLATION OF STATUTE

Terms of Plea Agreement Illegal — Defendant Not Entitled to Specific Performance of Plea Agreement: The defendant entered into a plea agreement under which he would receive a deferred sentence. Later, however, it was learned that he did not qualify for a deferred sentence and the District Court instead imposed a suspended sentence. On appeal, the Supreme Court concluded that the terms of the plea agreement were illegal and unenforceable and the defendant was therefore not entitled to specific performance of the agreement. St. v. Cleveland, 2014 MT 305, 377 Mont. 97, 338 P.3d 606.

Failure to Conform With Literal Language of Administrative Rule Not Illegal and Therefore Not Justification for Breach of Contract: Lewis subcontracted to do the electrical work on five units being built by Huyser. In the first four units, some of the rough-in wiring was covered, but the electrical inspector did not require that all the wiring be visible even though the literal language of the administrative rule indicated that it should be. On the fifth unit, shelving had been installed before the inspection. Lewis insisted that it all be taken down, claiming that he could lose his license if it was not. Huyser had some of the shelving removed, exposing some of the rough-in wiring. Lewis refused to complete the work, and Huyser hired another electrician to complete the job. Lewis sued for payment, and Huyser counterclaimed. The lower court found for Huyser on the basis that the inspector had informed Lewis that he would not lose his license and that the inspector would accept part of the rough-in wiring being exposed. The Supreme Court affirmed, holding that the administrative rule should be reasonably interpreted to allow for waiver by the inspector of the requirement that all rough-in wiring be exposed. The Supreme Court further held that violation of the rule was not a statutory ground for losing an electrical license. The rule having been waived, the contract was not contrary to the policy of express law so that Lewis had a good faith duty to perform the remainder of the contract. Lewis v. Huyser, 264 M 141, 870 P2d 95, 51 St. Rep. 192 (1994).

Employment Contract for Performance of Embryo Transfers by Nonveterinarian Void for Illegal Purpose: Employment contracts entered into in 1980 by an embryonics corporation and two persons who were not veterinarians, for the performance of bovine embryo transfers in Montana, were contracts for the illegal purpose of unauthorized practice of veterinary medicine and were therefore void. Actions arising from alleged breach of the contracts were unenforceable. Portable Embryonics, Inc. v. J.P. Genetics, Inc., 248 M 242, 810 P2d 1197, 48 St. Rep. 415 (1991).

Failure to Pay Wage Rates Prescribed in Contract — Employer Liable for Penalties: Contractors appealed from a District Court order, arguing that because wage rates were not adopted in compliance with administrative procedures, inclusion constituted an illegal provision in the contract with which contractors were not required to comply. The Supreme Court held that contractors were legally bound to pay the wage rates agreed to by all parties and contained in a voluntarily executed contract. Lix v. Kenney, 246 M 426, 804 P2d 391, 48 St. Rep. 23 (1991).

Contract for Sale of Illegal Slot Machines Void and Unenforceable: In December 1984, MPH Company (MPH) contracted to purchase 24 "Poker All Keno" electronic gambling machine kits. The kits were delivered in March 1985, but by May and June 1985 had proved to be inoperable. MPH sued the manufacturer for breach of contract, breach of warranty, fraud, and bad faith. In lieu of trial, the parties stipulated that the machines contained design defects rendering them commercially unacceptable and constituting a breach of contract. The District Court awarded MPH $193,663, representing funds expended in satisfaction of the contract, plus $79,354 in prejudgment interest. The Supreme Court reversed after finding that at the time the parties entered into the contract, the machines were not authorized under Montana gambling law and were at best illegal slot machines. Because the machines were unlawful, the entire contract was void. A party to an illegal contract may not use the courts of this state to enforce the agreement. MPH Co. & Tropic Indus. v. Imagineering, Inc., 243 M 342, 792 P2d 1081, 47 St. Rep. 947 (1990).

Contract Made Without License: The District Court erred in concluding that the contract entered into between the parties was illegal and therefore void. Appellant admits that it did not have a public contractor's license as required by statute when it accepted the bid proposal. It admits that it may have violated the law and may be assessed a misdemeanor fine. Nowhere in the statutes is it declared that a contract made without a license is unenforceable or void. Taurman v. Cascade, 192 M 529, 629 P2d 226, 38 St. Rep. 906 (1981).

Public Policy: The absence of "omnibus" coverage in a liability insurance policy with car dealer is not violative of public policy if there is no violation of any statute. Universal Underwriters Ins. Co. v. St. Farm Mut. Auto. Ins. Co., 166 M 128, 531 P2d 668 (1975).

Contract to Extinguish Tax Liability: A resolution of the Board of County Commissioners which extinguished the assessed tax of a taxpayer was void because such Boards have no power, authority, or jurisdiction under the 1889 Montana Constitution or statutes to reduce, compromise, remit, release, cancel, diminish, or extinguish any state tax, obligation, or liability, or any assessed tax valuation or percentage assignments of property after the same has been found, determined, and fixed by the State Board of Equalization (now Montana Tax Appeal Board). Likewise, the direction of the Board directing the County Attorney to stipulate with the attorneys for the taxpayer, to request the court to enter judgment against the county and state was and is wholly void and of no legality whatever. Such void act, understanding, or agreement by public officials, void in its inception, is not validated by performance and remains a void act or agreement under the public policy established by the Legislature. Carlson v. Flathead County, 130 M 36, 293 P2d 279 (1956).

Contract Not to Contravene Law: Plaintiff entered a lease on certain mining claims with a lessee. Lessee operated the mines pursuant to the lease. Pursuant to the lease, what would normally be treated as royalty payments were called purchase money payments. The court held that the payments were subject to taxation, as a law established for a public reason cannot be contravened by private contract. Silver Bell Min. Co. v. Lewis & Clark County, 129 M 269, 284 P2d 1012 (1955).

Contracts Violating Statutes: Contracts made in violation of express statutes are contrary to public policy and void. Hutterian Brethren v. Haas, 116 F. Supp. 37 (D.C. Mont. 1953); Hames v. Polson, 123 M 469, 215 P2d 950 (1950); Glass v. Basin & Bay St. Min. Co., 31 M 21, 77 P 302 (1904).

Law Cannot Prohibit and Enforce Contract: A broker in the state of Illinois there entered into a contract with an oil well owner operating in Montana to sell stock of the company in which the latter was interested. The Securities Act of Illinois required that before stock of the kind in question could be sold, certain information relative thereto had to be filed with the Secretary of State and declared sales made in that disregard of the requirements of the Act a misdemeanor. The broker sold the stock notwithstanding that the first-mentioned provisions had not been complied with and forwarded the proceeds to his principal in Montana without deducting his commission. The stock thereafter increased greatly in value. In an action by the broker for breach of contract for failure of payment of the commission, the court held that the contract was void, since it was expressly prohibited by a valid statute, and the law cannot at the same time prohibit a contract and enforce it. McManus v. Fulton, 85 M 170, 278 P 126, 67 ALR 690 (1929).

Lawful Contracts Void When Object Becomes Unlawful: A contract under which defendant was granted the right to use a patented process for dealcoholizing malt beverages which was lawful when it was first entered into became unlawful when the prohibition law took effect (December 31, 1918) and was void thereafter insofar as it remained executory, thereby depriving plaintiff patent owner of his remedy to recover under a clause of the contract providing that, in addition to a certain royalty per barrel of beverage manufactured, defendant should pay for the use of the process not less than $500 per year for 3 years from and after December 18, 1917. Baltimore Process Co. v. Red Lodge Brewing Co., 66 M 407, 213 P 798 (1923).

Contract Contrary to Law: A statute requiring the County Commissioners to contract with a newspaper of general circulation published within the county for the county printing, including blanks and blank books, was a prohibition against contracting with any other than a newspaper of the county, and any contract in derogation thereof is void. Hill County v. Shaw & Borden Co., 225 F 475 (9th Cir. 1915).

VIOLATION OF PUBLIC POLICY

Limited Exceptions for Only One Party Insufficient to Render Arbitration Clause Facially Unconscionable: A contract between the defendant-appellee and a third-party provider ("TPP") of home automation products allowing remote control over property access, HVAC, and hot water systems included a clause requiring the parties to arbitrate disputes, with two narrow exceptions, both of which would allow the TPP to seek relief in court in lieu of arbitration. The District Court held that the arbitration clause was unenforceable because the exceptions unreasonably favored the TPP, resulting in a lack of mutuality. The Supreme Court disagreed and upheld the arbitration clause. The two exceptions allowed the TPP to join the defendant-appellee as a third-party defendant for purposes of enforcing the contract indemnification provisions and allowed the TPP to seek injunctive relief if the defendant-appellee breached the contract with respect to the TPP's intellectual property, proprietary rights, or business reputation. The Supreme Court held that the defendant-appellee and TPP were dissimilarly situated such that the defendant-appellee had no need for either of the narrow exceptions. Therefore, the limited exceptions being available only for the TPP was insufficient to show the arbitration agreement was lacking in mutual consideration or was otherwise unconscionable. Stowe v. Big Sky Vacation Rentals, Inc., 2019 MT 288, 398 Mont. 91, 454 P.3d 655.

Choice of Law — Nonbeneficiary Third Party Cannot Assert Defenses and Counterclaims Arising From Contract: The defendant set up Limegrove Corporation for tax purposes, and he informally ran the day-to-day operations. Limegrove's sole shareholder was a trust for the defendant's children. To secure a property loan for a Montana-based property to be held by Limegrove, the defendant signed a promissory note and a term loan agreement, both subject to New York law, and Limegrove and the plaintiff bank signed a trust indenture security agreement subject to Montana law. Because judicial foreclosures must occur where the property is located, the parties correctly agreed that the subsequent foreclosure action on the property was governed by Montana law, but the parties disagreed on which state governed the defendant's defenses and counterclaims. Because the defendant was not a party to the trust indenture, his defenses and counterclaims could not arise from it, and because New York law did not offend Montana public policy, the District Court did not err in concluding that New York law governed the defendant's defenses and counterclaims. HSBC Bank USA, N.A. v. Anderson, 2017 MT 257, 389 Mont. 106, 406 P.3d 416.

Unenforceability of Buy-Sell Agreement on Grounds of Impossibility or Impracticality of Performance — Requiring Performance of Contract With Potential for Environmental Degradation Unconstitutional: Cape-France Enterprises (Cape-France) entered a buy-sell agreement with Peed (now deceased) and Moore to purchase some property near Bozeman for a subdivision. Before the subdivision could be completed, water needed to be procured for the site. According to the agreement, as buyers, Peed and Moore were responsible to bring water to the property, but because city water was not available, a well needed to be drilled. However, the presence of a pollution plume was discovered near the land. After the subdivision process was commenced, the Department of Environmental Quality notified Cape-France that: (1) the plume may have advanced under the property; (2) a subdivision would not be approved unless a well was drilled and tested; (3) a well could be drilled, but if testing showed pollution in the water, treatment would be extensive; and (4) if drilling or pumping of the water caused expansion of the pollution, then Cape-France, as owner of the property, would be held liable for cleanup costs. On cross-motions for summary judgment, the District Court held that the buy-sell agreement could be rescinded on the basis of mutual mistake of fact and impossibility or impracticality of performance and that specific performance would not be granted. The Supreme Court affirmed. A court may determine that an act is impossible in legal contemplation when it is not practicable, when the act can be done only at an excessive, unreasonable, and unbargained-for cost. The doctrine of impossibility or impracticability is applied when, aside from the object of a contract being unlawful, the public policy underlying the strict performance of the contract is outweighed by the senselessness of requiring performance. The doctrine is not limited to cases of literal impossibility but may also be applied in cases that present a potential for substantial and unbargained-for damages. In this case, requiring Cape-France to go forward with the performance of the contract when there was a very real possibility of substantial environmental degradation and resultant financial liability for cleanup was not in the public interest or in the interests of the contracting parties and was not in accord with the guarantee of a clean and healthful environment in Art. II, sec. 3, Mont. Const., or the mandate to maintain and improve a clean and healthful environment for present and future generations in Art. IX, sec. 1, Mont. Const. Thus, rescission of the contract was proper. Cape-France Enterprises v. Estate of Peed, 2001 MT 139, 305 M 513, 29 P3d 1011 (2001). See also Smith v. Zepp, 173 M 358, 567 P2d 923 (1977), and Mont. Envtl. Information Center v. Dept. of Environmental Quality, 1999 MT 248, 296 M 207, 988 P2d 1236 (1999).

Subrogation of Medical Payments Under Motor Vehicle Insurance Policy — Against Public Policy: Subrogation is an equitable doctrine that is not dependent on privity or on a contractual relationship between the parties. Its purpose is to prevent injustice by compelling the ultimate payment of a debt by the one who, in justice, equity, and good conscience, should pay it, and it is an appropriate means of preventing unjust enrichment. Subrogation is distinguishable from assignment of a claim. With some exceptions, subrogation between an insurer and an insured up to the amount the insurer actually paid is allowed if the insured has been fully compensated, including compensation for costs and attorney fees. One exception is a motor vehicle insurance medical payments subrogation clause, which violates public policy because the insured paid a premium for medical coverage, the insured is the one likely to suffer most if medical payments received must be repaid out of a third-party recovery, and the tortfeasor's insurer may believe that the injured insured has already been paid medical expenses and that the insurer can thus make a smaller offer on the basis that medical payments have already been made. Youngblood v. Am. St. Ins. Co., 262 M 391, 866 P2d 203, 50 St. Rep. 1601 (1993).

Effect of "As Is" Clause in Used Car Sales Agreement: When defendant failed to inspect a car for defects before sale to plaintiff and the defect that was the proximate cause of plaintiff's accident and subsequent injuries would have been discovered in a reasonable safety inspection, defendant should not be allowed to hide behind the cloak of a simple "as is" disclaimer. Public policy requires a used car dealer to inspect the cars he sells and to make sure they are in safe, working condition. Kopischke v. First Cont. Corp., 187 M 471, 610 P2d 668 (1980).

Release From Liability Void as Contrary to Public Policy: This section, together with 1-3-204 and 27-1-701, was broad enough to render illegal any exculpatory clause or release relieving a potential tortfeasor from all liability for future negligent conduct where such clause or release was contrary to public policy or against the public interest. Release relieving county fair board from any liability to livestock while on fairgrounds was illegal and unenforceable as contrary to public policy and against public interest and precluded the county from disclaiming liability in a negligence action for exhibitor's horses killed in a barn fire on county fairgrounds. The suppression of the release in exhibitor's negligence action was not error or ground for new trial. Haynes v. County of Missoula, 163 M 270, 517 P2d 370 (1973).

Public Officer — Interest in Contract: Contracts entered by a city in which a city officer was interested may be avoided at the instance of any party except the public officer. These contracts were merely voidable and were not legally void until declared so. Grady v. Livingston, 115 M 47, 141 P2d 346 (1943).

Circumvention of "Scale-Down" Agreement by Farmer's Creditor: Where a farmer's creditor, after signing a so-called "scale-down" agreement required under the Emergency Farm Mortgage Act as a prerequisite to a loan to the farmer, whereby he agreed to accept partial payment of his claim in full settlement of the farmer's obligation, thereafter required the farmer's son-in-law to execute a note as accommodation maker for the difference between the settlement and the amount of the claim, the note amounted to a fraud upon the bank, the debtor, and his creditors and was void as against public policy, and the creditor was not a holder in due course. May v. Whitbeck, 111 M 568, 113 P2d 332 (1941).

Public Policy Not to Prohibit Lawful Contracts: A state may not, under the guise of protecting the public by the exercise of its police power, arbitrarily interfere with private business or prohibit lawful occupations or impose unreasonable or unnecessary restrictions upon them. The fact that unscrupulous men may enter into fraudulent contracts respecting a lawful business, in this case burial contracts not made in contemplation of imminent death, is not alone a sufficient ground for the Legislature to prohibit lawful contracts respecting that business, under the police power, by declaring such contracts void as against public policy. St. v. Gateway Mortuaries, Inc., 87 M 225, 287 P 156, 68 ALR 1512 (1930).

Contract Increasing Taxable Property Not Illegal: A contract between a Board of County Commissioners and an individual under which the latter agreed to furnish the Board information which would enable the placing of a large amount of property on the assessment roll which had escaped taxation is one which affects the public welfare beneficially, not adversely, and is therefore not void as against public policy. Simpson v. Silver Bow County, 87 M 83, 285 P 195 (1930).

Determination of Fees by Probate Judge Not Contrary to Public Policy: A contract between an attorney and the administratrix, under which the amount of the fees to which the former should be entitled for services rendered to the latter in her representative capacity, was to be determined by the judge of the probate court, was not void as against public policy on the ground that it contemplated the doing of an extrajudicial or unlawful act by the judge. Fitzgerald v. Eisenhauer, 62 M 582, 206 P 685 (1922).

Contract to Influence Legal Process: A contract between an attorney and one convicted of the crime of introducing intoxicating liquors on an Indian reservation, under which the former should use his personal influence and friendship with a U.S. District Attorney to secure from the latter a recommendation for the convict's pardon, was void as against public policy, the facts that unlawful means in carrying out the contract were not resorted to or contemplated and that no injustice resulted to anyone from the execution of the contract being immaterial. Spaulding v. Maillet, 57 M 318, 188 P 377 (1920).

Exemption From Liability: A provision in a contract to exempt another from liability for violation of law is void as contrary to public policy. Since the provision was not severable, the entire contract was void. Cooper v. N. Pac. Ry., 212 F 533 (D.C. Mont. 1914).

Future Possible Violation of Public Policy Disregarded: A court of equity will not lend its aid to carrying the object of an illegal contract into effect; neither will it declare an agreement which is fair and just as between the parties and under a specific enforcement of which each party will receive what he agreed he should receive void as against public policy because at the time of its execution one of the parties claimed that by virtue of its terms he would be enabled to defraud a third party. Murray v. White, 42 M 423, 113 P 754 (1910).

VIOLATION OF MORALS

When Equity Will Uphold Separation Agreement Made Prior to Divorce: The husband, prior to divorce, had entered into a separation agreement under which he agreed to pay his wife a monthly sum, and thereafter she brought suit to enforce payment thereof. He alleged in his answer that the agreement was executed collusively in aid of the subsequent divorce and was therefore void as against public policy. Because the answer did not state a defense under prior holdings of the court, the court granted the wife judgment on the pleadings under the rule of equity that he could not accept the benefits and shirk the burdens, particularly where she relinquished her property rights. Ryan v. Ryan, 111 M 104, 106 P2d 337 (1940).

Contract Suppressing Investigation of Criminal Offense Illegal: A contract which tends to suppress the investigation of a criminal offense is illegal, even though it does not amount to compounding of a felony, for the reason that it is contrary to good morals and public policy. Portland Cattle Loan Co. v. Featherly, 74 M 531, 241 P 322 (1925).

MISCELLANEOUS

Arbitration Requirement Not Void or Unconscionable Under Circumstances: A former financial advisor sought to have an arbitration agreement set aside under theories of lack of mutuality, lack of explicit waiver of Montana constitutional rights, and unconscionability. Upon review of the case and after extensive discussion of its circumstances, the Supreme Court disagreed with all such contentions. Bucy v. Edward Jones & Co., 2019 MT 173, 396 Mont. 408, 445 P.3d 812.

Insurance Company Indemnification Agreement Valid — Partial Summary Judgment on Pleadings Proper: The District Court did not err in granting partial summary judgment on the pleadings to a plaintiff insurance company. The District Court properly limited its decision on partial summary judgment to the issue of whether the indemnity agreements allowed the plaintiff to seek indemnity for appropriate expenses while reserving the issue of damages and the amount of damages for the trier of fact. Moreover, the indemnity agreements did not violate 28-2-701 and 28-2-702 because they did not provide the plaintiff with carte blanche indemnification and the defendant insured was not required to indemnify the plaintiff for any illegal actions. Ohio Farmers Ins. Co. v. Jem Contracting, Inc., 2016 MT 343, 386 Mont. 49, 386 P.3d 613.

Severance Agreement Legal — Violation of Employer's Policy Not Violation of Law: The plaintiff and her former employer, the Department of Military Affairs, entered into a severance agreement in which the Department agreed to lay off the plaintiff instead of terminating her in exchange for her releasing any claims she had against the Department. Months later, the plaintiff sued to have the agreement rescinded, claiming that the agreement violated the Department's reduction in force policy and was therefore unlawful. The District Court granted summary judgment to the Department. On appeal, the Supreme Court affirmed, holding that even if the agreement violated the Department's reduction in force policy, the policy was not law. Fenwick v. St., 2016 MT 80, 383 Mont. 151, 369 P.3d 1011.

Defective Trust Indenture: The trust indenture in this case is a defective trust indenture which will be enforced between the parties as an equitable lien, but the lien of such defective trust indenture is subordinate to the claims of subsequent encumbrancers and of judgment creditors who extended credit subsequent to the date of the instrument without actual knowledge of the existence of the indenture. Amsterdam Lumber, Inc. v. Dyksterhouse, 179 M 133, 586 P2d 705 (1978).

Failure of Corporation to Possess Articles of Incorporation: Failure of a corporation to possess articles of incorporation until 21 days after the execution of the contract with the state does not constitute an illegal purpose which would void the agreement from its inception. On the contrary, this defect rendered the contract voidable at the state's option. Mont. Ass'n of Underwriters v. Dept. of Admin., 172 M 211, 563 P2d 577 (1977).

Exception to Illegal Contracts — Enforceability: While generally a party to an illegal contract will not be permitted to enforce it, an exception uniformly accepted by the courts is that where refusal to enforce would produce a harmful effect on parties for whose protection the law making the transaction illegal was enacted, enforcement is allowed. Fergus County v. Osweiler, 107 M 466, 86 P2d 410, 120 ALR 1457 (1938).

One Unlawful Act — Entire Contract Void Where Single Consideration: Where there is but a single consideration passing for the performance of several separate and distinct acts, one of which is unlawful, the entire contract, it not being severable, is void, particularly where it is wholly executory. In re Cummings' Estate, 89 M 405, 298 P 350 (1931).

Failure to Perform Legal Duty: A failure to perform an act imposed by law as an absolute duty is an unlawful omission. Conway v. Monidah Trust, 47 M 269, 132 P 26 (1913).

County Printing Contract: A contract for county printing for the 2 succeeding years made by a Board of County Commissioners a few weeks before the expiration of its term of office and upon the expiration of a prior contract is valid in the absence of fraud or bad faith in the making. Picket Pub. Co. v. Bd. of County Comm'rs, 36 M 188, 92 P 524 (1907).

Contract Limiting Liability for Loss of Baggage Valid: A contract by a railway company with a passenger, limiting the liability of the carrier to $100 for loss of baggage, is valid. Rose v. N. Pac. Ry. Co., 35 M 70, 88 P 767 (1907).

28-2-702. Contracts that violate policy of law — exemption from responsibility — exception.

Compiler's Comments

2015 Amendment: Chapter 410 at beginning inserted exception clause; and made minor changes in style. Amendment effective May 5, 2015.

Preamble: The preamble attached to Ch. 410, L. 2015, provided: "WHEREAS, the citizens of Montana and visitors to this state should enjoy the maximum ability to participate in sports or recreational opportunities; and

WHEREAS, public, private, and nonprofit entities that provide sports or recreational opportunities to citizens and visitors to this state need and deserve a measure of protection against lawsuits; and

WHEREAS, citizens and visitors to this state have a fundamental right and responsibility to make decisions concerning the activities in which they participate and the contracts and agreements in which they desire to enter; and

WHEREAS, individuals are accustomed to making conscious choices on their own behalf regarding the benefits and risks of various activities that are available; and

WHEREAS, such choices, when voluntarily made upon consideration of appropriate information, should not be ignored, but should be afforded the same value and legal effect as other choices and contractual obligations; and

WHEREAS, prospective liability waivers and releases encourage the availability and affordability of sports and recreational opportunities to citizens and visitors; and

WHEREAS, the Legislature intends to encourage the continued availability of sports or recreational opportunities in this state by shielding providers of such activities from claims resulting from conduct that constitutes ordinary negligence or for risks that are inherent in the sport or recreational opportunity; and

WHEREAS, the Legislature does not intend for liability waivers and releases to be used in a manner that would allow a person to waive or release claims for willful, wanton, reckless, or grossly negligent acts or omissions."

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Contract Limiting Liability Between Businesses — Enforceable: A contract containing a clause that limits liability, rather than eliminates liability, between two business entities that have equal bargaining power does not violate this section. Zirkelbach Constr., Inc. v. Dowl, LLC, 2017 MT 238, 389 Mont. 8, 402 P.3d 1244.

Insurance Company Indemnification Agreement Valid — Partial Summary Judgment on Pleadings Proper: The District Court did not err in granting partial summary judgment on the pleadings to a plaintiff insurance company. The District Court properly limited its decision on partial summary judgment to the issue of whether the indemnity agreements allowed the plaintiff to seek indemnity for appropriate expenses while reserving the issue of damages and the amount of damages for the trier of fact. Moreover, the indemnity agreements did not violate 28-2-701 and 28-2-702 because they did not provide the plaintiff with carte blanche indemnification and the defendant insured was not required to indemnify the plaintiff for any illegal actions. Ohio Farmers Ins. Co. v. Jem Contracting, Inc., 2016 MT 343, 386 Mont. 49, 386 P.3d 613.

Indemnity Agreement Redundant of Protection Afforded by Contributory Negligence: Langemo had an agreement with Montana Rail Link and Burlington Northern Santa Fe Railroad to establish access via a private railroad crossing to Langemo's property. After Langemo was injured at the crossing, the railroads counterclaimed against Langemo for indemnification pursuant to the private crossing agreement. The District Court held that although this section precluded the railroads from being indemnified for their own negligence, the indemnity agreement was enforceable as applied to Langemo's negligent acts or omissions and allowed the railroads to enforce their indemnity claim at the same time that they claimed the right to a reduction in Langemo's damage award based on contributory negligence. The Supreme Court reversed, concluding that the indemnity agreement was redundant of the protection afforded by the contributory negligence statute. Langemo's recovery would already be reduced by any negligence attributable to Langemo, so the railroads could not rely on additional protection from the indemnity agreement. Langemo v. Mont. Rail Link, Inc., 2001 MT 273, 307 M 293, 38 P3d 782 (2001).

Liability Exemption Distinguished From Contractual Indemnification: Liss had a homeowner's policy with Safeco Insurance Co. (Safeco) that covered personal liability and medical payments to others. Liss shot Bruthers and claimed that it was an accident and that she was involuntarily intoxicated, but she was nevertheless convicted of aggravated assault after pleading nolo contendere. Bruthers was a nonresident and filed a federal action for compensation for physical injuries, emotional distress, and punitive damages, but eventually dropped the intentional tort claim. Liss gave Safeco a copy of the complaint, and Safeco provided Liss a defense under the personal liability provisions of the homeowner's policy. Safeco then filed a declaratory action, claiming that it had no duty to defend Liss in federal court or to indemnify Liss, based on its theory that: (1) Montana policy and this section forbid the contractual indemnification of an individual for intentional and illegal acts; (2) the shooting did not constitute an occurrence as defined in the policy; (3) the intentional act and illegal act exclusions barred coverage; and (4) Liss was collaterally estopped to contest the issue based on the guilty plea. Safeco's motion was granted by summary judgment based on policy provisions excluding intentional and illegal acts from personal liability coverage and the undisputed fact that Liss pleaded guilty to aggravated assault. Both Liss and Bruthers appealed. The Supreme Court noted that a contract whose object is to exempt a person from future potential liability is clearly distinguishable from an insurance contract that indemnifies a person for another party's damages once liability is imposed. Therefore, Safeco's duty to defend and indemnify Liss could not be excused by a declaratory judgment based on public policy in this section. The question of whether the shooting incident constituted an insurable occurrence or accident remained shrouded in material facts and was inappropriate grounds for summary judgment. The shooting did not fall within the nexus of the per se intentional act case law, absent an admission or substantial evidence establishing the intent of the insured. Lastly, Safeco presented no evidence other than Liss's guilty plea to satisfy its burden of proof that Liss either intentionally shot Bruthers or that the shooting was an illegal act, so the Supreme Court addressed whether a nolo contendere guilty plea in a criminal matter is conclusive proof of intent or illegality and precludes relitigation of the issues in a subsequent civil proceeding. The court applied the three-part collateral estoppel rule in Teitelbaum Furs, Inc. v. Dominion Ins. Co., 375 P2d 439 (Calif. 1962), and Aetna Life & Cas. Ins. Co. v. Johnson, 207 M 409, 673 P2d 1277 (1984), the second prong of which requires a final judgment on the merits. A guilty plea as a matter of law fails the test because a guilty plea does not constitute a final judgment, so in this case, the plea to aggravated assault carried no collateral estoppel effect in the subsequent civil proceedings. Summary judgment was improper, and the case was remanded. Safeco Ins. Co. of America v. Liss, 2000 MT 380, 303 M 519, 16 P3d 399, 57 St. Rep. 1621 (2000).

Certified Questions — Settlement or Judgment Not Required as Precondition to Action Against Insurer — Unfair Claims Settlement Practices Action Not Barred by Terms of Policy: In an original proceeding pursuant to former Rule 44, M.R.App.P. (now superseded), the Supreme

Court responded to two certified questions from the Ninth Circuit Court of Appeals and held that an insured need not pursue the underlying claim to the point of settlement or judgment before bringing an action against the insurer under the unfair claims settlement practices statutes codified in Title 33, ch. 18. This was true, notwithstanding a "no action" clause in the insurance policy, because the clause was contrary to public policy. The Supreme Court also held that the insured was not barred by the "no action" clause of the policy from bringing an action under the unfair claims settlement practices statutes when the company did not object to direct settlement between the plaintiff and insured in the underlying action and when the insurer contributed the policy limits to that settlement. Peris v. Safeco Ins. Co., 276 M 486, 916 P2d 780, 53 St. Rep. 481 (1996).

Pre-Injury Release Form: The trial court committed reversible error by granting summary judgment to defendant employer on the basis of a pre-injury release form signed by the plaintiff. The fact the waiver is a private contract is not determinative in this case. Such waiver is invalid and violates public policy if it seeks to exempt one from liability for those actions specified in 28-2-702. Miller v. Fallon County, 222 M 214, 721 P2d 342, 43 St. Rep. 1185 (1986).

Release and Subrogation as Single, Nonseverable Contract: Plaintiff was severely burned after a truck driven by an employee of H. Pierce Manufacturing Co. ran into the rear of her 1970 Ford Mustang, which caught fire. Plaintiff retained James Reno to represent her. Reno began negotiations with Pierce's insurer, St. Paul Fire and Marine Co. At the time Pierce was insured with St. Paul for up to $100,000 and with an excess carrier, Atlantic Co., for up to $2 million. Reno did not inquire as to what the excess carrier's coverage limits were. Reno and the adjuster agreed to a settlement entered by plaintiff for $300,000. Two separate documents consisting of the combined release and indemnification agreements and a subrogation agreement were executed. Reno agreed with the insurers to also pursue their interests against Ford. The insurers later retained independent counsel, and Reno filed an action against Ford. Ford sought to have the subrogation provision declared invalid. The release and subrogation agreements were so indivisible as to prevent enforcing one without the other, since both were offered in consideration of the settlement, and there was no way to allocate the settlement among the release, indemnification, and subrogation portions of the contract. Voiding the subrogation agreement requires voiding the entire release agreement. Abell v. Ford Motor Co., 39 St. Rep. 1347 (D.C. Mont. 1982) (apparently not reported in Federal Supplement).

Subrogation Agreement Void: Plaintiff was severely burned after a truck driven by an employee of H. Pierce Manufacturing Co. ran into the rear of her 1970 Ford Mustang, which caught fire. Plaintiff retained James Reno to represent her. Reno began negotiations with Pierce's insurer, St. Paul Fire and Marine Co. At the time Pierce was insured with St. Paul for up to $100,000 and with an excess carrier, Atlantic Co., for up to $2 million. Reno did not inquire as to what the excess carrier's coverage limits were. Reno and the adjuster agreed to a settlement entered by plaintiff for $300,000. Two separate documents consisting of the combined release and indemnification agreements and a subrogation agreement were executed. Reno agreed with the insurers to also pursue their interests against Ford. The insurers later retained independent counsel, and Reno filed an action against Ford. Ford contended the release agreement was champertous. Champerty occurs when a person who is without interest in a suit intrudes into litigation by agreeing to defray the expenses of the suit in consideration of a share of the recovery. Memos and letters of the adjusters and the insurance personnel reveal clearly that both the insurers and Reno contemplated using the settlement to launch a lawsuit against Ford. The subrogation agreement was an attempt by the insurers to avoid their own liability. It is champertous, against public policy, and void. Abell v. Ford Motor Co., 39 St. Rep. 1347 (D.C. Mont. 1982) (apparently not reported in Federal Supplement).

Workers' Compensation: The exclusionary clause in 39-71-411 of the Workers' Compensation Act, as part of virtually all employment contracts in the state, is not a contract prohibited by this section. Great W. Sugar Co. v. District Court, 188 M 1, 610 P2d 717 (1980).

Specific Indemnity Clause in Lease: A specific indemnity clause in a lease agreement between a railroad and a lessee, which clause provided that the lessee would indemnify the railroad for claims "whether due or not due to the negligence" of the railroad, was not invalid as applied to the allegations in a complaint by a person seeking recovery from the railroad for injuries allegedly received because of a violation by the railroad of 69-14-562 (now repealed), making it a misdemeanor for a railroad to permit a locomotive to approach a crossing without giving a proper warning. Ryan Mercantile Co. v. Great N. Ry., 186 F. Supp. 660 (D.C. Mont. 1960), affirmed in Ryan Mercantile Co. v. Great N. Ry., 294 F2d 629 (9th Cir. 1961).

Exception — Where Illegal Contract Enforceable: Where refusal to enforce an illegal contract would have harmed the parties for whose protection the law was enacted, in this case the taxpayers, enforcement was allowed where the County Commissioners allowed a bondsman to execute a note to postpone his payment under a depository bond securing county funds in an insolvent bank, in violation of Art. V, sec. 39, 1889 Mont. Const. (similar to Art. II, sec. 31, 1972 Mont. Const.), and the county could enforce payment of the note. Fergus County v. Osweiler, 107 M 466, 86 P2d 410 (1938), distinguished in McFarland v. Stillwater County, 109 M 544, 98 P2d 321 (1940).

Strict Construction of Terms: The parties to a bailment may diminish the liability of the bailee by special contract, the principle being that the bailee may impose whatever terms he chooses if he gives the bailor notice that there are special terms and the means of knowing what they are; and if the bailor chooses to make the bailment, he is bound by them, provided the contract is not in violation of law or public policy, and that it stops short of protection in cases of fraud or negligence of the bailee, and provided further that the terms of the contract are clear, such stipulations being strictly construed. Jones v. Great N. Ry., 67 M 231, 217 P 673, 37 ALR 754 (1923).

Limitation of Actions: A stipulation by a telegraph company, on one of its blanks, that it will not be answerable for damages or statutory penalties if a claim is not made within a specified time, is void under this section as against public policy, if it was ever intended as a cloak for fraud or crime. Lahood v. Cont. Tel. Co., 52 M 313, 157 P 639 (1916).

Exemption From Liability: A provision in a contract to exempt another from liability for violation of law is void as contrary to public policy. Since the provision was not severable, the entire contract was void. Cooper v. N. Pac. Ry., 212 F 533 (D.C. Mont. 1914).

Assumption of Risk: The defense of assumption of risk, which has for its basis the common-law principle expressed by the maxim "Volenti non fit injuria" and does not rest in contract between the master and servant, is not abrogated by this section and 39-2-705. Osterholm v. Boston & Mont. Consol. Copper & Silver Min. Co., 40 M 508, 107 P 499 (1910). See also Garrison v. Averill, 282 M 508, 938 P2d 702, 54 St. Rep. 454 (1997).

Attorney General's Opinions

Termination of Payments in Lieu of Participation in Group Health Plan for Nonunion County Employee: The Board of County Commissioners may terminate payments in lieu of participation in a group health plan for a nonunion county employee only if termination is consistent with the county's employment agreement with the employee. 51 A.G. Op. 11 (2005).

28-2-703. Contracts in restraint of trade generally void.

Case Notes

Covenant Not to Compete Enforceable — Remand for Dobbins Analysis: The plaintiff, an accounting firm, sued the defendants, former shareholders of a satellite office, after they established a new accounting firm and took most of the plaintiff's clients. The plaintiff sought to enforce a covenant not to compete found in an employment agreement each of the defendants had signed. The District Court granted the defendants summary judgment, concluding that the agreement was not enforceable because it did not provide a method for compensation and that it was a contract of adhesion. On appeal, the Supreme Court reversed, concluding that the contract was enforceable because it provided sufficient consideration and that the defendants, who were shareholders of the accounting firm at the time the parties entered into the agreement, had a bargaining position such that the agreement did not constitute a contract of adhesion. The Supreme Court remanded the matter for the District Court to apply the Dobbins analysis to determine whether the covenant not to compete was reasonable. Junkermier v. Alborn, 2016 MT 218, 384 Mont. 464, 380 P.3d 747.

Covenant Not to Compete — Unenforceable When Employer Terminates Employment Relationship Absent Legitimate Business Interest: An accounting firm chose not to renew a contract with the plaintiff, a long-term employee, and later attempted to enforce a covenant not to compete against her. The District Court concluded that the covenant not to compete was reasonable and enforceable, and the plaintiff appealed. The Supreme Court reversed the District Court and adopted the requirement that an employer must establish a legitimate business interest in order to enforce a covenant not to compete. A legitimate business interest, the Supreme Court expounded, is one necessary to protect an employer's good will, customer relationships, or trade information. Because the firm chose to terminate the relationship and the covenant did not protect a legitimate business interest, the covenant was not enforceable. Wrigg v. Junkermier, Clark, Campanella, Stevens, P.C., 2011 MT 290, 362 Mont. 496, 265 P.3d 646.

Reasonableness of Noncompetition Covenant Subject to Determination at Trial: A noncompetition covenant contained in a partnership agreement did not constitute an absolute prohibition on the right of dissociating partners to engage in their professions, but rather provided for a reduced payment to separating partners who practice in the area where the partnership practiced. The District Court granted summary judgment in favor of dissociating partners on grounds that the covenant was void as a matter of law, but on appeal the Supreme Court reversed. Because the prohibition was not absolute, the court held that the reasonableness of the noncompetition covenant should be tested at trial under the criteria in Dobbins, Deguire & Tucker, P.C. v. Rutherford, 218 M 392, 708 P2d 577 (1985), and summary judgment was therefore inappropriate. Mungas v. Great Falls Clinic, LLP, 2009 MT 426, 354 M 50, 221 P3d 1230 (2009).

Signing of Separation Agreements and Acceptance of Payments Precluding Obligation for Further Payments: Several physicians signed separation agreements when terminating employment with a medical clinic. The agreements provided that the physicians expressly accepted payments representing a reduced amount of profits, stock, and partnership interest and that the payments called for by the agreements constituted the full amount payable by the clinic. The physicians later asserted that the provision in the agreement reducing payments was void or unreasonable. The Supreme Court disagreed. Pursuant to 28-1-1403, any obligation of the clinic to pay more was extinguished when the physicians accepted the terms of the separation agreement. Mungas v. Great Falls Clinic, LLP, 2009 MT 426, 354 M 50, 221 P3d 1230 (2009).

Noncompetition Agreement Unenforceable for Lack of Consideration: Four months after beginning employment with plaintiff produce company, Hernandez signed a noncompetition agreement and a nondisclosure agreement providing that Hernandez would not directly or indirectly compete with plaintiff company during employment and for a 2-year period following termination of employment. When the company began experiencing financial difficulties, Hernandez was laid off. Hernandez then began another produce business in the area, and plaintiff filed for a restraining order seeking to enforce the noncompetition agreement and to prevent Hernandez from operating a competing business. The District Court held that the agreement was enforceable and issued a preliminary injunction restraining Hernandez from competing with plaintiff and contacting any of plaintiff's customers and from disclosing any of plaintiff's trade secrets. Hernandez appealed on grounds that the noncompetition agreement was unenforceable as a matter of law. The Supreme Court held that, in the context of noncompetition agreements, clear evidence is required that the employee received good consideration in exchange for bargaining away some postemployment freedom to practice the profession or trade of choice. Here, the District Court found that continuation of Hernandez's employment and income with plaintiff was sufficient consideration, but the Supreme Court strictly construed the agreement and disagreed. Consideration exists if an employee enters a noncompetition agreement as a condition of employment or if an existing employee receives additional independent consideration for entering a noncompetition agreement, but Hernandez signed the agreement 4 months after being hired and received no additional independent consideration for signing, and past consideration cannot serve as good consideration for a present agreement. Therefore, the covenant not to compete was unenforceable as a matter of law for lack of consideration, and it was also error for the District Court to enter the preliminary injunction. The District Court was reversed. Access Organics, Inc., v. Hernandez, 2008 MT 4, 341 M 73, 175 P3d 899 (2008), distinguishing In re Wage Claim of Langager v. Crazy Creek Products, Inc., 1998 MT 44, 287 M 445, 954 P2d 1169 (1998).

Covenant Not to Compete Unlawful Restraint on Trade — No Claim for Interference With Contractual or Business Relations: Curl worked for a company that finished products for Montana Silversmiths. The company was purchased by plaintiff company, and plaintiff hired Curl to do the same work but required Curl to sign an employment contract that included a noncompetition covenant. After Curl's employment ended, a new business hired Curl to do the same work for Montana Silversmiths. Plaintiff sued the new business and Curl, claiming breach of contract and intentional interference with business relations based on the noncompetition covenant. The District Court granted summary judgment for Curl, and plaintiff appealed. The Supreme Court applied the reasonableness test outlined in O'Neil v. Ferraro, 182 M 214, 596 P2d 197 (1979), and concluded that because Curl's only option was to work in the vicinity of her residence as a subcontractor for Montana Silversmiths, the covenant prohibited Curl from engaging in her profession and was thus unreasonable and an unlawful restraint on trade. Plaintiff's claims were based on the presumption that the covenant was valid, but because the covenant was void, summary judgment for Curl was affirmed. Mont. Mtn. Prod. v. Curl, 2005 MT 102, 327 M 7, 112 P3d 979 (2005).

Good Will Exception Applicable to Stock Sale as Well as Asset Sale: Roessmans purchased 100% of the stock in a construction company, which constituted a complete transfer and conveyance of all of Laabses' right, title, and interest in the company. The sale agreement contained a covenant not to compete, restricting Laabses from performing any construction in the area for 7 years, including construction for any prior, existing, or referred clients of the company. About 4 years later, Roessmans filed a complaint alleging that Laabses had repeatedly breached the covenant not to compete by continuing construction in the area and performing projects for prior clients. Laabses moved for summary judgment on grounds that the covenant was void because it violated public policy against restraint of trade, contending that the exception in 28-2-704 did not apply because the sale in question was a sale of stock rather than a sale of assets. Laabses asserted that shareholders do not own the good will of a business, which belongs to the corporation, and that when shares of stock are bought and sold by individuals, the good will itself is not transferred. The Supreme Court found that such an interpretation would exalt form over substance. In this context, the stock purchase agreement specifically contemplated the transfer of good will and there was no substantive difference between sale of the company stock and sale of the company's assets, so the good will exception applied to the stock sale as well as the asset sale. Snow Country Constr., Inc. v. Laabs, 1999 MT 279, 296 M 520, 989 P2d 847, 56 St. Rep. 1125 (1999). See also Earthworks, Inc. v. Sehn, 553 NW 2d 490 (N. Dak. 1996).

Reasonableness and Enforceability of Employment Contract Noncompetition Covenant: Allen sold her accounting practice to Joseph Eve & Co. (Eve). The purchase and sale agreement contained a provision pursuant to which Allen agreed not to compete with Eve for a 3-year period from the date of closing. A separate professional employment contract entered at the same time provided that Allen could work for Eve as an employee. After 3 years, Allen had the option to reacquire her client base from Eve. If she chose not to exercise the option but to still represent those clients, she agreed to reimburse Eve on a percentage basis for work performed for Eve clients for up to 3 years. After 3 years, Allen notified Eve of her intent to leave the employment and exercise the purchase option but the parties could not agree on terms. A few days later, Allen's attorney notified Eve that she had decided not to exercise the purchase option but to instead take client accounts with her and make payments pursuant to the reimbursement provision of the contract. Although Allen performed services for Eve's clients, Allen refused to make payments, so Eve sued to recover amounts allegedly due. Allen contended that Eve had breached the contract by refusing to provide her with the necessary client files. As outlined in Dobbins, Deguire & Tucker, P.C. v. Rutherford, 218 M 392, 708 P2d 577 (1985), for a covenant in restraint of trade to be reasonable, it: (1) must be limited in operation as to either time or place; (2) must be based on some good consideration; (3) should afford only a fair protection to the interests of the party in whose favor it is made; and (4) must not be so large in its operation as to interfere with the interests of the public. The trial court explicitly discussed each of the factors, held that the noncompetition clause in the contract was enforceable, and ordered partial summary judgment in favor of Eve, and the case proceeded to trial. At close of trial, the court instructed the jury that a covenant in restraint of trade may be enforced if reasonable. While it was error for the court to submit to the jury an issue already decided by the court on summary judgment, the error was harmless because the summary judgment did not address the ultimate questions of either party's liability or the enforceability against either party, which were left to the jury. Joseph Eve & Co. v. Allen, 1998 MT 189, 290 M 175, 964 P2d 11, 55 St. Rep. 767 (1998). However, see Wrigg v. Junkermier, Clark, Campanella, Stevens, P.C., 2011 MT 290, 362 Mont. 496, 265 P.3d 646, requiring an employer to establish a legitimate business interest in order to enforce a covenant not to compete.

Covenant Not Limited as to Time and Geographical Area as Unreasonable Restraint of Trade: The covenant in a contract forbade employees from disclosing customer lists and trade secrets for an unlimited period of time and covered an unrestricted geographical area. The Supreme Court ruled that the covenant was an unreasonable restraint of trade and unenforceable as a matter of law. St. Medical Oxygen & Supply, Inc. v. Am. Medical Oxygen Co., 240 M 70, 782 P2d 1272, 46 St. Rep. 1951 (1989).

Prohibition Against Restraint of Trade — Applies to All Contracts: The employer argued that the statute prohibiting restraint of trade did not apply to restrictive covenants in the contract before the District Court because the contract was not an employment contract. The Supreme Court, in affirming the lower court, ruled that the statute applied to all contracts regardless of subject matter. St. Medical Oxygen & Supply, Inc. v. Am. Medical Oxygen Co., 240 M 70, 782 P2d 1272, 46 St. Rep. 1951 (1989).

Covenant Against Competition Valid: A covenant restricting the seller of a radio station from any involvement with a radio or television station within 50 miles of Bozeman for a period of 10 years was not found to be void as an unlawful restraint of trade. W. Media, Inc. v. Merrick, 224 M 28, 727 P2d 547, 43 St. Rep. 1991 (1986).

Limited Commercial Use Restriction on Parking Lot: The Supreme Court determined that there was a commercial use restriction on a Bridger Bowl ski area parking lot. Appellants argued that the restriction acted to prohibit use of the parking lot by customers who bought beer and wine on other Bridger Bowl lands. The court noted that the primary purpose of the parking lot was to provide parking for skiers using the ski hill, that the land was conveyed to respondents for that purpose, and that the parking lot was not being used primarily by commercial business patrons. The court refused to construe the fact that skiers using the lot might incidentally buy beer or wine in ski area chalets as violative of the commercial use restriction on the parking lot. Haggerty v. Gallatin County, 221 M 109, 717 P2d 550, 43 St. Rep. 674 (1986).

Properly Created Negative Easements Not Automatically Void: Appellants contended the District Court erred in concluding that the commercial use limitation on Bridger Bowl land was void as an unlawful restraint of trade. The Supreme Court agreed and reversed the District Court, finding that the conditions of the test outlined in O'Neil v. Ferraro, 182 M 214, 596 P2d 197 (1979), had been met. Additionally, the Supreme Court noted the statutory authority in 70-17-101 for allowing creation of covenants and easements governing the right to transact business on land and held that properly created negative easements are not automatically void under 28-2-703. Haggerty v. Gallatin County, 221 M 109, 717 P2d 550, 43 St. Rep. 674 (1986).

Public Accountants — Employment Contract With Reasonable Restrictive Covenants Relating to Postemployment Relationship: An employment contract for accountants contained a restriction that upon termination of employment the defendants must pay a fee if they obtained any of plaintiff's clients within 12 months. The fee was to be 100% of gross fees payable in installments over a 3-year period at 8% interest. The trial court erred in dismissing plaintiff's complaint for an accounting and payment based on the restriction as an unlawful restraint of trade. The Supreme Court held that the restrictions did not on their face either prohibit or directly restrain the business of public accounting. The court provided the following guidelines for determining whether a covenant is a reasonable restraint on the profession of public accounting: (1) the covenant should be limited either as to time or place; (2) the covenant should be based upon some good consideration; and (3) the covenant should afford a reasonable protection for and not impose an unreasonable burden on the employer, the employee, or the public. Dobbins, DeGuire & Tucker, P.C. v. Rutherford, MacDonald & Olson, 218 M 392, 708 P2d 577, 42 St. Rep. 1680 (1985). These guidelines were applied in Daniels v. Thomas, Dean & Hoskins, Inc., 246 M 125, 804 P2d 359, 47 St. Rep. 2293 (1990), and Joseph Eve & Co. v. Allen, 1998 MT 189, 290 M 175, 964 P2d 11, 55 St. Rep. 767 (1998). However, see Wrigg v. Junkermier, Clark, Campanella, Stevens, P.C., 2011 MT 290, 362 Mont. 496, 265 P.3d 646, requiring an employer to establish a legitimate business interest in order to enforce a covenant not to compete.

Violation of Employer's Confidence: Defendant, a clerical worker for plaintiff, became licensed as an insurance agent at plaintiff's urging in 1979. She was assigned a book of business customers to service in exchange for a guaranteed salary. She signed an employment contract which contained a covenant not to compete and a covenant not to disclose. Defendant terminated her employment and opened her own insurance business. Plaintiff filed a complaint seeking injunctive relief, alleging defendant had violated both covenants and had in her possession a confidential customer list. The covenant not to compete was void as a violation of 28-2-703. Plaintiff had the burden of proving that the covenant not to disclose did not also violate 28-2-703. No evidence was presented showing that defendant had retained any records or lists. The general rule is that an employee, having left his employment, is free to make use of his experience, as long as he does not violate his employer's confidence. First Am. Ins. Agency v. Gould, 203 M 217, 661 P2d 451, 40 St. Rep. 402 (1983).

Negative Easement Not a Restraint of Trade: A written agreement in the form of a settlement agreement that creates a negative easement prohibiting the use of property as a restaurant and bar does not constitute a contract in restraint of trade. The agreement is not merely a personal contract between the parties that would fall within the scope of this section, prohibiting restraint of trade, but rather creates a property interest that runs with the land. Reichert v. Weeden, 190 M 95, 618 P2d 1216, 37 St. Rep. 1788 (1980), followed in Haggerty v. Gallatin County, 221 M 109, 717 P2d 550, 43 St. Rep. 674 (1986).

Alleged Oral Covenant Not to Compete: The sellers and buyers of a grocery business discussed a noncompetition agreement, but excluded such a provision from the written contract. The trial court found that this omission was not induced by sellers' fraud. Even if the alleged noncompetition agreement had been entered in the contract, it could not be enforced because although the two businesses are only 7 miles apart, they are in different counties (prior to 1983 amendment of 28-2-704) and therefore not within the permissible exceptions for contracts in restraint of competition. Lar-Con Corp. v. Murman Properties, Ltd., 188 M 183, 612 P2d 676 (1980).

Covenant Not to Compete: A covenant not to compete contained in a dissolution of partnership agreement stated that defendant, Sullivan, would refrain from competing with plaintiff in any area where the partnership had done business. The covenant was to be effective for 3 years. Plaintiff sued to enforce this covenant for an area encompassing 32 counties, but it was in contravention of the applicable statutes which limit such covenants to a single city or town (prior to 1983 amendment of 28-2-704). Therefore, the covenant was enforceable only as to business transacted within the city of Billings. Treasure Chem., Inc. v. Team Laboratory Chem. Corp., 187 M 200, 609 P2d 285 (1980).

Restrictive Covenant — Test of Validity: Plaintiff operates a restaurant in part of a building owned by the defendant. The lease between plaintiff and defendant contains a covenant which provides that the defendant will not permit a competing restaurant to operate in the building. Such a covenant is valid only if it is a reasonable and limited restraint of trade. This covenant meets the test and is therefore valid. O'Neill v. Ferraro, 182 M 214, 596 P2d 197 (1979).

Employment Agreement — Restrictive Covenant: A restrictive covenant contained in an employment agreement between plaintiffs and defendants was not enforceable under Montana law as long as the defendant did not violate his employer's confidence. J.T. Miller Co. v. Madel, 176 M 49, 575 P2d 1321 (1978), limited and explained in Dobbins, DeGuire & Tucker, P.C. v. Rutherford, MacDonald & Olson, 218 M 392, 708 P2d 577, 42 St. Rep. 1680 (1985). However, see Wrigg v. Junkermier, Clark, Campanella, Stevens, P.C., 2011 MT 290, 362 Mont. 496, 265 P.3d 646, requiring an employer to establish a legitimate business interest in order to enforce a covenant not to compete.

Covenant Not to Compete — Restraint of Trade: A covenant not to compete is a restrictive covenant in restraint of trade and is valid only if it constitutes a reasonable restriction on the freedom to do business within the provisions of 28-2-704 and 28-2-705. Jenson v. Olson, 144 M 224, 395 P2d 465 (1964).

Marketing Contract: Plaintiffs in an action seeking the forfeiture of an oil and gas lease, on the ground, among others, that the lessee failed to fulfill the provision of the lease making it its duty to market the gas found, could properly urge that a contract entered into by the lessee with a natural gas company under which the former bound itself not to sell gas to others within a certain market was invalid as creating a monopoly contrary to the provisions of Art. XV, sec. 20, 1889 Mont. Const. (similar to Art. II, sec. 31, 1972 Mont. Const.), and this section. Stranahan v. Independent Natural Gas Co., 98 M 597, 41 P2d 39 (1935).

Common-Law Statute:

This section is not a novel statute; it is but declaratory of the common law. Schwanekamp v. Modern Woodmen of Am., 44 M 526, 120 P 806 (1912).

A statute of this character refers only to a contract which, by its terms, restrains a party to it from exercising a lawful business, and the breach of which subjects the delinquent to liability. Schwanekamp v. Modern Woodmen of Am., 44 M 526, 120 P 806 (1912).

Fraternal Benefit Insurance: A clause in the contract of insurance entered into between a member of a fraternal society and the association, that the certificate of insurance should be void if the insured engaged in the sale of intoxicating liquor in any capacity, is not in violation of the provisions of this section. Schwanekamp v. Modern Woodmen of Am., 44 M 526, 120 P 806 (1912).

Law Review Articles

The Post-Employment Covenant Not to Compete: An Old Dog Doing a New Trick, Watt, 49 Mont. L. Rev. 353 (1988).

Montana's Law Regarding Contracts in Restraint of Trade, Cain, 30 Mont. L. Rev. 185 (1969).

28-2-704. Exception — sale of goodwill of business.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

1983 Amendment: In (1), after "business within" substituted "the areas provided in subsection (2)" for "a specified county, city, or part thereof"; and inserted (2) stating geographical limitations on agreement.

Case Notes

Noncompete Clause of 5 Years and 100 Miles Upheld: When the sale of a business includes sale of goodwill, the seller may agree to refrain from carrying on a similar business. In this case, because the noncompete clause was upheld by the District Court, it is likely that the plaintiffs will ultimately prevail and that the contract and the noncompete clause will be determined to be valid and enforceable. The likelihood of success is sufficient to warrant the preliminary injunction. Friedman v. Lasco, 2016 MT 115, 383 Mont. 381, 372 P.3d 451.

Goodwill Exception Not Applicable When No Sale Occurs Under Partnership Agreement: Several physicians signed separation agreements when terminating employment with a medical clinic. The agreements provided that the physicians expressly accepted payments representing a reduced amount of profits, stock, and partnership interest and that the payments called for by the agreements constituted the full amount payable by the clinic. The clinic argued that the forfeiture provision in the agreements constituted the sale of goodwill of a business and therefore fell within the provisions of 28-2-704 and could not be considered a restraint of trade. The District Court held that the goodwill exception did not apply, and on appeal the Supreme Court agreed. In this case there was no payment or agreement to pay a pecuniary consideration in exchange for the transfer of an interest in property, so no sale occurred, and absent a sale the exception to the prohibition on contracts in restraint of trade did not apply to the partnership agreement at issue. Mungas v. Great Falls Clinic, LLP, 2009 MT 426, 354 M 50, 221 P3d 1230 (2009).

Reasonableness of Noncompetition Covenant Subject to Determination at Trial: A noncompetition covenant contained in a partnership agreement did not constitute an absolute prohibition on the right of dissociating partners to engage in their professions, but rather provided for a reduced payment to separating partners who practice in the area where the partnership practiced. The District Court granted summary judgment in favor of dissociating partners on grounds that the covenant was void as a matter of law, but on appeal the Supreme Court reversed. Because the prohibition was not absolute, the court held that the reasonableness of the noncompetition covenant should be tested at trial under the criteria in Dobbins, Deguire & Tucker, P.C. v. Rutherford, 218 M 392, 708 P2d 577 (1985), and summary judgment was therefore inappropriate. Mungas v. Great Falls Clinic, LLP, 2009 MT 426, 354 M 50, 221 P3d 1230 (2009).

Covenant Not to Compete Unlawful Restraint on Trade — No Claim for Interference With Contractual or Business Relations: Curl worked for a company that finished products for Montana Silversmiths. The company was purchased by plaintiff company, and plaintiff hired Curl to do the same work but required Curl to sign an employment contract that included a noncompetition covenant. After Curl's employment ended, a new business hired Curl to do the same work for Montana Silversmiths. Plaintiff sued the new business and Curl, claiming breach of contract and intentional interference with business relations based on the noncompetition covenant. The District Court granted summary judgment for Curl, and plaintiff appealed. The Supreme Court applied the reasonableness test outlined in O'Neil v. Ferraro, 182 M 214, 596 P2d 197 (1979), and concluded that because Curl's only option was to work in the vicinity of her residence as a subcontractor for Montana Silversmiths, the covenant prohibited Curl from engaging in her profession and was thus unreasonable and an unlawful restraint on trade. Plaintiff's claims were based on the presumption that the covenant was valid, but because the covenant was void, summary judgment for Curl was affirmed. Mont. Mtn. Prod. v. Curl, 2005 MT 102, 327 M 7, 112 P3d 979 (2005).

Good Will Exception Applicable to Stock Sale as Well as Asset Sale: Roessmans purchased 100% of the stock in a construction company, which constituted a complete transfer and conveyance of all of Laabses' right, title, and interest in the company. The sale agreement contained a covenant not to compete, restricting Laabses from performing any construction in the area for 7 years, including construction for any prior, existing, or referred clients of the company. About 4 years later, Roessmans filed a complaint alleging that Laabses had repeatedly breached the covenant not to compete by continuing construction in the area and performing projects for prior clients. Laabses moved for summary judgment on grounds that the covenant was void because it violated public policy against restraint of trade, contending that the exception in this section did not apply because the sale in question was a sale of stock rather than a sale of assets. Laabses asserted that shareholders do not own the good will of a business, which belongs to the corporation, and that when shares of stock are bought and sold by individuals, the good will itself is not transferred. The Supreme Court found that such an interpretation would exalt form over substance. In this context, the stock purchase agreement specifically contemplated the transfer of good will and there was no substantive difference between sale of the company stock and sale of the company's assets, so the good will exception applied to the stock sale as well as the asset sale. Snow Country

Constr., Inc. v. Laabs, 1999 MT 279, 296 M 520, 989 P2d 847, 56 St. Rep. 1125 (1999). See also Earthworks, Inc. v. Sehn, 553 NW 2d 490 (N. Dak. 1996).

Distance in Noncompetition Covenant Determined by Most Usual Mode of Travel: The parties in a suit over a noncompetition covenant disagreed on whether the 100-mile limit included or excluded Billings. The Supreme Court held that the distance was to be determined by highway mileage, not air mileage, because automobile travel is the most usual mode of travel between Lewistown and Billings. Dumont v. Tucker, 250 M 417, 822 P2d 96, 48 St. Rep. 996 (1991).

Unenforceability of Part of Noncompetition Covenant: The District Court found that part of a noncompetition covenant was void. Tucker argued that the District Court erred in not ruling that an entire noncompetition covenant was void and that he was entitled to a refund for the full amount paid for the covenant. The Supreme Court held that the District Court had properly applied the "blue pencil approach" in limiting the covenant to the contiguous counties and, in so doing, did not void the covenant in its entirety. Dumont v. Tucker, 250 M 417, 822 P2d 96, 48 St. Rep. 996 (1991).

Covenant Against Competition Valid: A covenant restricting the seller of a radio station from any involvement with a radio or television station within 50 miles of Bozeman for a period of 10 years was not found to be void as an unlawful restraint of trade. W. Media, Inc. v. Merrick, 224 M 28, 727 P2d 547, 43 St. Rep. 1991 (1986).

Alleged Oral Covenant Not to Compete: The sellers and buyers of a grocery business discussed a noncompetition agreement, but excluded such a provision from the written contract. The trial court found that this omission was not induced by sellers' fraud. Even if the alleged noncompetition agreement had been entered in the contract, it could not be enforced because although the two businesses are only 7 miles apart, they are in different counties (prior to 1983 amendment) and therefore not within the permissible exceptions for contracts in restraint of competition. Lar-Con Corp. v. Murman Properties, Ltd., 188 M 183, 612 P2d 676 (1980).

Breach of Contract — Value of Goodwill Determined: In an action for breach of a contract to sell and purchase a barbershop business, the sole issue on appeal was the proper determination of the value of goodwill attributable to the shop's location. The court found that the District Court improperly restricted the reasonable value of goodwill associated with the shop's location to a 1-month period, in light of the facts that the purchaser had obtained a long-term lease and that there was no indication that the lessor would have been unwilling to have leased to the seller on a long-term rather than a month-to-month basis. While there is no rigid rule for determining the value of goodwill, the best indicator is the purchase price agreed upon in a voluntary arm's-length transaction. The three elements comprising the purchase price in this contract were the goodwill associated with the shop's location, the seller's furniture and fixtures, and the shop's telephone connection. The seller removed the fixtures and furniture and disconnected the telephone upon learning of the purchaser's new lease arrangements. These things were valued at $3,000. The seller's recovery was therefore based on the purchase price less the $3,000. An estimate of business lost due to changing locations was then used to determine the percentage of the base price representing the shop's goodwill attached to the shop's location. Baldwin v. Stuber, 187 M 430, 610 P2d 160 (1980).

Covenant Not to Compete: A covenant not to compete contained in a dissolution of partnership agreement stated that defendant, Sullivan, would refrain from competing with plaintiff in any area where the partnership had done business. The covenant was to be effective for 3 years. Plaintiff sued to enforce this covenant for an area encompassing 32 counties, but it was in contravention of the applicable statutes which limit such covenants to a single city or town (prior to 1983 amendment). Therefore, the covenant was enforceable only as to business transacted within the city of Billings. Treasure Chem., Inc. v. Team Laboratory Chem. Corp., 187 M 200, 609 P2d 285 (1980).

Commercial Speech: Plaintiffs were guaranteed the right to advertise the availability, nature, and prices of their products and services as constitutionally protected commercial speech when the record indicated they made no agreement prohibiting advertising. Bauer v. Chaussee, 173 M 270, 567 P2d 448 (1977).

Requirement of Sale: Where articles of an unincorporated association require withdrawing members to sell whatever interest they have, including goodwill, without cost, a restrictive covenant not to compete does not fall within the sale of goodwill exception, because in order to have a sale pecuniary consideration must be given in exchange. The withdrawing members cannot sell the goodwill as it belongs to the association. W. Mont. Clinic v. Jacobson, 169 M 44, 544 P2d 807 (1976).

Restrictive Covenant Not to Compete: Covenant between partners dissolving dairy products partnership, one taking retail business, the other the wholesale business, which was to last for 9 years and was to be confined to city where partnership had been conducted, was valid as a restrictive covenant not to compete. Jenson v. Olson, 144 M 224, 395 P2d 465 (1964).

Breach by Seller: Where buyer broke contract by failing to make agreed payments for exclusive business rights in a territory and seller entered the territory after buyer's breach but in violation of the agreement, buyer was then entitled to a setoff of the amount of profit which seller took from the restricted territory when seller brought action on the full amount of the contract. Leiman-Scott, Inc. v. Holmes, 142 M 58, 381 P2d 489 (1963).

Corporate Goodwill:

It would seem that a stockholder has no interest in the goodwill of his corporation which he can sell. Wylie v. Wylie Permanent Camping Co., 57 M 115, 187 P 279 (1920).

Goodwill is an incident to and inherent in the business to which it attaches. Wylie v. Wylie Permanent Camping Co., 57 M 115, 187 P 279 (1920).

The goodwill of a corporation is an intangible asset dependent on the corporate existence; it constitutes an element of value in connection with, but not apart from, the corporation and its business. Wylie v. Wylie Permanent Camping Co., 57 M 115, 187 P 279 (1920).

Law Review Articles

The Post-Employment Covenant Not to Compete: An Old Dog Doing a New Trick, Watt, 49 Mont. L. Rev. 353 (1988).

28-2-705. Exception — dissolution of partnership.

Compiler's Comments

1983 Amendment: Substituted language allowing contracts in restraint of trade within geographical limits set forth in 28-2-704(2) for: "Partners may, upon or in anticipation of a dissolution of the partnership, agree that none of them will carry on a similar business within the same city or town where the partnership business has been transacted or within a specified part thereof."

Case Notes

Covenant Not to Compete Unlawful Restraint on Trade — No Claim for Interference With Contractual or Business Relations: Curl worked for a company that finished products for Montana Silversmiths. The company was purchased by plaintiff company, and plaintiff hired Curl to do the same work but required Curl to sign an employment contract that included a noncompetition covenant. After Curl's employment ended, a new business hired Curl to do the same work for Montana Silversmiths. Plaintiff sued the new business and Curl, claiming breach of contract and intentional interference with business relations based on the noncompetition covenant. The District Court granted summary judgment for Curl, and plaintiff appealed. The Supreme Court applied the reasonableness test outlined in O'Neil v. Ferraro, 182 M 214, 596 P2d 197 (1979), and concluded that because Curl's only option was to work in the vicinity of her residence as a subcontractor for Montana Silversmiths, the covenant prohibited Curl from engaging in her profession and was thus unreasonable and an unlawful restraint on trade. Plaintiff's claims were based on the presumption that the covenant was valid, but because the covenant was void, summary judgment for Curl was affirmed. Mont. Mtn. Prod. v. Curl, 2005 MT 102, 327 M 7, 112 P3d 979 (2005).

Covenant Not to Compete: A covenant not to compete contained in a dissolution of partnership agreement stated that defendant, Sullivan, would refrain from competing with plaintiff in any area where the partnership had done business. The covenant was to be effective for 3 years. Plaintiff sued to enforce this covenant for an area encompassing 32 counties, but it was in contravention of the applicable statutes which limit such covenants to a single city or town (prior to 1983 amendment). Therefore, the covenant was enforceable only as to business transacted within the city of Billings. Treasure Chem., Inc. v. Team Laboratory Chem, Corp., 187 M 200, 609 P2d 285 (1980).

Unincorporated Association: When articles of an unincorporated association state the relationship between members and the association shall be treated as a corporation, a restrictive covenant as to withdrawing members does not fall within partnership exception. W. Mont. Clinic v. Jacobson, 169 M 44, 544 P2d 807 (1976).

Restrictive Covenant Not to Compete: Covenant between partner dissolving dairy products partnership, one taking retail business, the other the wholesale business, which was to last for 9 years and was to be confined to city where partnership had been conducted, was valid as a restrictive covenant not to compete. Jenson v. Olson, 144 M 224, 395 P2d 465 (1964).

Law Review Articles

The Post-Employment Covenant Not to Compete: An Old Dog Doing a New Trick, Watt, 49 Mont. L. Rev. 353 (1988).

28-2-706. Contracts in restraint of marriage generally void.

Case Notes

Operation and Effect: A contract in restraint of marriage of any person other than a minor is void under this section. Sec. St. Bank v. McIntyre, 71 M 186, 228 P 618 (1924).

Law Review Articles

Contract Marriage, Invalid in Montana, Briggs, 18 Mont. L. Rev. 43 (1956).

28-2-707. What conditions void.

Case Notes

What Constitutes Impossibility: Appealing in a breach of contract case, the seller asserted a defense of impossibility attributable to harsh weather conditions at the time set for delivery. The trial court apparently found the seller did not intend to deliver until after January 1 in any case. Such a finding was supported by the following facts: the seller had been telling the buyer for some time that no delivery could be made until after January 1; the seller had been intimating an unwillingness or inability to comply with the contract for months; and the seller, in order to wean the calves for the agreed 45-day period before delivery, would have had to start weaning by October 31 in order to deliver by December 15, the extended delivery date. (The contract had called for a mid-November delivery.) October 31 was 9 days before the snow that allegedly created impossibility of performance because of an inability to round up the calves. The Supreme Court found there was adequate evidence to support the trial court's rejection of this defense. Miller v. Titeca, 192 M 357, 628 P2d 670, 38 St. Rep. 853 (1981).

Impossibility of Performance of Contract: A joint venture was formed, the contract contemplating the feeding of cattle by one party until 80% graded "choice", followed by sale and splitting of the proceeds with the supplier of the cattle, who was the second party. A drop in cattle prices which caused the feeder to lose his financing was not a case of commercial impossibility for two reasons. First, in order for commercial impossibility to excuse performance of a contract, the parties thereto must have had no reason to foresee the impossibility at the time they contracted. Fluctuation in cattle prices is foreseeable prior to the breach. On the contrary, a contract against the feeder for damages was upheld. Second, in order for commercial impossibility to excuse performance, the contractual duties must be impossible for anyone to perform. Subjective (personal) impossibility does not inhere to the nature of the act to be performed and does not excuse nonperformance. A loss of financing is personal impossibility. Roundup Cattle Feeders v. Horpestad, 184 M 480, 603 P2d 1044 (1979), distinguishing Murphy v. Redland, 178 M 296, 583 P2d 1049 (1978).

Pro Rata Clause Discriminatory: Where insured was charged the same premium as another insured who carried no other crop insurance, but the benefits payable to him would be only a part of those payable to another insured without other crop insurance under policy's pro rata clause, it was proper for the District Court to find the pro rata clause a violation of the unfair discrimination statute and unlawful because a "full risk" premium was paid and only a partial recovery was possible due to the pro rata clause. McCarter v. Glacier Gen. Assurance Co., 169 M 269, 546 P2d 249 (1976). See also Musselman v. Mtn. W. Farm Bureau Mut. Ins. Co., 251 M 262, 824 P2d 271, 49 St. Rep. 50 (1992), in which it was held that the District Court did not err in failing to enforce a pro rata clause in a fire insurance policy when two separate individuals were insuring two entirely different interests in the same property.

One Unlawful Act — Entire Contract Void Where Single Consideration: Where there is but a single consideration passing for the performance of several separate and distinct acts, one of which is unlawful, the entire contract, it not being severable, is void, particularly so where it is wholly executory. In re Cummings' Estate, 89 M 405, 298 P 350 (1931).

28-2-708. Restraints upon legal proceedings void.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

1985 Amendment: Inserted last sentence, referring to Title 27, chapter 5.

Case Notes

Forum Selection Clause Valid by Operation of Choice of Law Clause: In a contract containing a paragraph that contained both a choice of law clause for Washington state and a forum selection clause that included Spokane, Washington, the Supreme Court determined that the choice of law clause was valid under the factors set out in Modroo v. Nationwide Mutual Fire Insurance Company, 2008 MT 275, 345 M 262, 191 P3d 389 (2008), and since Washington law recognizes forum selection clauses and Appleway chose Spokane as the venue, Montana venue is improper. Polzin v. Appleway Equipment Leasing Inc., 2008 MT 300, 345 M 508, 191 P3d 476 (2008), followed in San Diego Gas & Electric Co. v. Ninth Judicial District Court, 2014 MT 191, 375 Mont. 517, 329 P.3d 1264.

Choice of California Forum for Arbitration Held Void: Keystone, an auto parts business located in Montana, purchased a computer system from Triad for the management of Keystone's auto parts business. The contract was to be performed in Montana. The system failed to work properly, and Keystone sued Triad in Montana for breach of warranty, breach of contract, negligence, and negligent misrepresentation. The contract provided that disputes between the parties were to be settled before the American Arbitration Association in California, and the District Court held that the proper forum for arbitration was California. Citing Casarotto v. Lombardi, 268 M 369, 886 P2d 931 (1994), reversed on other grounds in Doctor's Associates, Inc. v. Casarotto, 517 US 681 (1996), the Supreme Court held that a contractual choice of law is governed in Montana by sections 187 and 188 of Restatement (Second) of Conflict of Laws. These sections provide that: (1) the state chosen by the parties will be the forum unless the application of the law of the chosen state would be contrary to the fundamental policies of another state that has a materially greater interest than the chosen state; (2) the other state would be the forum in the absence of an effective choice of law by the parties; and (3) one of the factors to be considered in making the determination of whether another state has a material interest in the enforcement of the contract is the place where the contract is to be performed. The Supreme Court noted that the contract was to be performed exclusively in Montana and therefore held that Montana had a materially greater interest in the contract issue than did California and that Montana law would therefore apply in the absence of the choice of a forum provision in the contract. The Supreme Court then held, citing State ex rel. Polaris Indus., Inc. v. District Court, 215 M 110, 695 P2d 471 (1985), and Rindal v. Seckler, 786 F. Supp. 890 (D.C. Mont. 1992), that the application of California law would be contrary to a fundamental policy of Montana as expressed in this section because this section has historically been applied: (1) to protect Montana residents from having to litigate outside of Montana; and (2) to invalidate predispute arbitration agreements. The Supreme Court noted that whether or not this section applies to arbitration contracts, 27-5-323 provides the same protection as this section does, but explicitly in the context of arbitration agreements. Because 27-5-323 allows the waiver of a party's right to arbitration in Montana only upon advice of counsel and because there was no evidence that the right was waived based on the advice of counsel, the Supreme Court held that the provision in the contract making California the forum for arbitration was void. Keystone, Inc. v. Triad Sys. Corp., 1998 MT 326, 292 M 229, 971 P2d 1240, 55 St. Rep. 1321 (1998), followed in Wolf's Interstate Leasing & Sales, LLC v. Banks, 2009 MT 354, 353 M 189, 219 P3d 1260 (2009).

Montana Law Not Preempted by Federal Arbitration Act: Keystone, an auto parts business located in Montana, purchased a computer system from Triad for the management of Keystone's auto parts business. The contract was to be performed in Montana. The system failed to work properly, and Keystone sued Triad in Montana for breach of warranty, breach of contract, negligence, and negligent misrepresentation. The contract provided that disputes between the parties were to be settled before the American Arbitration Association in California, and the District Court held that the proper forum for arbitration was California because, among other reasons, Montana law was preempted by the Federal Arbitration Act (FAA)(9 U.S.C. 2). The Supreme Court reviewed the opinion of the U.S. Supreme Court in the case of Doctor's Associates, Inc. v. Casarotto, 517 US 681 (1996), and interpreted that opinion to mean that a state may not place arbitration clauses on an unequal footing from general contract provisions. The Supreme Court pointed out that although 27-5-323 does apply only to arbitration provisions, this section applies to contracts generally and that therefore it cannot be said that arbitration provisions are treated differently from contracts generally. The Supreme Court also pointed out that the Montana statutes preserve and do not nullify the parties' duty to arbitrate and for that reason, the case should be distinguished from those cases cited by Triad, holding that the FAA preempted state statute. For these reasons, the Supreme Court held that under the rationale of Casarotto, 27-5-323 and this section are not preempted by the FAA. Keystone, Inc. v. Triad Sys. Corp., 1998 MT 326, 292 M 229, 971 P2d 1240, 55 St. Rep. 1321 (1998).

Suit in State Court for Breach of Provisions of Federal Act Incorporated by Reference Into Contract — Not Preempted by Procedural Limitations in Federal Act: The Graveleys and the Farm

Credit Bank entered into a loan agreement that incorporated by reference the provisions of the Agricultural Credit Act of 1987. When the bank attempted to foreclose on the loan, the Graveleys argued that the bank was in breach of the provisions of the Act. The bank responded that the terms of the Act precluded suit in state court to enforce the terms of the Act. The Supreme Court held that the incorporation of the Act's provisions into the contract made the enforcement of those provisions as enforceable in state court as any other contract term and that the mere provision in the Act for review of a restructuring denial by a credit review committee did not express an intent by Congress to limit the other methods of enforcing the Act's provisions. State ex rel. Farm Credit Bank of Spokane v. District Court, 267 M 1, 881 P2d 594, 51 St. Rep. 709 (1994), distinguished in AgAmerica, FCB v. Robson, 272 M 413, 901 P2d 100, 52 St. Rep. 800 (1995).

When Arbitration Not Applicable — Insurance Contracts: Plaintiffs challenged a provision of their insurance contract that required arbitration of the value of loss in case of dispute between them and the insurer. The court held that arbitration of such disputes is not provided for under the Uniform Arbitration Act (specifically 27-5-114(2)(b)) and is therefore not exempt from the prohibition of this section. However, citing Randall v. Am. Fire Ins. Co., 10 M 340, 25 P 953 (1891), the court held that this section did not prevent agreements to arbitrate factual questions relating to value or quantity and upheld the arbitration provision in plaintiffs' contract. Garretson v. Mtn. W. Farm Bureau Mut. Ins. Co., 234 M 103, 761 P2d 1288, 45 St. Rep. 1764 (1988).

Contract Forum Selection Clauses Void: A Montana distributor sued an out-of-state manufacturer in Montana court for tort and contract claims arising from their agreement which provided that Minnesota would be the sole forum for such disputes. The District Court denied defendant's motion to dismiss. The Supreme Court affirmed and held that the forum selection clause was void under 28-2-708 because it restricted the parties from enforcing their contract rights. State ex rel. Polaris Indus., Inc. v. District Court, 215 M 110, 695 P2d 471, 42 St. Rep. 220 (1985), followed in Keystone, Inc. v. Triad Sys. Corp., 1998 MT 326, 292 M 229, 971 P2d 1240, 55 St. Rep. 1321 (1998).

Arbitration Clause Unenforceable: An architect's service contract contained a standardized arbitration clause. At issue were questions of law and mixed questions of law and fact. Neither party consented to arbitrate the dispute. Without the consent of the parties, the clause was unenforceable under this section. Ace Plumbing & Heating, Inc. v. School District, 204 M 81, 662 P2d 1327, 40 St. Rep. 678 (1983). (Decided prior to 1985 amendment.)

Invalidity of Agreement to Arbitrate All Disputes Under a Contract — Injunctive Relief: A contract may require future disputes as to value or quantity to be submitted to arbitration, but contract provisions which require parties to submit future disputes as to questions of law are void. Claims of breach of contract, negligence, and breach of warranty are issues of law or mixed issues of law and fact. In a case involving these claims, an agreement to arbitrate all future disputes is unenforceable and a nullity. An injunction to stay all arbitration proceedings is a proper remedy to avoid a real threat of irreparable injury when the rules of the arbitration body provide that the parties are presumed to have consented to the entry of a judgment upon the arbitrators' award. Palmer Steel Structures v. Westech, Inc., 178 M 347, 584 P2d 152 (1978). (Decided prior to 1985 amendment.)

Void Arbitration Clause: Any contract provision which states that all future contract disputes shall be submitted to arbitration is void because it restricts access to the courts. Smith v. Zepp, 173 M 358, 567 P2d 923 (1977). (Decided prior to 1985 amendment.)

Architect's Insurance Policy: Insurance policy requirement that insured would have to file complaint on or before certain date in order to receive coverage would be void as against public policy under this section. J. G. Link & Co. v. Cont. Cas. Co., 470 F2d 1133 (9th Cir. 1972).

Arbitration Provision:

On application for Writ of Supervisory Control, District Court would be required to take jurisdiction of claim by contractor for additional work performed on contract with drainage district, notwithstanding decision for drainage district under arbitration clause, since arbitration cannot be final as to questions of law. State ex rel. Cave Constr. Co. v. District Court, 150 M 18, 430 P2d 624 (1967). (Decided prior to 1985 amendment.)

A provision in a contract requiring all "differences or controversies" arising between the parties to be submitted to arbitration will not bar the litigation of such controversies when brought into court. School District v. Globe & Republic Ins. Co., 146 M 208, 404 P2d 889 (1965); Green v. Wolff, 140 M 413, 372 P2d 427 (1962). (Decided prior to 1985 amendment.)

Arbitration Clause in Insurance Policy:

Where clause in insurance contract provided that school district was to submit to arbitration with insurance company controversies over the "value" of destroyed property, such clause was not void as against public policy, and disagreement on value of damaged school building should first have been arbitrated with the company. School District v. Globe & Republic Ins. Co., 146 M 208, 404 P2d 889 (1965), followed in Garretson v. Mtn. W. Farm Bureau Mut. Ins. Co., 234 M 103, 761 P2d 1288, 45 St. Rep. 1764 (1988). (Decided prior to 1985 amendment.)

When an arbitration clause in an insurance policy expressly or impliedly limits the time within which an appraisal must be made, such demand must be made within a reasonable time after disagreement as to the amount has arisen. School District v. Globe & Republic Ins. Co., 146 M 208, 404 P2d 889 (1965). (Decided prior to 1985 amendment.)

Whether a demand for appraisal has been made within a reasonable time depends upon the circumstances of each case, although two factors have been decisive: prejudice resulting from the delay, and the breakdown of good-faith negotiations. School District v. Globe & Republic Ins. Co., 146 M 208, 404 P2d 889 (1965). (Decided prior to 1985 amendment.)

"No Judgment" Clause: A "no judgment" clause, making uninsured motorist coverage inapplicable if the insured prosecutes his claim against an uninsured third party without the consent of the insurer, is void and unenforceable. Dominici v. St. Farm Mut. Auto. Ins. Co., 143 M 406, 390 P2d 806 (1964). See also St. Farm Mut. Auto. Ins. Co. v. Taylor, 223 M 215, 725 P2d 821, 43 St. Rep. 1667 (1986).

Agreement as to Venue: This statute is not violated by a stipulation regarding venue of an action brought against one in a county where he agreed it might be brought. Elec. Prod. Consol. v. Bodell, 132 M 243, 316 P2d 788 (1957).

Fraternal Benefit Insurance:

The constitution of an Ohio fraternal benefit society which limited the time for bringing actions against the society would not govern the Statute of Limitations in view of this section. Trammel v. Brotherhood of Locomotive Firemen & Enginemen, 126 M 400, 253 P2d 329 (1953).

A provision in the bylaws of a fraternal benefit society, requiring a member claiming to be entitled to benefits, as a condition precedent to his maintaining an action in the courts, to follow an elaborate procedure before various committees of the branch and supreme bodies of the society in an effort to exhaust all his remedies therein prescribed, was invalid. Cacic v. Slovenska Narodna Podporna Jednota, 102 M 438, 59 P2d 910 (1936).

Sale of Timber: A provision in timber sale regulations, made a part of contract for sale of timber on Indian reservation, that depreciation in value and quantity caused by purchaser's breach should be estimated under direction of officer approving the contract was valid under this section. Polley's Lumber Co. v. U.S., 115 F2d 751 (9th Cir. 1950).

Fire Insurance Policy: A provision in a fire insurance policy that no action shall be sustainable in any court of law or equity "unless commenced within twelve months after the fire" was void as against public policy under this section, declaring that every stipulation or condition in a contract which limits the time within which a party may enforce his rights is void. Thielbar Realties, Inc. v. Nat'l Union Fire Ins. Co., 91 M 525, 9 P2d 469 (1932).

Common Law:

This section is the statement in the form of a statutory enactment of the common law as it existed in this state prior to the adoption of the codes in 1895. According thereto, a provision of a contract by which the construction to be placed on it by the agent of one of the parties should be final and without the right of appeal to the courts is void. Wortman v. Mont. Cent. Ry., 22 M 266, 56 P 316 (1899), explained in Polley's Lumber Co. v. U.S., 115 F2d 751 (9th Cir. 1950).

This section does not apply to contracts made before its adoption. Cotter v. Grand Lodge A. O. U. W., 23 M 82, 57 P 650 (1899).

Law Review Articles

Contract Clause Providing for Arbitration of Future Disputes Is Not Enforceable in Montana, Swanberg, 24 Mont. L. Rev. 77 (1962).

Contract Provisions Stipulating Venue, Sorte, 19 Mont. L. Rev. 165 (1958).

28-2-709. Illegality of agreement to allow another person to confess judgment, accept service of process, or accept default.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Law Review Articles

The Supreme Court's Still Changing Attitude Toward Consumer Protection and Its Impact on the Integrity of the Court, McDermott, 37 Mont. L. Rev. 27 (1976).

The Supreme Court's Changing Attitude Toward Consumer Protection and Its Impact on Montana Prejudgment Remedies, McDermott, 36 Mont. L. Rev. 165 (1975).

Mitchell v. W. T. Grant Co.: Return to Prejudgment Remedies?, Karell, 36 Mont. L. Rev. 103 (1975).

28-2-710. Compromise and settlement of civil claims — negotiation.

Compiler's Comments

Effective Date: This section is effective October 1, 2023.

Codification Change: Section 2, Ch. 273, L. 2023, provided that this section was to be codified as an integral part of Title 27, chapter 1. The Code Commissioner has codified this section in Title 28, chapter 2, part 7, to more closely reflect the subject matter.

28-2-721. When provision fixing liquidated damages valid.

Case Notes

Conscionability Analysis of Contractual Liquidated Damages Clause — Liquidated Damages Clause Presumed Enforceable: To provide direction to contracting parties and resolve the disparities in case law regarding liquidated damages, the Supreme Court adopted a rule to analyze liquidated damages clauses from the perspective of whether or not the clause is unconscionable as indicated by the nature of the bargaining process between the parties. Unconscionability involves a two-pronged determination regarding whether: (1) the clause fits the doctrine of contract of adhesion such that the weaker party had no meaningful choice regarding acceptance of the contract provisions; and (2) the contractual terms are unreasonably favorable to the drafter, which is usually the party with superior bargaining power. Whether the clause is unreasonably favorable to the drafter in turn involves an inquiry into whether the clause is within the reasonable expectations of or unduly oppressive to the weaker party. Liquidated damages clauses are presumed enforceable, and the party seeking to avoid the clause has the burden of proving unconscionability. Unless there are underlying disputed issues of fact, the question of unconscionability is purely a matter of law for the court to decide. Arrowhead School District No. 75 v. Klyap, 2003 MT 294, 318 M 103, 79 P3d 250 (2003), overruling Daugherty Cattle Co. v. Gen. Constr. Co., 254 M 479, 839 P2d 562 (1992), to the extent that it prevented one party from introducing relevant evidence by granting summary judgment based on contract language alone, overruling Story v. Bozeman, 259 M 207, 856 P2d 202 (1993), to the extent that it placed the burden on the nonbreaching party to prove the enforceability of a liquidated damages clause, and followed in Am. Music Co. v. Higbee, 2004 MT 349, 324 M 348, 103 P3d 518 (2004), and in Highway Specialties, Inc. v. Mont. Dept. of Transportation, 2009 MT 253, 351 M 527, 215 P3d 667 (2009).

Liquidated Damages Clause in Personal Services Contract — Conscionability of Liquidated Damages Clause in Teacher's Form Contract: In determining the enforceability of a 20% liquidated damages clause in defendant's teaching contract, the Supreme Court examined the conscionability of the clause. The court first held that the clause constituted a contract of adhesion because defendant, as the weaker bargaining party, had no meaningful choice regarding acceptance of the contract provisions. The court also noted that the contract was a form contract that provided no negotiation between the parties. However, the court held that unconscionability does not render all form contracts unacceptable and that form contracts are only unconscionable if the terms are not within the reasonable expectation of the party who had no opportunity to negotiate. Although the liquidated damages clause in defendant's contract was harsher than most, as a teacher, defendant knew that teachers are typically employed for an entire year and how difficult it is to replace equivalent services at small rural schools, so it was within defendant's reasonable expectations to agree to a contract with a 20% liquidated damages provision for departing so close to the start of the school year, even though defendant had no meaningful choice regarding the provision. The enforceability of the liquidated damages clause was affirmed. Arrowhead School District No. 75 v. Klyap, 2003 MT 294, 318 M 103, 79 P3d 250 (2003).

Standard of Review of Contractual Stipulated Damages Provision — Enforceable Liquidated Damages Versus Unenforceable Penalty: Whether a stipulated damages provision in a contract constitutes enforceable liquidated damages or an unenforceable penalty is a question of law, and if the underlying facts are not in dispute, the Supreme Court will review a determination of this conclusion of law for correctness. Arrowhead School District No. 75 v. Klyap, 2003 MT 294, 318 M 103, 79 P3d 250 (2003), followed in Highway Specialties, Inc. v. Mont. Dept. of Transportation, 2009 MT 253, 351 M 527, 215 P3d 667 (2009). See also Lake River Corp. v. Carborundum Co., 769 F2d 1284 (7th Cir. 1985).

Contract Remedy Providing Transfer of Twenty-Acre Parcel of Land as Security for Contractual Obligations Not Considered Unenforceable Liquidated Damages Provision — Award of Actual Damages Not Including Expectancy Damages and Lost Profits: As part of a sale of real property, Canton pledged a 20-acre parcel to Riverview Homes II, Ltd. (Riverview), as security in the event that Canton breached his contractual obligation to complete a proposed subdivision and construct an artificial lake. Canton breached the contract, and Riverview sought to quiet title to the 20-acre parcel. The District Court agreed that Canton breached the contract, but held that the contract remedy was an unenforceable liquidated damages provision because the amount of damages to be paid for breach of Canton's obligations was determined in anticipation of Canton's possible breach. The court then examined the contract for another possible method to determine the appropriate amount of damages, and ultimately awarded Riverview $92,046 as the amount that Riverview would have received for the sale of the property as bare lots without homes. Riverview appealed, contending that the contractual language was not a liquidated damages provision because the parties did not agree on the amount of compensation or damages to be paid by Canton in case of a breach of contract, and arguing that the District Court erred in setting the damage amount by failing to account for the profit that Riverview would have received from the sale of the lots with homes. The Supreme Court agreed that the contract language was not an unenforceable liquidated damages provision, but found that the discussion regarding liquidated damages was not essential to the resolution of the parties claims, and moved on to the actual award of damages. The Supreme Court declined to allow Riverview an award of speculative profits in the absence of lost profits attributable to Riverview's inability to sell developed lots. The District Court's determination of damages was affirmed. If the contract had been performed, Riverview would have had six bare lots approved as a subdivision, and an artificial lake. Because of Canton's breach, Riverview had neither. The District Court's award accounted for the expectations of the parties at the signing of the contract, and Riverview was not allowed to recover a greater amount of damages than would have been gained by full performance of the contract. Riverview Homes II, Ltd. v. Canton, 2001 MT 309, 307 M 517, 38 P3d 848 (2001).

Contract Provision Setting Damages Generally Void — Exception Distinguished: The real estate contract between Webers and Riveras contained a clause stating that if either party failed to perform, the amount of liquidated damages was to be 10% of the agreed sale price, an amount ordered to be paid to Webers when Riveras defaulted. The Supreme Court recognized the exception provided in Morgen v. Big Sky of Mont., 171 M 268, 557 P2d 1017 (1976), for situations when parties agree in advance on an amount of damages because it would be impracticable or extremely difficult to fix the actual damages. However, in this case, the contract provided for a set amount of damages without any regard for or attempt to determine what actual damages might be. Considering the subject matter, the surrounding circumstances, and the intent of the parties, the provision was held to be a void penalty clause. The fact that the liquidated damages provision might approximate the amount of actual damages was insufficient to create a valid liquidated damages provision. The matter was remanded for a determination of actual damages. Weber v. Rivera, 255 M 195, 841 P2d 534, 49 St. Rep. 969 (1992).

Holdover Rent Provisions Not Excessive, Unreasonable, or Illegal: The parties signed a contract at the conclusion of an earlier foreclosure action whereby the foreclosed purchasers were allowed to lease the property for an additional period. When the lessees remained on the property beyond the agreed lease period, the lessors commenced the present foreclosure action. The lessees have not shown that the contract holdover rent provision of $75 a day constituted illegal liquidated damages and penalty. The provision is not excessive, unreasonable, or illegal. The holdover amount is substantially less than the worth of the property on a yearly basis. Ruegsegger v. Welborn, 237 M 317, 773 P2d 305, 46 St. Rep. 833 (1989).

Agreement Containing Remedy for Breach — Remedy Not Expressly Made Exclusive — Injunction to Enforce Agreement Improper: A tender of stock containing an agreement not to compete contained a clear provision setting forth an appropriate remedy upon breach, which was a reduction of one-third in the stock price. Injunction was not a proper remedy to enforce the agreement because the agreement provided an adequate remedy in law. Although the agreement didn't expressly limit available remedies to those in the agreement, the court held that such limitation was not necessary because allowing injunctive relief would have nullified the remedy agreement agreed to by the parties, contrary to the intentions of the parties. Foster v. Realty Title Co., Inc., 209 M 183, 680 P2d 323, 41 St. Rep. 630 (1984).

Method of Determination — Not Liquidated Damages: The parties entered into an agreement for the lease of a truck. The lease agreement contained a noncancellation provision and provided alternative remedies to the lessor in the event of a default. Lessee returned the truck with current payments to lessor prior to the termination date of the lease. Lessor had to make repairs to the truck. Lessor held a public sale pursuant to the lease and repurchased the truck. He then leased it to another party. Lessee contended the remedy of sale in the lease was void as a liquidated damage. "Liquidated damages" refers to an amount of damage. The sale provision was merely an optional procedure to determine the amount. There was no stipulated amount of damages in the lease. The law of liquidated damages was inapplicable. Diede v. Davis, 203 M 205, 661 P2d 838, 40 St. Rep. 394 (1983).

Penalty or Liquidated Damages — Determination by Court: Whether a forfeiture provision imposes a penalty or provides for liquidated damages is to be determined by the court from the language and subject matter of the contract, the intent of the parties, and all facts and circumstances under which the contract was made. The most important facts to be considered are whether the damages were difficult to ascertain and whether the stipulated amount is a reasonable estimate of probable damages or is reasonably proportionate to the actual damage sustained at the time of the breach. Morgen & Oswood Constr. Co. v. Big Sky of Mont., 171 M 268, 557 P2d 1017 (1976), followed in Story v. Bozeman, 259 M 207, 856 P2d 202, 50 St. Rep. 761 (1993).

Liquidated Damages — Time — Delay Due to Contractee: Where the contractee caused a substantial part of the delay in the building and progress of the work, without any agreement for an extension of time to offset the delay, the time fixed in the contract and any provisions for liquidated damages based thereon are abrogated, leaving the contractor responsible only to complete the work within a reasonable time. Haggerty v. Selsco, 166 M 492, 534 P2d 874 (1975).

Provision for Maximum Recovery:

Limitation of telephone company's liability for errors in contract for "yellow pages" advertising and providing for maximum recovery was valid under this section. State ex rel. Mtn. St. Tel. & Tel. Co. v. District Court, 160 M 443, 503 P2d 526 (1972).

Without a demonstration of bad faith, fraud, or willful or wanton conduct by telephone company, a limitation of liability for errors and omissions in its advertising expressed in a written and signed contract is reasonable, and it was within the power of the company and subscribers to include such a clause in a valid and binding contract. State ex rel. Mtn. St. Tel. & Tel. Co. v. District Court, 160 M 443, 503 P2d 526 (1972).

Pleading and Proof:

Where the substance of the provisions of Montana statutes indicating facts which a party seeking to recover liquidated damages under a construction contract must allege and prove were embodied by agreement in a construction contract which the United States was seeking to enforce, further allegations and proof of such facts were unnecessary. U.S. v. Grogan, 39 F. Supp. 819 (D.C. Mont. 1941).

Since the language of this section is general, every contract containing a stipulation such as is denounced in subsection (1) is prima facie void as to the stipulation. Therefore, when recovery is sought upon it, the plaintiff's allegations and proof must bring it within the exception provided in subsection (2). Clifton v. Willson, 47 M 305, 132 P 424 (1913).

Waiver of Deficiencies: The provision in a contract of sale of certain machinery to the effect that 20 days' use should constitute an acceptance and waiver of deficiencies is neither void as a stipulation for liquidated damages, as provided in this section, nor obnoxious as a restriction upon the right to have one's claims adjudicated in a court of law, as provided by 28-2-708. Best Mfg. Co. v. Hutton, 49 M 78, 141 P 653 (1914).

Forfeiture Clause: Where a contract of purchase provides that a failure to make any deferred payment shall work an immediate forfeiture of the contract, the contract, insofar as it provides for liquidated damages, may be void and of no effect under this section. Still, in any event, the defaulting purchaser, in the absence of a showing on his part, such as would appeal to the conscience of a court of equity, is not entitled to a return of any part of the purchase price made by him, though he asks for it. Fratt v. Daniels-Jones Co., 47 M 487, 133 P 700 (1913); Cook-Reynolds Co. v. Chipman, 47 M 289, 133 P 694 (1913), followed in Daugherty Cattle Co. v. Gen. Constr. Co., 254 M 479, 839 P2d 562, 49 St. Rep. 820 (1992).

Purchase of Real Estate: Even if a provision in a contract for the sale of real estate that the purchaser, in case of his default, shall forfeit all advance payments is a stipulation for liquidated damages within the inhibition of this section, this fact would not of itself require that the defaulting purchaser should have return of the money paid by him. On the contrary, its effect is to leave the parties where they would be if no such stipulation had been made. Without such a stipulation the defaulting purchaser is not, in the absence of an equitable showing, entitled to a return of any part of the money paid. Cook-Reynolds Co. v. Chipman, 47 M 289, 133 P 694 (1913), followed in Daugherty Cattle Co. v. Gen. Constr. Co., 254 M 479, 839 P2d 562, 49 St. Rep. 820 (1992).

Water Contract: A contract which bound the defendant irrigation company to furnish to plaintiff a certain amount of water during a certain season and which provided that if the company should for any reason fail to deliver the water, it would return to plaintiff the money paid by him (and plaintiff agreed to accept the same and to release the company from any damage arising from such failure) fell clearly within the provisions of this section and was void on its face to the extent of the liquidated damages agreed on in case of a breach. Deuninck v. W. Gallatin Irr. Co., 28 M 255, 72 P 618 (1903).

Stipulated Versus Actual Damages — Burden on Defendant: Where a suit is brought on a contract for the actual and not the liquidated damages, it is for the defendant to show by proper answer and competent proof that the contract for stipulated damages is valid under this section, and such question cannot be presented to the court by demurrer to the complaint. Deuninck v. W. Gallatin Irr. Co., 28 M 255, 72 P 618 (1903).

28-2-723. Construction contracts requiring lien or bond waiver void.

Compiler's Comments

Effective Date — Applicability: Section 3, Ch. 119, L. 1999, provided: "[This act] is effective on passage and approval [approved March 19, 1999] and applies to construction contracts entered into on or after [the effective date of this act]." Effective March 19, 1999.

28-2-724. Prohibition of contracts that restrict practice — applicability — exceptions.

Compiler's Comments

Effective Date: Section 3, Ch. 479, L. 2023, provided: "[This act] is effective on passage and approval." Approved May 8, 2023.

Part 8
Consideration

Part Case Notes

Receipt Precluding Failure of Consideration: In an action for specific performance of a buy-sell agreement, there was no failure of consideration because the buyers received that for which they bargained. Halcro v. Moon, 226 M 121, 733 P2d 1305, 44 St. Rep. 504 (1987).

Real Estate Listing Agreement — Expenditure of Time and Money as Adequate Consideration: Buechler entered into a contract with Payne, granting him the right to sell Buechler's property. Payne attempted to sell the property and expended $1,120 to attract purchasers. Buechler canceled the contract before its term expired and sold the property herself. Buechler argued that the contract lacked consideration and therefore she was entitled to cancel the contract. The court found that Payne was employed on a commission basis and that his expenditure of time and money to attract a purchaser constituted consideration for Buechler's agreement to pay a commission. Payne v. Buechler, 192 M 311, 628 P2d 646, 38 St. Rep. 799 (1981).

Parties to Determine Consideration: Consideration, as essential evidence of the parties' intent to create a legal obligation, must be that which the parties adopt and regard as such. Kintner v. Harr, 146 M 461, 408 P2d 487 (1965).

28-2-801. What constitutes good consideration.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Legal Obligation 219
Promissory Note 222
Benefit or Detriment 222
Effect on Pending Litigation 224
Miscellaneous 224

LEGAL OBLIGATION

Materiality of Claim of Failure of Consideration to Contract Required Before Rescission Available as Remedy — Partial Failure of Consideration — Meltdown of Ice Cream Distributorship Agreement: Under Johnson v. Meiers, 118 M 258, 164 P2d 1012 (1946), a breach that goes to only part of the consideration, that is incidental and subordinate to the main purpose of the contract, and that may be compensated in damages does not warrant rescission. The injured party is still bound to perform that party's part of the contract, and the only remedy for the breach consists of the damages suffered from the breach. By contrast, under Van Hook v. Baum, 245 M 407, 800 P2d 151, 47 St. Rep. 1883 (1990), a party may rescind if, through the fault of the other party, consideration fails in whole or in part. In clarifying the disparate holdings, the Supreme Court noted that the term "failure of consideration", as either a claim or an affirmative defense, does not relate to the absence of consideration or whether there is good consideration for the formation of a valid, enforceable contract, but rather the term pertains to the failure of one party's performance, which then suspends or excuses the performance of the other party pursuant to the terms of a valid contract. Failure of consideration is generally synonymous with a material breach of performance of a contract, rather than whether a contract was enforceable because of the absence of the essential element of consideration. Thus, a claim or affirmative defense of failure of consideration that gives rise to the equitable remedy of rescission requires a showing by the claiming party that the other party's failure to perform was, in fact, material to the contract, and whether consideration was sufficient or good is immaterial. To reconcile this holding with 28-2-1711, the court went on to hold that failure of part of a promised performance may warrant rescission, but only if the claiming party proves that the deficient part of the other party's performance was material to the contract. If the failure to perform was not material, rescission is not an available remedy, performance cannot be excused, and the claiming party "may only be entitled to money damages for breach". Here, the District Court erred when it did not determine whether Norwood's failure to assign an ice cream distributor agreement to Service Distributing, Inc. (SDI), was material to the transaction as a whole. Absent that finding, SDI could not as a matter of law rescind the contract and be excused from further performance of its obligation to Norwood, so the case was remanded to determine whether a material breach occurred. Norwood v. Serv. Distrib., Inc., 2000 MT 4, 297 M 473, 994 P2d 25, 57 St. Rep. 8 (2000). See also Flaig v. Gramm, 1999 MT 181, 295 M 297, 983 P2d 396, 56 St. Rep. 710 (1999).

Consideration Under Contract Creating Relationship of Lender and Approved Dealer for Making Housing Loans: A contract between the parties created a relationship of Green Tree Financial Corporation (Green Tree) as "lender" and Larson, doing business as Majestic Homes, Inc. (Majestic), as "approved dealer", for purposes of making federal housing loans pursuant to federal Housing and Urban Development (HUD) regulations. Majestic submitted an application to become an approved dealer, and Green Tree then approved Majestic as a dealer and required Majestic to enter into a dealer agreement that included terms expressly provided for by HUD regulations. In order to become and remain an approved dealer, Majestic promised to operate pursuant to HUD regulations—something that it was not otherwise obligated to do in the course of its business. Complying with HUD regulations and meeting other requirements of Green Tree constituted good consideration on the part of Majestic. In return for Majestic's conformance to federal regulations and a security interest in Majestic's assets, Green Tree agreed to perform a service for Majestic by reviewing and approving or rejecting credit applications that Majestic submitted on behalf of its customers. Majestic was allowed to hold itself out as an approved dealer, which provided a competitive advantage in the manufactured home business. The arrangement constituted a contractual relationship whereby the parties exchanged valuable consideration and was enforceable. This relationship is distinguishable from an indefinite requirements or output contract in which there is no exchange of obligations and no establishment of a lender-dealer relationship. Larson v. Green Tree Financial Corp., 1999 MT 157, 295 M 110, 983 P2d 357, 56 St. Rep. 618 (1999). See also Linn v. City County Health Dept., 1999 MT 235, 296 M 145, 988 P2d 302, 56 St. Rep. 922 (1999).

Mining Agreement Supported by Adequate Consideration: Nordwick and Berg agreed in writing to purchase unimproved mining property. The agreement provided that Nordwick would enter into an earnest money and buy-sell agreement with the property owner and that Berg would pay the earnest money and balance of the purchase price. Under the agreement, Berg received surface title and the timber rights, with each party receiving a one-half interest in the mineral rights. After Nordwick secured the buy-sell agreement, Berg paid the owner the earnest money and a warranty deed was recorded. Berg subsequently refused to convey to Nordwick the one-half interest in mineral rights, entering instead into a contract with a third party without revealing Nordwick's one-half interest. The District Court ruled that Nordwick was entitled to one-half interest. The Supreme Court denied Berg's assertion on appeal that the written agreement lacked adequate consideration. Nordwick v. Berg, 223 M 337, 725 P2d 1195, 43 St. Rep. 1768 (1986). See also Larson v. Green Tree Financial Corp., 1999 MT 157, 295 M 110, 983 P2d 357, 56 St. Rep. 618 (1999).

Contract for Sale — Change to Option Contract: Plaintiff and realtor authorized to sell lots for corporation executed a 1975 contract under which plaintiff deposited $500, would pay $5,000 upon payment to plaintiff at a future uncertain time of a bonus in that amount, and would pay the balance of the purchase price within 90 days of the $5,000 payment and be given title. The contract was later modified to provide that if the bonus was not paid by January 1, 1980, plaintiff could either purchase the lot by paying the balance of the purchase price beyond the deposit within 90 days or choose not to purchase and to receive back his deposit. The modification changed both parties' rights and obligations, and such changes constituted consideration for the modification. The benefits and obligations of the parties under the modification were sufficient to constitute a mutually binding contract. Naylor v. Hall, 201 M 59, 651 P2d 1010, 39 St. Rep. 1953 (1982).

Counterclaim on Contract — Fulfillment of Preexisting Duties Not Consideration — Effect of Lack of Consideration: Plaintiffs contracted with defendant to build their log home. Before and after occupancy of the home, structural problems requiring repair occurred. At trial, defendant counterclaimed against the plaintiffs for his expenses in installing tie rods in the walls of the home. The plaintiffs had authorized the installation of the tie rods after a windstorm had shown the home to be unstable. Although noting the ratification of the agreement after the rods were installed, the Supreme Court also noted that the home remained unstable and that the rods may have been improperly installed. It said that defendant had a common-law duty to construct the home in a workmanlike manner, in a manner as to assure stability. The duty was not fulfilled even after the installation of the tie rods. Because a promise to perform a preexisting legal or contractual obligation is insufficient consideration for a promise made in return, consideration was lacking in the supplemental (tie rod installation) agreement. Under former Rule 41, M.R.Civ.P. (now superseded), a counterclaim may be dismissed where, upon the facts and the law, the claimant has shown no right to relief. With consideration lacking, the contract was unenforceable, and the defendant had no right to relief on his counterclaim. Estoppel will not support the defendant's claim without a showing of detrimental reliance, and it has no application when the omissions of the party claiming estoppel brought about the problem. Carroccia v. Todd, 189 M 172, 615 P2d 225, 37 St. Rep. 1437 (1980), followed in McGregor v. Cushman/Mommer, 220 M 98, 714 P2d 536, 43 St. Rep. 206 (1986).

No Valid Prior Oral Contract — Consideration for Written Contract: A legal duty to provide a pump under an oral contract would not be sufficient consideration for a later written contract covering the same transaction. When, however, the trial court found that no prior oral contract existed, agreement to provide the pump did constitute valid consideration for the written contract and hence it is not void for lack of consideration. Keil v. Glacier Park, Inc., 188 M 455, 614 P2d 502, 37 St. Rep. 1151 (1980), followed in Keesun Partners v. Ferdig Oil Co., Inc., 249 M 331, 816 P2d 417, 48 St. Rep. 710 (1991).

Relinquishment of Legal Right Sufficient Consideration: A contract entered into in 1974 under which the parties agreed to release and discharge each other from liability and damages related to a previous contract entered into by the parties was supported by consideration. Each relinquished legal rights in executing the 1974 contract. The relinquishment of a legal or contract right is sufficient consideration to support a contract. Rickett v. Doze, 184 M 456, 603 P2d 679 (1979), followed in Johnson v. Estate of Shelton, 232 M 85, 754 P2d 828, 45 St. Rep. 887 (1988). See also Sunburst Oil & Gas Co. v. Neville, 79 M 550, 257 P 1016 (1927); Naylor v. Hall, 201 M 59, 651 P2d 1010, 39 St. Rep. 1953 (1982).

Oral Promise to Pay as Insufficient Consideration: A mere oral promise to pay, as in this case, is not sufficient consideration to support a contractual obligation. Such a promise must be binding and impose some legal obligation on the one making it. A contract is not made so long as, in the contemplation of both parties thereto, something remains to be done in order to establish contract relations. Schwedes v. Romain, 179 M 466, 587 P2d 388 (1978).

Promise to Fulfill Existing Obligation as Insufficient Consideration: A promise to do what a person is already obligated by law or contract to do is not sufficient consideration for a promise made in return, and an agreement to surrender possession of property which promisor is already under legal obligation to surrender is not sufficient consideration to support a promise. Hewitt v. Novak, 117 M 365, 158 P2d 627 (1945).

Family Debt: Where defendant was conversant with the fact the money procured on a mortgage on her land was to be, and was, used to pay off an indebtedness of her father for supplies used by the family and she made no complaint until action to foreclose was commenced, her defense of lack of consideration (since she received only $50 in cash of the $4,000 loaned) was unavailing. Morigeau v. Lozar, 81 M 434, 263 P 985 (1928).

Preexisting Debt Constitutes Value: A preexisting debt constitutes value, and therefore the surrender of an old promissory note upon execution of one to take its place is a sufficient consideration for the latter, and the fact that the obligation surrendered is that of another person is immaterial. First St. Bank v. Mussigbrod, 83 M 68, 271 P 695 (1928).

PROMISSORY NOTE

Loan Consolidation — Valid Consideration: A note consolidating and representing an accumulation of previous loans involving the same bank is a prior debt sufficient to constitute consideration. Farmers St. Bank v. Johnson, 188 M 55, 610 P2d 1172 (1980).

Promissory Note Constitutes Valuable Consideration: A promissory note given in consideration of an oil and gas lease was a valuable consideration, and the fact that the lessor, more than a year after its delivery, returned it to the lessee was immaterial; it having been the property of the lessor, he could do with it as he saw fit. Nadeau v. Texas Co., 104 M 558, 69 P2d 586 (1937).

Partial Consideration — Sufficiency: The fact that the maker of a promissory note did not receive all he desired by way of consideration did not vitiate his promise; having received a substantial part of it, it was sufficient to sustain the contract. Farmers & Miners' St. Bank v. Probst, 81 M 248, 263 P 693 (1928).

Note for Conditional Sale Contract: Where defendants, who had bought various pieces of farm machinery under a conditional sale contract, giving their promissory note therefor, thereafter disposed of part of them, and upon failure to pay the note plaintiff, in an action in claim and delivery, recovered a portion of the property crediting the value thereof on the note, there was a sufficient consideration in support of plaintiff's action to recover the balance due on the note. Lindsay Bros. Co. v. Montgomery, 68 M 294, 216 P 795 (1923).

Possession of Land: In an action on a promissory note for $650 in which defense of want of consideration was raised, where plaintiff, in possession of public land under a claim of right to desert entry and upon which he had made improvements consisting of about 3 miles of fencing, located defendants thereon, delivering possession and surrendering the improvements to them, defendants giving the note in payment, there was sufficient consideration for the instrument. McConnell v. Blackley, 66 M 510, 214 P 64 (1923).

New Agreement Good Consideration: Plaintiff had drilled a well for defendants, accepting their promissory notes in payment. The notes were not paid. The well proved unsatisfactory, and the parties entered into another agreement whereby plaintiff undertook to put the well in working condition and the defendants were to execute new notes and a first mortgage upon their lands to secure the amount then due. The agreement to put the well in condition was a good consideration for the mortgage contract. White v. Hulls, 59 M 98, 195 P 850 (1921).

BENEFIT OR DETRIMENT

Change of Plea Agreement Properly Denied — Application of Contract Law Standards — Agreement Not to Prosecute Father — Benefit Derived by Defendant: Keys agreed to accept a motorcycle as collateral for a loan, but the motorcycle, which Keys subsequently sold, turned out to belong to the father of the individual to whom Keys made the loan. Both Keys and his father were charged with theft, but through his attorney, Keys negotiated an Alford plea with the prosecutor whereby the charges against Keys' father would be dropped and the prosecutor would recommend to the court that Keys' sentence be deferred for 4 years. At the hearing on the plea agreement, Keys, who could not read, had difficulty understanding that the District Court was not bound by and did not have to accept the agreement. However, after a lengthy colloquy with the District Court Judge, Keys eventually did state that he understood the agreement. The District Court then ordered that Keys' sentence be deferred for 6 years, and Keys requested that his plea be withdrawn, based upon his lack of understanding and a lack of consideration for his guilty plea. The District Court refused to allow the withdrawal, and the Supreme Court affirmed that refusal. The Supreme Court held that Keys did benefit from the agreement, that the benefits included the dismissal of charges against his father, and that in dismissing those charges, the state suffered the deprivation of a right (to pursue the conviction of Keys' father) that the law did not require. The Supreme Court also held that even though there was some confusion in Keys' mind over the role of the District Court in the agreement, the record showed by Keys' responses to questions by the District Court that Keys understood, at least at one point in time, that the court was not bound by the agreement. St. v. Keys, 1999 MT 10, 293 M 81, 973 P2d 812, 56 St. Rep. 44 (1999), followed in St. v. D'Amico, 2000 MT 63, 299 M 57, 997 P2d 773, 57 St. Rep. 297 (2000), St. v. White, 2004 MT 103, 321 M 45, 88 P3d 1258 (2004), and Lout v. St., 2005 MT 93, 326 M 485, 111 P3d 199 (2005).

Licensing Requirement as Partial Failure of Consideration in Sale of Business — Rescission Proper: When the seller warranted in a special provision of a contract for deed that no license was required to operate a business and that no restrictions or license would be required as a result of change of ownership and seller later defaulted under these terms when it was discovered that a license was required but denied, it constituted a partial failure of consideration under 28-2-801 because seller did not transfer a going business and buyer was unable to operate the kind of business intended at the time of purchase. Rescission was therefore proper under 28-2-1711. Carey v. Wallner, 223 M 260, 725 P2d 557, 43 St. Rep. 1706 (1986), affirmed, 229 M 57, 744 P2d 881, 44 St. Rep. 1778 (1987).

Obligation to Refund Payment for Gas Field Option: Plaintiff corporation rescinded a gas field option upon which it had paid $50,000 to defendant. After defendant failed to refund money due, plaintiff filed suit and was granted summary judgment for $71,320.55. On appeal, the Supreme Court held that, based upon the exhibits, affidavits, and briefs before the lower court, there was no evidence of a genuine issue of material fact. The escrow agreement and release based upon plaintiff's rescission were supported by adequate consideration since release from contract obligations and forbearance to sue are both adequate consideration. Ayers Oil and Gas, Inc., was a party to both the option and the release agreements as evidenced by Ayers' signature as president. Devon Oil & Gas Co., Inc. v. Ayers, 218 M 223, 707 P2d 523, 42 St. Rep. 1536 (1985).

Resolution of Dispute — Adequate Consideration: Defendant represented plaintiff in a civil action in federal court. The parties agreed that the case was originally handled on a 50% contingency fee basis. The case lasted almost 10 years. Plaintiff signed a formal authorization for defendant to settle. At the time of settlement, plaintiff contended the parties agreed to replace their 50% of net fee agreement with a percentage distribution of the gross settlement amount. At some point in time, the parties signed an agreement in defendant's handwriting providing for a 75%-25% split of the settlement. Defendant contended the second fee agreement failed for lack of consideration. On appeal, the Supreme Court found that there was evidence that both parties agreed to rescind the original agreement and enter the second because of a dispute over costs. The change from a net to a gross computation to eliminate the accounting problem was valid consideration for the second contract. Accounts that were in dispute were settled by the revised handwritten contract. Resolution of issues in dispute constituted consideration in support of the second fee agreement. The second fee agreement was a valid, enforceable contract supported by consideration. Eaton v. Morse, 212 M 233, 687 P2d 1004, 41 St. Rep. 1708 (1984).

Refraining From Forming Bank — Good Consideration for Contract to Provide Financing: The bank had an ongoing relationship with Stensvad in which the bank would provide financing for Stensvad's cattle feeding operation. At one point a major stockholder of the bank indicated the bank's intention to withdraw its financial support unless Stensvad withdrew his efforts in the creation of a new bank in Roundup. Stensvad agreed to discontinue his efforts to form a new bank, and the bank agreed to continue to finance the operation. The bank later refused to continue to finance the operation, and Stensvad sued for breach of the agreement. The court found that the interest passing to the bank on the loans and the agreement of Stensvad not to engage in the formation of another bank were good consideration. Stensvad v. Miners & Merchants Bank of Roundup, 196 M 193, 640 P2d 1303, 39 St. Rep. 27 (1982).

What Constitutes Consideration and Mutuality: On appeal from a verdict for the buyer in a breach of contract action, the seller argued that valid consideration and mutuality of obligation were essential to a contract, that the District Court's findings and conclusions failed to set forth those elements, and that the buyer had suffered no legal detriment in the nature of consideration for the reason that his later contract for resale of the calves had not been enforced by that purchaser. However, the mutual promises were valid consideration. The buyer promised to pay the seller a certain amount in return for the seller's promise to deliver the calves on a certain date in a certain condition. The buyer delivered a $2,000 check as downpayment on his promise. Under 28-2-801, mutual promises alone were enough to constitute valid consideration. Miller v. Titeca, 192 M 357, 628 P2d 670, 38 St. Rep. 853 (1981).

Lack of Consideration: The court found that a "letter of instruction and joint assignment of funds" was unenforceable because it was not supported by consideration. The issuers, a bank and the purchaser of a modular home, were not bound because no benefit was conferred on them by the plaintiff manufacturer of the home and the plaintiff did not incur any detriment. The consideration recited in the letter was "inducement . . . to begin production" of the home. At the time of the execution of the letter, the home had already been manufactured and delivered to the plaintiff's authorized dealer. No dealings occurred between the plaintiff and the bank; the lending arrangement was rather between the bank and the dealer. Boise Cascade Corp. v. First Sec. Bank of Anaconda, 183 M 378, 600 P2d 173 (1979).

Prejudice Suffered by Payee: Where the purchaser of real property, desiring to assume the liability of the vendor upon a promissory note held by a bank, executed a new note to take the place of the former, and the bank, instead of applying a part of the cash payment made by the vendee and deposited by the vendor to the payment of the latter's note as it properly could have done, accepted the new note in lieu thereof, it thereby suffered such a prejudice which it was not lawfully bound to suffer as an inducement for the maker of the second note to sign it, as constituted a good consideration for the note. Farmers & Miners' St. Bank v. Probst, 81 M 248, 263 P 693 (1928).

Benefit Conferred or Prejudice Suffered: Any benefit conferred upon a promisor or a prejudice suffered or agreed to be suffered by the promisee, as an inducement to the promisor, is a good consideration. Farmers & Miners' St. Bank v. Probst, 81 M 248, 263 P 693 (1928).

Release of Debtor: The loss sustained by a debtor in agreeing to make an assignment for the benefit of his creditors was a sufficient consideration for his release from liabilities owing by him to them under this section in that he suffered a prejudice which he was not lawfully bound to suffer. Stone-Ordean-Wells Co. v. Anderson, 66 M 64, 212 P 853 (1923).

EFFECT ON PENDING LITIGATION

Contractual Obligation for Support Incorporated in Decree — Not Subject to Modification: Husband, to avoid having his divorce contested and thereby besmirching his girlfriend's name, agreed, in a property settlement agreement incorporated into the divorce decree, to pay $500 per month for 10 years for support of his children and maintenance of their home. In husband's petition for modification of this amount, the District Court was correct in identifying the property settlement agreement as a contract supported by valid consideration that, in the absence of any showing that the welfare of the children was affected, could not be modified. Winters v. Winters, 188 M 43, 610 P2d 1165 (1980).

Contract to Cut Stumpage on Mining Property: There was sufficient consideration to create a binding contract when the contract was executed to resolve a disagreement and a pending injunction and suit. Rogers v. Relyea, 184 M 1, 601 P2d 37 (1979).

Property Agreement Made Before Divorce: An agreement, the purpose of which is to facilitate the granting of a divorce without proper grounds existing, is void. Where proper grounds do exist, an agreement with respect to a property settlement cannot be said to perpetrate a fraud upon the court and will not be held void. Schulz v. Fox, 136 M 152, 345 P2d 1045 (1959).

Extension of Time for Payment of Debt: An agreement by a debtor to pay interest during the period for which maturity of the debt is extended by the creditor is based on a sufficient consideration, in that the creditor promises to forbear bringing suit during the time of the extension, and the debtor forgoes his right to pay the debt before the end of that time. Shipman v. Terrill, 84 M 322, 276 P 21 (1929).

Forbearance to Sue: Forbearance to sue is a sufficient consideration to support a contract, provided there be an agreement, express or implied, to that effect, mere nonaction being of no avail. Doorly v. Goodman, 71 M 529, 230 P 779 (1924). See also Emerson-Brantingham Implement Co. v. Anderson, 58 M 617, 194 P 160 (1920).

Relinquishment of Claim: Where both plaintiff and defendant in a suit looking to the specific performance of a contract to convey lands had a claim to three 40-acre tracts, the relinquishment by plaintiff of his claim to one of them in favor of defendant, for the purpose of effecting a compromise and facilitating the issuance of a patent, was sufficient consideration for the contract sued upon. Murray v. White, 42 M 423, 113 P 754 (1910).

MISCELLANEOUS

Noncompetition Agreement Unenforceable for Lack of Consideration: Four months after beginning employment with plaintiff produce company, Hernandez signed a noncompetition agreement and a nondisclosure agreement providing that Hernandez would not directly or indirectly compete with plaintiff company during employment and for a 2-year period following termination of employment. When the company began experiencing financial difficulties, Hernandez was laid off. Hernandez then began another produce business in the area, and plaintiff filed for a restraining order seeking to enforce the noncompetition agreement and to prevent Hernandez from operating a competing business. The District Court held that the agreement was enforceable and issued a preliminary injunction restraining Hernandez from competing with plaintiff and contacting any of plaintiff's customers and from disclosing any of plaintiff's trade secrets. Hernandez appealed on grounds that the noncompetition agreement was unenforceable as a matter of law. The Supreme Court held that, in the context of noncompetition agreements, clear evidence is required that the employee received good consideration in exchange for bargaining away some postemployment freedom to practice the profession or trade of choice. Here, the District Court found that continuation of Hernandez's employment and income with plaintiff was sufficient consideration, but the Supreme Court strictly construed the agreement and disagreed. Consideration exists if an employee enters a noncompetition agreement as a condition of employment or if an existing employee receives additional independent consideration for entering a noncompetition agreement, but Hernandez signed the agreement 4 months after being hired and received no additional independent consideration for signing, and past consideration cannot serve as good consideration for a present agreement. Therefore, the covenant not to compete was unenforceable as a matter of law for lack of consideration, and it was also error for the District Court to enter the preliminary injunction. The District Court was reversed. Access Organics, Inc., v. Hernandez, 2008 MT 4, 341 M 73, 175 P3d 899 (2008), distinguishing In re Wage Claim of Langager v. Crazy Creek Products, Inc., 1998 MT 44, 287 M 445, 954 P2d 1169 (1998).

Reciprocal Rights and Obligations Considered Sufficient Consideration to Sustain Shareholders' Agreement: Following his termination from employment with Bitterroot International Systems, Inc. (Bitterroot), Knutson sought to exercise his buyout rights under the shareholders' agreement. Bitterroot refused to pay on grounds of insufficient consideration, contending that the essential consideration for the shareholders' agreement was the exchange of stocks of equal value—an argument based on the premise that the stock exchange and the shareholders' agreement were one agreement. However, the shareholders' agreement was enforceable independent of the stock exchange between the parties, and the creation of reciprocal rights and obligations among the shareholders was sufficient consideration to sustain the shareholders' agreement; thus, the District Court did not err in concluding that the consideration was sufficient. Knutson v. Bitterroot Int'l Sys., Inc., 2000 MT 203, 300 M 511, 5 P3d 554, 57 St. Rep. 800 (2000).

Agreement to Convey Partnership Property Void for Lack of Consideration — Agreement to Fund and Forbearance in Dissolving Partnership Held Insufficient: Marsha and Mac formed M&M Walkers, a partnership for the breeding, raising, training, and marketing of Tennessee Walker horses. Their partnership agreement was oral and was sealed with a handshake. When Marsha became concerned about the amount of time and money that she was putting into the partnership, Mac executed a written conveyance of his share of partnership property, which said that if anything happened to him, Marsha was to get all the partnership property. After Mac died, Marsha tried to enforce Mac's written statement against his estate, but the District Court held the statement to be invalid for lack of consideration. The Supreme Court held that while the written instrument is presumptive evidence of consideration, that presumption could be rebutted by Mac's estate, which sought to invalidate the statement. Marsha contended that her agreement to continue funding the partnership was sufficient consideration, but the Supreme Court held that because she had a legal duty to contribute to the partnership in accordance with her share of the profits, her "agreement" was not sufficient consideration. Marsha also argued that her forbearance from dissolving the partnership was also sufficient consideration. Citing Rudio v. Yellowstone Merchandising Corp., 200 M 537, 652 P2d 1163 (1982), the Supreme Court noted that it had held that forbearance is sufficient consideration only if there is an agreement to forbear, and in this case, there was no evidence in the record that Marsha had made such an agreement with Mac. The Supreme Court therefore affirmed the District Court's finding that there was insufficient consideration to support Mac's written conveyance of the partnership's property to Marsha. Nitzel v. Wickman, 283 M 304, 940 P2d 451, 54 St. Rep. 684 (1997). See also St. v. Keys, 1999 MT 10, 293 M 81, 973 P2d 812, 56 St. Rep. 44 (1999).

Alleged Lack of Permit for Business — Legal Consideration: Lutes contended that the contract that he entered with Houdashelts for sale of an engine rebuilding business was void for failure of consideration because the sump system in the business did not have the proper permits and was therefore illegal. The District Court rejected the contention that the system was illegal. The Supreme Court held that the parties had each received good consideration in the simple sale of the business and that rescission was thus improper. Houdashelt v. Lutes, 282 M 435, 938 P2d 665, 54 St. Rep. 420 (1997).

Personal Check Valid Consideration: When the contract stated that $1,000 earnest money was due to be applied at closing, the plaintiff's check, rendered after the contract was signed, constituted valid consideration. Whether the defendants actually cashed the check is irrelevant to the question of its adequacy. Hofmann v. George, 267 M 292, 883 P2d 826, 51 St. Rep. 1007 (1994).

No Accord When Payment Stopped on Check — Evidence of Agreement Properly Excluded: In a dispute over the charges for the care and training of horses, the parties agreed that Watkins would accept $5,000 for his services. The Williamses gave Watkins two checks for $2,500, but they stopped payment on the second check and refused to tender the rest of the money on the basis that one of the horses had been mistreated. The jury returned a verdict in favor of Watkins for $20,191 for services. The Williamses argued that the lower court erred in initially excluding the accord and satisfaction affirmative defense. The Supreme Court ruled that there was no accord because of the Williamses' failure to pay the agreed-upon sum and that the District Court had been correct in excluding testimony concerning the agreement. Watkins v. Williams, 265 M 306, 877 P2d 19, 51 St. Rep. 489 (1994).

Repurchase Agreement Supported by Adequate Consideration: When a contract was construed as a whole, it was apparent that an option to repurchase real property was supported by adequate consideration as part of the original purchase contract. The sellers agreed to provide the buyers with water and access to the sellers' sewer facility. In return, the buyers paid a nominal consideration, agreed to maintain the sewer, and granted the sellers a repurchase option. Even nominal consideration will support an option contract. Edgar v. Hunt, 218 M 30, 706 P2d 120, 42 St. Rep. 1372 (1985).

Novation of Lease — New Lessee's Obligation Not Affected by His Ownership Rights: Franchisor took possession of franchise after franchisee indicated a desire to sell the franchise. To make the franchise more attractive to prospective purchasers, franchisor agreed with Godwin, who had leased equipment to the franchise, to make the rental payments on the equipment if Godwin would forgo repossession of the equipment. In a proceeding involving right to possession of the equipment and recovery of rental payments, although franchisor claimed a right under the Uniform Commercial Code to possession of the equipment under its security agreement with franchisee, the lower court correctly found franchisor liable for rent. That franchisor may have been entitled to possession did not preclude it from making a binding agreement with Godwin to take over franchisee's rental payments. Taylor Rental Corp. v. Ted Godwin Leasing, Inc., 209 M 124, 681 P2d 691, 41 St. Rep. 594 (1984).

Promise to Hold Hearing — Requirement of Independent Consideration: Plaintiff, a custodian at the Yellowstone County Courthouse for 18 years, was discharged. His employment was "at will". After discharge, he was told by the County Commissioners that he would be given a grievance hearing. A letter was later sent to plaintiff, informing him that no hearing would be held. The promise to hold a hearing was not supported by independent consideration. Therefore, it was not an enforceable promise under contract law. Section 39-2-503 (now repealed) was, in effect, a part of the employment contract between plaintiff and the county. A promise to hold a hearing, given at a later date, could not modify that part of the contract without independent consideration unless consented to by both parties in writing. Reiter v. Yellowstone County, 192 M 194, 627 P2d 845, 38 St. Rep. 686 (1981), distinguished in Boreen v. Christensen, 267 M 405, 884 P2d 761, 51 St. Rep. 1014 (1994).

Option Agreement — Sufficiency of Consent and Consideration: The defendant appealed from a judgment granting specific performance of an option agreement to the plaintiff and ordering the property involved conveyed to the plaintiff. On appeal, the Supreme Court rejected the defendant's contention that the writing involved was not an option agreement because it failed to meet the essential requirements for the validity of a contract. In particular, he contended that there was a lack of consent and that the consideration was legally insufficient. The Supreme Court found the actual payment of $1 and actual participation in a family corporate dissolution sufficient consideration for the agreement. A memorandum here acted as an offer, and a binding agreement resulted from action on that offer by the offeree. The trial court was affirmed. Van Atta v. Schillinger, 191 M 472, 625 P2d 73, 38 St. Rep. 426 (1981).

Lease Modification to Be Supported by Adequate Consideration: When lessee was entitled to two-thirds of all grain crops harvested, lessor-purchaser's claim that crop belonged to his seller was without merit because the lease was plain and unambiguous and needed no construction. Under the terms of the lease, proof of adequate consideration was required to force the lessee to remake that portion of the lease requiring him to give up his two-thirds share. Edwards v. Peavey Co., 170 M 45, 549 P2d 1082 (1976).

Lack of Consideration as a Defense: There was no basis for the contention that there was no consideration for the execution of a lease of a liquor establishment when in the lease there was a promise to pay a monthly rent, and also the lessee had released a mortgage on the liquor and beer licenses. Sears v. Barker, 126 M 101, 244 P2d 516 (1952).

Waiver of Seller's Right to Cancel Contract — Effect on Buyer's Use of Equity: Although the vendor under a contract to sell realty had given notice of cancellation of the contract pursuant to the forfeiture clause, vendor could thereafter waive the right to stand upon the forfeiture clause, in which case purchaser would have the right to retain possession and use his equity in the realty to form consideration for an agreement with third parties to purchase the equity. Hewitt v. Novak, 117 M 365, 158 P2d 627 (1945).

Past Consideration:

A promise founded partly on a past consideration and partly on an executory one is enforceable. W. T. Rawleigh Co. v. Miller, 105 M 456, 73 P2d 552 (1937).

Where a surgeon, after agreeing to perform an operation for a stated amount, was sought to be held under an alleged special contract subsequently made to the effect that he would guarantee that as a result of the operation plaintiff's hand would be rendered 100% efficient, the alleged special contract was void for want of consideration, the past consideration of the operation not covering the subsequent contract of warranty. Wilson v. Blair, 65 M 155, 211 P 289 (1922), overruled on another point in Klemens & Son v. Reber Plumbing & Heating Co., 139 M 115, 360 P2d 1005 (1961).

Want of Consideration — Burden of Proof: The burden of showing a want of consideration sufficient to support an instrument lies with the party seeking to avoid it. Farmers & Miners' St. Bank v. Probst, 81 M 248, 263 P 693 (1928); Morigeau v. Lozar, 81 M 434, 263 P 985 (1928); W. T. Rawleigh Co. v. Washburn, 80 M 308, 260 P 1039 (1927).

Continuation of Contract: Before plaintiff manufacturing company would enter into a renewal contract with a distributor of its goods, it required him to furnish a written contract of guaranty signed by responsible parties agreeing to pay the company on termination of the renewal contract the amount due it from the distributor at the time of the execution of the guaranty or what might become due thereafter. In consideration it promised to furnish the distributor with more goods. The guaranty was furnished, no further goods, however, being thereafter ordered. In an action to recover on the guaranty, trial court did not err in holding that there was a sufficient consideration to support the contract of guaranty of the distributor's indebtedness existing at the time of the execution of the contract, to wit, extension of time of payment, and that, in addition, the agreement as to payment of existing and future indebtedness, being indivisible, was based upon the further consideration that the company would sell more goods to the distributor, the fact that he thereafter did not order more goods did not affect its sufficiency. W. T. Rawleigh Co. v. Washburn, 80 M 308, 260 P 1039 (1927).

Consideration for an Enforcement of Implied Indemnity: Defendant, special administratrix of an estate, had a deposit as such in bank, and Weisner, claiming to have been appointed special administrator, made a claim for payment to him of the sum deposited. The bank notified defendant of this demand, and she requested it to refuse the demand and retain the deposit in her name until it could be ascertained who was entitled to it. The bank relied upon her implied promise to indemnify and save it harmless from all damage by reason of its compliance with her request and refused to comply with Weisner's demand. This constituted a good consideration for the implied promise, that is, a benefit conferred on Mrs. Nett and a prejudice suffered by the bank. Mrs. Nett was subsequently removed from her office, and, after her removal, Weisner recovered judgment against the bank for the amount of the deposit with interest from the date of his deposit. Mrs. Nett was not liable to reimburse the bank for the amount paid as interest, it having been the bank's duty without request to retain the deposit to meet its obligation to her. Murphy v. Nett, 51 M 82, 149 P 713 (1915).

Promise to Pay: Where the defendants were assignees of money to be made out of certain wood contracts and plaintiff, an employee of the assignor, procured from the latter an order on defendants for wages due him, whereupon the defendants on presentation of the order for payment took an assignment from plaintiff of all money due him for wages, paying part of the order in cash and giving him a due bill for the balance, the promise to pay the due bill was a sufficient consideration. Parnell v. Davenport, 36 M 571, 93 P 939 (1908).

Law Review Articles

Consideration, Promise to Perform That Which is Due a Third Party, Babbitt, 8 Mont. L. Rev. 86 (1947).

28-2-802. Extent to which existing legal or moral obligation is good consideration.

Case Notes

Obligation to Refund Payment for Gas Field Option: Plaintiff corporation rescinded a gas field option upon which it had paid $50,000 to defendant. After defendant failed to refund money due, plaintiff filed suit and was granted summary judgment for $71,320.55. On appeal, the Supreme Court held that, based upon the exhibits, affidavits, and briefs before the lower court, there was no evidence of a genuine issue of material fact. The escrow agreement and release based upon plaintiff's rescission were supported by adequate consideration since release from contract obligations and forbearance to sue are both adequate consideration. Ayers Oil and Gas, Inc., was a party to both the option and the release agreements as evidenced by Ayers' signature as president. Devon Oil & Gas Co., Inc. v. Ayers, 218 M 223, 707 P2d 523, 42 St. Rep. 1536 (1985).

Warranty Deed — Donative Intent — No Fraud or Lack of Consideration: Plaintiff filed an action to set aside a warranty deed to defendant transferring land that plaintiff had received originally as a tenant in common with defendant's father under the condition that they deed the land to defendant "when they were done with it". The District Court found that defendant was not guilty of deceit or false representation and that there was fair and adequate consideration for the transfer and refused to void the deed. The Supreme Court affirmed, holding that there was sufficient evidence to support the District Court's findings. Although the land was valued at $300,000 to $600,000 and the consideration for the transfer was $1, plaintiff's performance of the condition requiring transfer of the land to defendant, coupled with the payment of $1, constituted fair and adequate consideration in this case. Wright v. Blevins, 217 M 439, 705 P2d 113, 42 St. Rep. 1311 (1985).

Corporation Owners' Personal Guarantee of Corporation's Contract Obligation: Defendant corporation purchased plaintiff's business under a contract which provided that the inventory of the business would not be reduced in value below the amount still owed plaintiff under the contract. When plaintiff became worried about corporation's plan to carry out such a reduction, the owners of the corporation personally guaranteed payment of that part of the sale price still due plaintiff. There was consideration for the guarantee, in that plaintiff, in return for the guarantee, relinquished various legal rights of action which he would otherwise have had upon reduction of the value of the inventory. Therefore, the guarantee was not void for lack of consideration. Rudio v. Yellowstone Merchandising Corp., 200 M 537, 652 P2d 1163, 39 St. Rep. 1923 (1982), followed, with regard to sufficiency of mutual promises as valid consideration, in Kephart v. Portmann, 259 M 232, 855 P2d 120, 50 St. Rep. 771 (1993).

Counterclaim on Contract — Fulfillment of Preexisting Duties Not Consideration — Effect of Lack of Consideration: Plaintiffs contracted with defendant to build their log home. Before and after occupancy of the home, structural problems requiring repair occurred. At trial, defendant counterclaimed against the plaintiffs for his expenses in installing tie rods in the walls of the home. The plaintiffs had authorized the installation of the tie rods after a windstorm had shown the home to be unstable. Although noting the ratification of the agreement after the rods were installed, the Supreme Court also noted that the home remained unstable and that the rods may have been improperly installed. It said that defendant had a common-law duty to construct the home in a workmanlike manner, in a manner as to assure stability. The duty was not fulfilled even after the installation of the tie rods. Because a promise to perform a preexisting legal or contractual obligation is insufficient consideration for a promise made in return, consideration was lacking in the supplemental (tie rod installation) agreement. Under former Rule 41, M.R.Civ.P. (now superseded), a counterclaim may be dismissed where, upon the facts and the law, the claimant has shown no right to relief. With consideration lacking, the contract was unenforceable, and the defendant had no right to relief on his counterclaim. Estoppel will not support the defendant's claim without a showing of detrimental reliance, and it has no application when the omissions of the party claiming estoppel brought about the problem. Carroccia v. Todd, 189 M 172, 615 P2d 225, 37 St. Rep. 1437 (1980), followed in McGregor v. Cushman/Mommer, 220 M 98, 714 P2d 536, 43 St. Rep. 206 (1986).

Loan Consolidation — Valid Consideration: A note consolidating and representing an accumulation of previous loans involving the same bank is a prior debt sufficient to constitute consideration. Farmers St. Bank v. Johnson, 188 M 55, 610 P2d 1172 (1980).

Performance of Legal Obligation Not to Make One a Purchaser for Value: Performance by a child of the legal obligation to support an indigent parent may be sufficient consideration to support a conveyance to the child, but not such a consideration as to make the child a purchaser in good faith, and for a valuable consideration so as to entitle her to precedence over another purchaser. Kelly v. Grainey, 113 M 520, 129 P2d 619 (1942).

28-2-803. Consideration to be lawful — effect of illegality.

Case Notes

Alleged Lack of Permit for Business — Legal Consideration: Lutes contended that the contract that he entered with Houdashelts for sale of an engine rebuilding business was void for failure of consideration because the sump system in the business did not have the proper permits and was therefore illegal. The District Court rejected the contention that the system was illegal. The Supreme Court held that the parties had each received good consideration in the simple sale of the business and that rescission was thus improper. Houdashelt v. Lutes, 282 M 435, 938 P2d 665, 54 St. Rep. 420 (1997).

Charging More Than Contract Price Not Unlawful Consideration: Greenwood's claim that a trucker charged more to haul cattle than was agreed upon did not make the contract void for unlawful consideration. Greenwood v. Steve Nelson Trucking, Inc., 270 M 216, 890 P2d 765, 52 St. Rep. 151 (1995).

Contract to Perform County Officials' Duties: County Commissioners cannot contract away duties which under the law are required to be performed by county officials. Thus, where the County Commissioners contracted with an individual for the individual to abstract, make applications for tax deeds, give, post, and publish proper notice of applications, and issue tax deeds, the entire contract is void although in some instances the County Commissioners may properly contract for abstracting. Here, it was unlawful for the County Commissioners to contract away the duties of the County Clerk and County Treasurer relating to the making of applications for tax deeds, giving and posting of notice, and the issuing of tax deeds; therefore the entire contract is void. Kelly v. Silver Bow County, 125 M 272, 233 P2d 1035 (1951).

Wagering or Gambling Transactions — Grain Market: In order to invalidate a contract as a wagering or gambling transaction (instant case grain market transaction) both parties must have intended that, instead of delivery of the article, there should be a mere payment of the difference between the contract price and the market price, i.e., a settlement of the difference, burden of proof on the party assailing the transaction. H. Earl Clack Co. v. Oltesvig, 104 M 255, 68 P2d 586 (1937).

Nonseverable Contracts:

Where there is but a single consideration passing for the performance of several separate and distinct acts, one of which is unlawful, the entire contract, it not being severable, is void, particularly so where it is wholly executory. In re Cummings' Estate, 89 M 405, 298 P 350 (1931).

A contract by the terms of which plaintiff in effect agreed, for a consideration of $50,000, to furnish evidence which would enable defendant to either win two certain suits, or one of them, upon trial, or which would put the latter in such a position that he could force a favorable settlement of one or both of them, was an entire contract, and void as against the policy of the law. Hughes v. Mullins, 36 M 267, 92 P 758 (1907), distinguished in Haley v. Hollenback, 53 M 494, 156 P 459 (1917).

By Whom Illegality May Be Raised: Whenever the illegality of a contract sued upon appears, whether the showing be made by one side or the other, the disclosure is fatal to the case. McManus v. Fulton, 85 M 170, 278 P 126 (1929).

Effect on Parties to Contract: Where a party comes into court seeking to enforce a contract which is against public policy or is prohibited by law, the court will refuse to aid either party and will leave them where they have placed themselves, irrespective of the moral side of the controversy or the claim that justice demands that the one who has received money which belongs to the other should account for it. McManus v. Fulton, 85 M 170, 278 P 126 (1929).

Illegality Under Laws of Another State: A contract void in another state where made will not be enforced in Montana. McManus v. Fulton, 85 M 170, 278 P 126 (1929).

Suppression of Criminal Investigation: A contract which tends to suppress the investigation of a criminal offense is illegal, even though it does not amount to compounding of a felony, for the reason that it is contrary to good morals and public policy. Portland Cattle Loan Co. v. Featherly, 74 M 531, 241 P 322 (1925).

28-2-804. Written instrument presumptive evidence of consideration.

Case Notes

Unambiguous Release of Claims Against Attorney for Malpractice — Parties Bound by Terms of Release: Rich was injured in two automobile accidents and retained attorney Ellingson to represent her in claims against her insurer. The first claim was dismissed when Ellingson failed to serve a timely summons on the insurer after filing the claim. Rich sued Ellingson for malpractice and received a settlement of $175,000 from Ellingson's malpractice insurer. As part of the settlement, Rich signed a release providing that Ellingson was released from any future malpractice claims arising from representation of Rich. Rich's second accident claim was subsequently dismissed when the statute of limitations had run, and Rich again sued Ellingson for malpractice. Ellingson contended that the suit was barred by the release. The District Court agreed and dismissed the claim, and Rich appealed. Considering the document as a whole, the Supreme Court held that the release clearly and unambiguously barred future claims arising from Ellingson's representation of Rich in the multiple actions against Rich's insurer. Rich's latent discontent with the release, without more, was an insufficient basis upon which to premise an alteration of the express, unambiguous agreement. The District Court was affirmed. Rich v. Ellingson, 2007 MT 346, 340 M 285, 174 P3d 491 (2007). See also Hanson v. Oljar, 231 M 272, 752 P2d 187 (1988).

Landowner Subdivision Rights Precluded by Restrictive Covenants — No Oral Contract Without Consideration — Statute of Frauds Applied: Plaintiffs subdivided about 80 acres into a 40-acre water ski lake and five residential lots. Restrictive covenants provided that no more than six landowners would be allowed to use the lake, that five landowners would be owners of lots in the subdivision, and that one landowner would be the owner of a single family dwelling built on property immediately west of the lake. Plaintiffs initially intended to build on the west side of the lake and become the sixth landowner but changed their minds, sold the west side property, and decided to build on the south side instead. Four of the five landowners filed an affidavit that when they purchased their lots, they understood that plaintiffs would be the sixth landowner and that they had orally approved the relocation of plaintiffs' residence to the south shore. After plaintiffs' home was built on the south side, they sought a declaratory judgment that they were the sixth landowner under the restrictive covenants and thus had the right to use the lake. One dissenting landowner opposed the declaratory judgment and moved for summary judgment on grounds that the restrictive covenants prohibited plaintiffs from use of the lake. The District Court agreed and granted summary judgment. On appeal, the Supreme Court agreed that there was no evidence of consideration given to the landowners for modification of the covenants and that as a result, the modification benefited plaintiffs only. The right to use the lake ran with the land and was therefore a real property interest, and under the statute of frauds, any transfer of the right from one parcel to another had to be in writing or altered by an executed oral agreement. However, without consideration, there could be no oral contract, and without an oral contract, there could be no executed oral contract. Plaintiffs' argument that because they relied on oral agreements, equitable estoppel should prohibit defendants from denying plaintiffs' use of the lake also failed because equitable estoppel does not apply under the statute of frauds except when the statute would operate to perpetuate a fraud. The District Court was affirmed. Hanson v. Water Ski Mania Estates, 2005 MT 47, 326 M 154, 108 P3d 481 (2005).

Consideration Under Contract Creating Relationship of Lender and Approved Dealer for Making Housing Loans: A contract between the parties created a relationship of Green Tree Financial Corporation (Green Tree) as "lender" and Larson, doing business as Majestic Homes, Inc. (Majestic), as "approved dealer", for purposes of making federal housing loans pursuant to federal Housing and Urban Development (HUD) regulations. Majestic submitted an application to become an approved dealer, and Green Tree then approved Majestic as a dealer and required Majestic to enter into a dealer agreement that included terms expressly provided for by HUD regulations. In order to become and remain an approved dealer, Majestic promised to operate pursuant to HUD regulations—something that it was not otherwise obligated to do in the course of its business. Complying with HUD regulations and meeting other requirements of Green Tree constituted good consideration on the part of Majestic. In return for Majestic's conformance to federal regulations and a security interest in Majestic's assets, Green Tree agreed to perform a service for Majestic by reviewing and approving or rejecting credit applications that Majestic submitted on behalf of its customers. Majestic was allowed to hold itself out as an approved dealer, which provided a competitive advantage in the manufactured home business. The arrangement constituted a contractual relationship whereby the parties exchanged valuable consideration and was enforceable. This relationship is distinguishable from an indefinite requirements or output contract in which there is no exchange of obligations and no establishment of a lender-dealer relationship. Larson v. Green Tree Financial Corp., 1999 MT 157, 295 M 110, 983 P2d 357, 56 St. Rep. 618 (1999). See also Linn v. City County Health Dept., 1999 MT 235, 296 M 145, 988 P2d 302, 56 St. Rep. 922 (1999).

Agreement to Convey Partnership Property Void for Lack of Consideration — Agreement to Fund and Forbearance in Dissolving Partnership Held Insufficient: Marsha and Mac formed M&M Walkers, a partnership for the breeding, raising, training, and marketing of Tennessee

Walker horses. Their partnership agreement was oral and was sealed with a handshake. When Marsha became concerned about the amount of time and money that she was putting into the partnership, Mac executed a written conveyance of his share of partnership property, which said that if anything happened to him, Marsha was to get all the partnership property. After Mac died, Marsha tried to enforce Mac's written statement against his estate, but the District Court held the statement to be invalid for lack of consideration. The Supreme Court held that while the written instrument is presumptive evidence of consideration, that presumption could be rebutted by Mac's estate, which sought to invalidate the statement. Marsha contended that her agreement to continue funding the partnership was sufficient consideration, but the Supreme Court held that because she had a legal duty to contribute to the partnership in accordance with her share of the profits, her "agreement" was not sufficient consideration. Marsha also argued that her forbearance from dissolving the partnership was also sufficient consideration. Citing Rudio v. Yellowstone Merchandising Corp., 200 M 537, 652 P2d 1163 (1982), the Supreme Court noted that it had held that forbearance is sufficient consideration only if there is an agreement to forbear, and in this case, there was no evidence in the record that Marsha had made such an agreement with Mac. The Supreme Court therefore affirmed the District Court's finding that there was insufficient consideration to support Mac's written conveyance of the partnership's property to Marsha. Nitzel v. Wickman, 283 M 304, 940 P2d 451, 54 St. Rep. 684 (1997). See also St. v. Keys, 1999 MT 10, 293 M 81, 973 P2d 812, 56 St. Rep. 44 (1999).

Partial Enforcement of Promissory Note: Respondent signed a promissory note to her former husband in the amount of $2,000. She did not make any payments on the note. At trial, she testified that the only consideration she had received for the note was $1,000 and the use of a pickup. Thus, the lower court's decision to enforce the note only partially was not clearly erroneous. In re Marriage of Jones, 218 M 441, 709 P2d 158, 42 St. Rep. 1722 (1985).

Resolution of Dispute — Adequate Consideration: Defendant represented plaintiff in a civil action in federal court. The parties agreed that the case was originally handled on a 50% contingency fee basis. The case lasted almost 10 years. Plaintiff signed a formal authorization for defendant to settle. At the time of settlement, plaintiff contended the parties agreed to replace their 50% of net fee agreement with a percentage distribution of the gross settlement amount. At some point in time, the parties signed an agreement in defendant's handwriting providing for a 75%-25% split of the settlement. Defendant contended the second fee agreement failed for lack of consideration. On appeal, the Supreme Court found that there was evidence that both parties agreed to rescind the original agreement and enter the second because of a dispute over costs. The change from a net to a gross computation to eliminate the accounting problem was valid consideration for the second contract. Accounts that were in dispute were settled by the revised handwritten contract. Resolution of issues in dispute constituted consideration in support of the second fee agreement. The second fee agreement was a valid, enforceable contract supported by consideration. Eaton v. Morse, 212 M 233, 687 P2d 1004, 41 St. Rep. 1708 (1984).

Promissory Note — Lack of Consideration: Where respondent executed a mortgage and promissory note payable to appellant (the victim of alleged theft by the respondent's son) under belief that the note was to provide for her son's bail bond and the son was later released on his own recognizance, the court held that the promissory note was unenforceable for lack of consideration. Bartmess v. Bourassa, 196 M 231, 639 P2d 1147, 39 St. Rep. 56 (1982).

Lack of Consideration Not Proved: The court properly discounted an affirmative defense of lack of consideration when the record did not reflect even a scintilla of evidence tending to prove a lack of good and sufficient consideration. Archer v. LaMarch Creek Ranch, 174 M 429, 571 P2d 379 (1977).

Presumption Rebuttable — Waiver of Claim to Stock: This statutory presumption as applied to the contention of defendants in the instant case that the written waiver of plaintiff's claim to a block of stock in issue was evidence of consideration was sufficiently rebutted by the testimony of plaintiff and one of the defendants that nothing was paid for the waiver. "Waiver" requires two parties, and to be operative must be supported by an agreement founded on a valuable consideration, not necessarily monetary, a benefit to the waiving party or additional burden on the other being sufficient. Gerard v. Sanner, 110 M 71, 103 P2d 314 (1940).

Written Deed: A deed in writing is presumptive evidence of a consideration and therefore satisfactory. One who seeks to invalidate an instrument for want of consideration has the burden of proof. Hodgkiss v. Northland Petroleum Consol., 104 M 328, 67 P2d 811 (1937); Bielenberg v. Higgins, 85 M 69, 277 P 636 (1929); Morigeau v. Lozar, 81 M 434, 263 P 985 (1928); Guerin v. Sunburst Oil & Gas Co., 68 M 365, 218 P 949 (1923); Schauer v. Morgan, 67 M 455, 216 P 347

(1923); Hinerman v. Baldwin, 67 M 417, 215 P 1103 (1923); Dilts v. Brooks, 66 M 346, 213 P 600 (1923); Saint v. Beal, 66 M 292, 213 P 248 (1923).

Consideration When Pleaded to Be Proved Notwithstanding Presumption: While plaintiff in an action on the guaranty of a promissory note need not plead the consideration upon which it was based, where he does so and introduces proof in support of the allegation, the fact must be determined, not upon the presumption of consideration declared by this section, but upon the proofs offered. Doorly v. Goodman, 71 M 529, 230 P 779 (1924).

Burden of Proof: A deed to land furnishes presumptive evidence of a consideration and the burden of showing want of consideration sufficient to support it is upon him who seeks to invalidate it or avoid its effect. Lee v. Laughery, 55 M 238, 175 P 873 (1918).

Debt Instruments:

Under this section and 28-2-805 the plaintiff in an action on a promissory note is not required to show that the instrument had been given for a consideration or a consideration equal in point of value to its face, since the law presumes a sufficient consideration. Ford v. Drake, 46 M 314, 127 P 1019 (1912).

In an action on an instrument acknowledging an indebtedness and promising to pay it, a consideration need not be averred or proven independently of the proof of the contract itself. Noyes v. Young, 32 M 226, 79 P 1063 (1905).

Written Instrument Securing an Antecedent Debt: An instruction given in an action to recover damages for the conversion of certain personal property seized by defendant constable that a note secured by mortgage imported a valuable consideration and that the burden of showing the want of consideration rested upon the party seeking to invalidate it correctly stated the law, even though the mortgage was given to secure an antecedent debt. Borden v. Lynch, 34 M 503, 87 P 609 (1906).

28-2-805. Burden of proof of want of consideration.

Case Notes

Equipment Rental Agreement Creating Presumption of Consideration — Burden of Proof: Carl Weissman & Sons (CWS) agreed to rent a rock drill to D&L Thomas Equipment (D&L). A clause in the rental agreement required D&L to inspect the drill and notify CWS within 10 days specifying any defects and provided that if CWS was not notified, the drill would be conclusively presumed to have been accepted in its condition at the time of receipt. D&L contended that there were problems with the drill immediately after it was received, but did not notify CWS in writing within the 10-day period specified in the rental agreement. D&L asserted that because the drill malfunctioned and overheated, there was failure of consideration on CWS's part, rendering the agreement void. Under this section, the burden to prove failure of consideration was borne by D&L. Absent notification of defects, D&L accepted the drill in its condition upon receipt, so the Supreme Court affirmed the trial court's decision that there was sufficient consideration in the contract between the parties. Carl Weissman & Sons, Inc. v. D&L Thomas Equip. Corp., 1998 MT 213, 290 M 433, 963 P2d 1263, 55 St. Rep. 896 (1998).

Agreement to Convey Partnership Property Void for Lack of Consideration — Agreement to Fund and Forbearance in Dissolving Partnership Held Insufficient: Marsha and Mac formed M&M Walkers, a partnership for the breeding, raising, training, and marketing of Tennessee Walker horses. Their partnership agreement was oral and was sealed with a handshake. When Marsha became concerned about the amount of time and money that she was putting into the partnership, Mac executed a written conveyance of his share of partnership property, which said that if anything happened to him, Marsha was to get all the partnership property. After Mac died, Marsha tried to enforce Mac's written statement against his estate, but the District Court held the statement to be invalid for lack of consideration. The Supreme Court held that while the written instrument is presumptive evidence of consideration, that presumption could be rebutted by Mac's estate, which sought to invalidate the statement. Marsha contended that her agreement to continue funding the partnership was sufficient consideration, but the Supreme Court held that because she had a legal duty to contribute to the partnership in accordance with her share of the profits, her "agreement" was not sufficient consideration. Marsha also argued that her forbearance from dissolving the partnership was also sufficient consideration. Citing Rudio v. Yellowstone Merchandising Corp., 200 M 537, 652 P2d 1163 (1982), the Supreme Court noted that it had held that forbearance is sufficient consideration only if there is an agreement to forbear, and in this case, there was no evidence in the record that Marsha had made such an agreement with Mac. The Supreme Court therefore affirmed the District Court's finding that there was insufficient consideration to support Mac's written conveyance of the partnership's property to Marsha. Nitzel v. Wickman, 283 M 304, 940 P2d 451, 54 St. Rep. 684 (1997). See also St. v. Keys, 1999 MT 10, 293 M 81, 973 P2d 812, 56 St. Rep. 44 (1999).

Partial Enforcement of Promissory Note: Respondent signed a promissory note to her former husband in the amount of $2,000. She did not make any payments on the note. At trial, she testified that the only consideration she had received for the note was $1,000 and the use of a pickup. Thus, the lower court's decision to enforce the note only partially was not clearly erroneous. In re Marriage of Jones, 218 M 441, 709 P2d 158, 42 St. Rep. 1722 (1985).

Cancellation of Oil and Gas Lease: In an action by lessor to cancel an oil and gas lease where the requirement of a geological survey was a part of the consideration, it was necessary for the lessor to plead and prove the requirement. Braun v. Mon-O-Co Oil Corp., 133 M 101, 320 P2d 366 (1958).

Party Seeking to Invalidate Instrument: A written instrument is presumptive evidence of a good and sufficient consideration, and the burden of showing a want of consideration sufficient to support it lies with the party seeking to invalidate it on that ground. Sommer v. Wigen, 103 M 327, 62 P2d 333 (1936); Bielenberg v. Higgins, 85 M 69, 277 P 636 (1929); Farmers & Miners' St. Bank v. Probst, 81 M 248, 263 P 693 (1928); Morigeau v. Lozar, 81 M 434, 263 P 985 (1928); W. T. Rawleigh Co. v. Washburn, 80 M 308, 260 P 1039 (1927); Allen v. Mont. Ref. Co., 71 M 105, 227 P 582 (1924); Schauer v. Morgan, 67 M 455, 216 P 347 (1923); Dilts v. Brooks, 66 M 346, 213 P 600 (1923); Lundquist v. Jennison, 66 M 516, 214 P 67 (1923); Hinerman v. Baldwin, 67 M 417, 215 P 1103 (1923); Saint v. Beal, 66 M 292, 213 P 248 (1923); Dackich v. Barich, 37 M 490, 97 P 931 (1908).

Release of Mortgage: On attacking the release of a mortgage, which was given to him and released by himself, in the manner prescribed in 71-1-211, prior to the 1981 amendment, defendant assumed the burden of showing the existence of facts sufficient to warrant a court of equity in setting it aside. Mueller v. Renkes, 31 M 100, 77 P 512 (1904).

28-2-811. Applicability of rules concerning object to executory consideration.

Case Notes

Lease — Lessor to Renovate — Bilateral Contract: Plaintiff and defendant signed a lease under which plaintiff was to renovate the leased office space and the two were to confer on the renovation and mutually agree on the final plans. Disagreements as to the plans arose. Plaintiff claimed he had increasing difficulties in contacting defendant. Defendant rescinded the lease on the ground that it had continually invested more time and money than plaintiff and thus from a business standpoint the lease was no longer feasible. Plaintiff's attempt to contact defendant's president failed, and plaintiff sent a notice of default and sued. The lease was not an executory unilateral contract; it was a bilateral obligation under which defendant was required to work with plaintiff in designing and approving plans and act reasonably if defendant disapproved the plans. The verdict for plaintiff and denial of defendant's motions for a directed verdict and judgment notwithstanding the verdict were affirmed. Nicholson v. United Pac. Ins. Co., 219 M 32, 710 P2d 1342, 42 St. Rep. 1822 (1985).

28-2-812. How amount of executory consideration may be determined.

Case Notes

Person Specified to Determine Consideration: Under this statute it was competent for the plaintiff and defendant to agree upon and specify any person whom they might desire to determine the amount of plaintiff's fee. They might have designated the Sheriff of the county, a bank cashier, or any other person. If the testimony of the plaintiff is to be believed, they did agree upon the judge of the probate court of Silver Bow County. Fitzgerald v. Eisenhauer, 62 M 582, 206 P 685 (1922).

28-2-813. Determination by interested party.

Case Notes

Reasonable Consideration: The burden was upon the plaintiff to justify the total number of hours required to repair a crane, and where it had taken an unreasonable time to complete the work, plaintiff was entitled to be compensated for only such time as would reasonably have been required to do the work. Holland Constr. Co. v. Lampson, 165 M 356, 528 P2d 1327 (1974).

Proof of Reasonable Worth: Submission of time cards of all employees for the period that repairs were being made did not constitute proof of reasonable worth of an oral contract to repair a crane. Holland Constr. Co. v. Lampson, 165 M 356, 528 P2d 1327 (1974).

28-2-814. Effect of impossibility of designated exclusive method of determination.

Case Notes

Actions on Contract After Provisions Became Impossible: The plaintiff sued when a contingent contract term became impossible and the defendant did not agree to act on alternative terms available within the contract. The District Court granted summary judgment for the plaintiff. On appeal, the Supreme Court reviewed the contract dispute de novo and affirmed, noting that when using the "blue pencil" approach, one void term does not void a whole contract, and finding that the defendant unreasonably withheld agreement to alternative terms for which the contract provided. Boulder Hydro LP v. NW. Corp., 2018 MT 248, 393 Mont. 85, 428 P.3d 250.

Escalator Clause: Clause in timber contract stating without explanation "Timber price will be esculated [sic] each year" had a positive and definite meaning in the vicinity where the contract was made, and was not so ambiguous as to prevent enforcement of the contract. Pegg v. Mid-State Dev. Corp., 164 M 525, 529 P2d 1399 (1974).

Part 9
Written Contracts

Part Case Notes

Statute of Frauds — No Bar to Fraud Claim: Because plaintiffs were not merely seeking to enforce an oral agreement, the Supreme Court overturned a District Court finding that the statute of frauds precluded a plaintiff's claim of actual fraud, constructive fraud, and violations of the Montana Consumer Protection Act. Rather, the plaintiffs were alleging that the defendants misrepresented an existing real estate loan and serviced the loan in an unfair and deceptive manner, a claim that relied on the oral contract as evidence of alleged fraud but that did not rely on the validity of the oral contract itself. Morrow v. Bank of America, N.A., 2014 MT 117, 375 Mont. 38, 324 P.3d 1167. However, see Bank of America, N.A. v. Alexander, 2017 MT 31, 386 Mont. 305, 389 P.3d 1020, in which a claim that the parties modified an oral agreement was dismissed because it was barred by the statute of frauds.

Part Law Review Articles

The Modification of Written Contracts in Montana, Brown, 10 Mont. L. Rev. 63 (1949).

May a Real Estate Broker in Montana Collect a Commission Orally Promised Him?, Gray, 7 Mont. L. Rev. 28 (1946).

28-2-901. When contracts may be oral.

Case Notes

Limited Agreement Not to Prosecute for Deviate Sexual Conduct — Not Grant of Statutory Immunity — Independently Derived Evidence Applicable: The Jefferson County Attorney contractually agreed not to prosecute Myrhow for criminal acts related to an investigation of deviate sexual conduct by Marks, of which Myrhow had knowledge. However, until other incidents came to light as part of a separate investigation, Myrhow at no time related that he was involved in other unrelated incidents of deviate sexual conduct, including an incident committed prior to the contractual agreement. Myrhow contended that the immunity granted for his information regarding Marks's conduct also extended to his own conduct. The District Court properly found that Myrhow had been granted de facto immunity from prosecution for acts directly related to the Marks investigation, but that immunity was a limited, contractual, transactional immunity arising solely from the agreement not to prosecute, rather than from 46-15-331. The statutory immunity provided by 46-15-331 did not apply because that immunity is granted only when a witness is compelled to testify by court order, a circumstance inapplicable to this case. Because the evidence used to convict Myrhow was derived independently of the Marks investigation and independently of any immunized evidence Myrhow provided through his agreement with the County Attorney, the District Court correctly convicted Myrhow for deviate sexual conduct committed prior to the immunity agreement. St. v. Myrhow, 262 M 229, 865 P2d 231, 50 St. Rep. 1528 (1993).

Certainty as to Terms of Contract Required — Summary Judgment: In suit for breach of alleged oral contract between law partners to find "a place" in the law firm for any of their children who might wish to become lawyers, District Court granted defendant's motion for summary judgment. Supreme Court affirmed and held that the contract was unenforceable for lack of certainty as to its terms. Defendant's daughter's work for the firm as a law clerk did not perfect the alleged agreement. Plaintiff failed to raise a genuine issue of material fact to preclude entry of summary judgment. Bishop v. Hendrickson, 215 M 158, 695 P2d 1313, 42 St. Rep. 259 (1985). See also Janz v. Quenzer, 232 M 439, 756 P2d 1174, 45 St. Rep. 1178 (1988).

Employment Contract — Interpretation — Deduction of Payments Under Previous Contract: Appellant's contract of employment with Ollie May Vestal was terminated by her death. After her death, he entered into a new employment contract with the personal representative of her estate. Payments made under the original contract may not be deducted from payments due under the second contract of employment, even if payments made under the original contract were greater than the stated amount. Heintz v. Vestal, 185 M 233, 605 P2d 606 (1980).

Lease of State Lands: The Statute of Frauds barred testimony of an alleged oral agreement to sell or assign a state lease when written lease agreements provided specifically for a sublease. Montana law is clear that evidence of oral representations relating directly to the subject matter of a contract is not admissible to add to or alter the provisions of a written contract. Furthermore, the alleged oral agreement involved an agreement to transfer an interest in real property and thus is required to be in writing. Aye v. Fix, 176 M 474, 580 P2d 97 (1978).

28-2-902. Enforcement of contract not in writing through fraud.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Absence of Contract: Where no oral contract could be shown to exist defendants could not be estopped from affirmatively pleading the Statute of Frauds as a defense. Anderson v. KFBB Broadcasting Corp., 143 M 423, 391 P2d 2 (1964).

28-2-903. What contracts must be in writing.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

General 235
Agreements Not to Be Performed Within a Year 238
Agreements to Answer for Another's Debt 239
Agreements to Lease for More Than a Year 240
Agreements to Sell Interest in Real Property 241
Agreements Authorizing Broker to Sell or Purchase Real Estate for Commission 248
Admissibility of Evidence 251

GENERAL

Purchase of Property — Statute of Frauds — Claim Regarding Interest in Property Dismissed: Plaintiffs contended they had an oral agreement to lease and purchase real property from the defendants and demanded a portion of insurance proceeds paid to the defendants after a fire destroyed the real property at issue. The parties stipulated that there was no written contract between them to enter a lease for a period longer than 1 year or to purchase the property. Because the statute of frauds requires both leases for a period longer than 1 year and agreements to purchase the property to be in writing, the Supreme Court affirmed the District Court's grant of summary judgment in favor of the defendants. Hinebauch v. McRae, 2011 MT 270, 362 Mont. 358, 264 P.3d 1098.

Agreement for Commission for Sale of Real Estate Not in Writing — Summary Judgment Denying Commission Affirmed: Andersen assisted in the sale of Schenk's ranch, and although Schenk allegedly told Andersen that Andersen would receive a commission on the sale, no listing agreement was ever reduced to writing. The District Court granted summary judgment for Schenk on the commission issue because 28-2-903 provides that a real estate agreement authorizing an agent to transact for a commission is invalid if it is not in writing. Even though Schenk allegedly told Andersen that a commission would be earned if the ranch sold for at least $10 million, the sale price was $6.5 million, so Andersen could not hold Schenk to an agreement that Schenk never made. Absent a genuine issue of material fact, summary judgment for Schenk was affirmed. Andersen v. Schenk, 2009 MT 399, 353 M 424, 220 P3d 675 (2009).

Refusal to Enforce Unsubstantiated Oral Agreement to Dismiss Claim for Prescriptive Easement — Parol Evidence Rule and Statute of Frauds Inapplicable: Defendant contended that the District Court erred in failing to estop plaintiff from asserting claims for a prescriptive easement across defendant's property because an agent of plaintiff orally agreed to dismiss the claims and defendant relied on the promise to defendant's detriment. The District Court held that the parol evidence rule and the statute of frauds prohibited admission of evidence of an oral agreement to dismiss the case because there were written temporary access agreements in place and that defendant did not offer sufficient evidence to meet either a fraud or estoppel exception to the parol evidence rule. The Supreme Court found that the trial court reached the correct result, albeit for the wrongs reasons, by automatically applying the parol evidence rule and the statute of frauds without determining whether either rule applied. Actually neither rule barred admission of the evidence in this case, so the trial court was free to consider the merits of the existence of an oral contract without defendant having to prove the elements of fraud or detrimental reliance. Nevertheless, the trial court found defendant's story of an oral agreement to be unsubstantiated and correctly refused to enforce an oral agreement based on the facts before it. Brimstone Min., Inc. v. Glaus, 2003 MT 236, 317 M 236, 77 P3d 175 (2003).

Guidelines for Determining Whether Indian Tribe Has Waived Sovereign Immunity in Contract — Inapplicability of Statute of Frauds to Question of Subject Matter Jurisdiction: Plaintiff contended that he signed a 7-year contract with the Crow Tribe to provide consulting services and to act as a program manager for the planning and construction of a power plant on tribal property and that the tribe breached the contract and failed to pay him. The tribe moved to dismiss on grounds that the District Court lacked personal and subject matter jurisdiction because of the tribe's sovereign immunity. The District Court denied the motion but reserved the right to readdress the issue of subject matter jurisdiction. Following further discovery, neither party could produce a signed copy of the alleged contract. The District Court concluded that because the alleged contract was for employment for more than 1 year, the statute of frauds applied and noted that although plaintiff's performance would normally create an exception to the statute of frauds pursuant to the court's equitable powers, to exercise that power in this case would circumvent the tribe's sovereign immunity in contravention of federal law. The District Court further concluded that although there was an express agreement that was partially performed and that the agreement contained a waiver of tribal immunity from suit in state court, as indicated by affidavits submitted by plaintiff and the tribal presiding officer, because of the fact that a signed copy of the contract was not produced, there was insufficient evidence to overcome the presumption against waiver of tribal immunity, so the action was dismissed for lack of jurisdiction. Plaintiff appealed, and the Supreme Court reversed. The Montana statute of frauds in this section limits the enforceability of certain contracts but does not affect a District Court's subject matter jurisdiction, so a District Court need not consider the statute of frauds when determining subject matter jurisdiction; furthermore, the court does not need to invoke its equitable powers to find jurisdiction. Rather, the question facing the District Court was whether the tribe clearly and unequivocally waived its sovereign immunity. The Supreme Court found that plaintiff's complaint alleged sufficient facts that, if true, would vest the District Court with subject matter jurisdiction. The tribe produced no evidence to refute the affidavits or to controvert the recollections of the affiants. Absent any factual issue to resolve, the Supreme Court concluded that plaintiff presented undisputed evidence proving the establishment of a contract that included an unequivocal waiver of sovereign immunity, so dismissal of the complaint by the District Court on jurisdictional grounds constituted reversible error. Bradley v. Crow Tribe of Indians, 2003 MT 82, 315 M 75, 67 P3d 306 (2003). On remand, the District Court again granted Bradley's motion for summary judgment after holding that the tribe's motion to alter or amend was denied because the court did not rule on the motion within 60 days. The Supreme Court held that because there is no provision in former Rule 56, M.R.Civ.P. (now superseded), for entry of summary judgment by default, denial of the tribe's motion was erroneous, and because questions of fact existed regarding contract ambiguity and damages, the case was again reversed and remanded for further consideration. Bradley v. Crow Tribe of Indians, 2005 MT 309, 329 M 448, 124 P3d 1143 (2005).

Use of Shared Access Easement Following Amendment of Plat — Statute of Frauds Inapplicable: Two neighbors signed an agreement in the form of an amended plat to relocate a common boundary and share an access easement. Both parties used the access road after executing the agreement, so part performance occurred. A dispute arose, and the District Court concluded that the amended plat constituted an instrument in writing sufficient to satisfy the statute of frauds. On appeal, the parties questioned whether the memorialized amended plat was a sufficient instrument in writing to comply with the statute of frauds. The Supreme Court did not reach the question, concluding that because the parties performed their obligations under the agreement and because part performance occurred at least for a time, the statute of frauds could not defeat the parties' agreement to share the access easement. Although the District Court did not reach its conclusion on the same grounds, the conclusion was nevertheless correct, and the Supreme Court affirmed. Morton v. Lanier, 2002 MT 214, 311 M 301, 55 P3d 380 (2002).

Unsigned Contract for Five-Year Term as Resulting in "At Will" Employment — Basis for Termination: Plaintiff, general manager of a health club, sued the corporation owning the club and its principal shareholder for lost wages and profits when plaintiff was terminated from his position. The District Court held for defendants. The Supreme Court affirmed, holding that because a written agreement drafted by the parties had never been signed, the agreement was invalid and not binding upon the parties. Therefore, plaintiff's employment was for an unspecified term, or employment "at will", and the plaintiff could be terminated at will, without the defendant employer following the termination provisions of the unsigned agreement. Scott v. Eagle Watch Inv., Inc., 251 M 191, 828 P2d 1346, 48 St. Rep. 1136 (1991).

Unjust Enrichment — Misconduct by Defendant Required — Denial of Restitution to Defaulting Purchaser: Upon default by purchasers, seller resold the property. Purchasers sought restitution, contending it was unfair to allow seller to be unjustly enriched by selling the property twice. However, restitution is normally denied to a defaulting purchaser. (See Contract Damages in Montana Part II: Reliance and Restitution, Burnham, 45 Mont. L. Rev. 1 (1984).) Further, in order for the equitable doctrine of unjust enrichment to apply, plaintiff must show some element of misconduct or fault on the part of defendant. Schweigert v. Fowler, 240 M 424, 784 P2d 405, 47 St. Rep. 1 (1990). See also Owen v. Skramovsky, 2013 MT 348, 372 Mont. 531, 313 P.3d 205.

Best Evidence of Contract Not in Evidence — Existence of Enforceable Contract Not Proved: A trial court did not err in denying recovery for money paid out on a performance bond when: (1) the bond surety failed to admit the original bond or the original rider into evidence and could offer no certainty as to where the originals were and no reason as to why they were not produced; and (2) all oral testimony offered to prove the contents of the contract was disputed. USF&G Co. v. Cromwell, 237 M 72, 771 P2d 970, 46 St. Rep. 631 (1989).

Certainty as to Terms of Contract Required — Summary Judgment: In suit for breach of alleged oral contract between law partners to find "a place" in the law firm for any of their children who might wish to become lawyers, District Court granted defendant's motion for summary judgment. Supreme Court affirmed and held that the contract was unenforceable for lack of certainty as to its terms. Defendant's daughter's work for the firm as a law clerk did not perfect the alleged agreement. Plaintiff failed to raise a genuine issue of material fact to preclude entry of summary judgment. Bishop v. Hendrickson, 215 M 158, 695 P2d 1313, 42 St. Rep. 259 (1985). See also Janz v. Quenzer, 232 M 439, 756 P2d 1174, 45 St. Rep. 1178 (1988).

Unjust Enrichment — Recovery for Repudiated Contract Not Barred by Statute of Frauds: Where the plaintiffs failed to make a final payment to the defendant under a lease of property upon which the plaintiffs had spent considerable time and effort to grow wheat and the defendant thereafter wrongfully terminated the lease and retained the proceeds from the sale of plaintiffs' crop, the District Court erred in holding the plaintiffs' claim of unjust enrichment barred by the Statute of Frauds. Where one party repudiates a contract or breaches it by nonperformance, the injured party may seek restitution of the unjust enrichment whether the Statute of Frauds applies or not. Here the defendant breached the lease, and the theory of unjust enrichment applies. Robertus v. Candee, 205 M 403, 670 P2d 540, 40 St. Rep. 1391 (1983).

Part Performance:

Over a period of years, grantor, a 95-year-old woman, had deeded various parcels of land near her home to several relatives. She filed a complaint against grantees, alleging that the land had been conveyed in return for their promise to support her and that they had failed to live up to their agreement. As relief, grantor sought either damages or, in the event that the agreement was determined to be unenforceable under the Statute of Frauds, return of the land. Grantees denied the existence of any agreement and pleaded the Statute of Limitations as a defense. The District Court granted grantees' motion for summary judgment and further ruled that grantor's claims were barred by the Statute of Limitations. The Supreme Court reversed in part, ruling that grantor was entitled to present evidence on two of her claims because Montana law provides for the enforcement of a grantor support agreement, that there was a genuine issue of fact as to whether or not such an agreement had been made, and that the trial court's ruling on the Statute of Limitations was premature. Additionally, the court ruled that grantor had no claim for return of the land since, if an agreement existed, grantor's partial performance of that agreement rendered the Statute of Frauds inapplicable, and if no agreement existed, grantor was not entitled to any relief. Sands v. Nestegard, 198 M 421, 646 P2d 1189, 39 St. Rep. 1101 (1982).

Part performance which will avoid the Statute of Frauds may consist of an act done in the performance of the contract which puts the party performing it in such a situation that the nonenforcement of the agreement would be a fraud upon him. Eccles v. Kendrick, 80 M 120, 259 P 609 (1927); McIntyre v. Dawes, 71 M 367, 229 P 846 (1924).

Memorandum — Defined: A memorandum may consist of several writings. Milkovich v. Orr, 529 P2d 1382 (1975) (apparently not reported in Montana Reports).

Party Charged: The "party to be charged" means the party to be charged in the particular suit. Johnson v. Elliot, 123 M 597, 218 P2d 703 (1950).

Form of Instrument: No particular form of language or instrument is necessary to constitute a memorandum or note in writing under Statute of Frauds, and a receipt may be sufficient, and two or more writings properly connected may be considered together. Johnson v. Ogle, 120 M 176, 181 P2d 789 (1947).

Memorandum Executed After Services Performed: Generally, memorandum executed after services have been performed is sufficient to satisfy requirement of Statute of Frauds. Johnson v. Ogle, 120 M 176, 181 P2d 789 (1947).

"Invalid" Defined: The word "invalid" as employed in this section means that the contract referred to, unless in writing, is of no force or effect and hence such contract cannot be relied upon or furnish evidence for any purpose. Mahoney v. Lester, 118 M 551, 168 P2d 339 (1946).

Life Insurance — Change of Beneficiary: This section applies to matters required by the Statute of Frauds, not to private contracts where parties have stipulated that certain things shall be in writing; hence an attorney's authority to request a change of beneficiary in a life insurance policy need not be in writing. Conlon v. N. Life Ins. Co., 108 M 473, 92 P2d 284 (1939).

Executory Contracts:

Complete performance of an oral contract by one of the parties to it takes the agreement out of the operation of the Statute of Frauds under which it otherwise would be invalid. Besse v. McHenry, 89 M 520, 300 P 199 (1931).

Where an oral agreement to adopt was fully performed by the mother upon surrender of the child, and thereafter by the child until the death of the adopting parties, it was taken out of the Statute of Frauds by full performance. Gravelin v. Porier, 77 M 260, 250 P 823 (1926).

AGREEMENTS NOT TO BE PERFORMED WITHIN A YEAR

Agency and Ratification to Be in Writing: The plaintiffs initiated a suit to have certain water rights distributed pursuant to the residuary clause of a will. The defendant argued that the rights had previously been assigned to him by a release that he signed as agent of the deceased and that the deceased had subsequently orally affirmed. The Supreme Court held that the original release had to be in writing because it called for payments for 32 years and therefore was subject to the statute of frauds. The court went on to hold that since the release had to be in writing, then the creation of an agency and the subsequent ratification also had to be in writing and that since they were not, the water rights passed under the will. Moore v. Adolph, 242 M 221, 789 P2d 1239, 47 St. Rep. 730 (1990).

Employment Contract — Interpretation — Deduction of Payments Under Previous Contract: Appellant's contract of employment with Ollie May Vestal was terminated by her death. After her death, he entered into a new employment contract with the personal representative of her estate. Payments made under the original contract may not be deducted from payments due under the second contract of employment, even if payments made under the original contract were greater than the stated amount. Heintz v. Vestal, 185 M 233, 605 P2d 606 (1980).

Full Performance by One Party: Oral contract extending for more than 1 year was taken out of the operation of this section by full performance by one party. Davis v. Davis, 159 M 355, 497 P2d 315 (1972).

Extension of Contract Period: Where employer had been awarded construction contract to be completed in 360 days and hired employee under oral agreement almost immediately thereafter, fact that contract was later amended resulting in an extension of time to correct construction error did not make it invalid under this section, and therefore did not affect employee's right to recover salary upon being fired, since extension of time was not contemplated in the original contract; fact that employee had worked 7 weeks also removed contract from bar of statute under doctrine of part performance. Fox v. Fifth W., Inc., 153 M 95, 454 P2d 612 (1969).

Estoppel: Promisor was estopped from raising Statute of Frauds as defense to action by promisee under oral agreement to divide equally income received from soil bank payments for 8-year period in view of evidence showing glaring inconsistencies in promisor's position. Daley v. Daley, 150 M 432, 436 P2d 88 (1968).

Optional Continuation of Business Relationship: Under the rule that where a contract is capable of performance within 1 year it is not invalid under the Statute of Frauds because not in writing, an oral agreement made between plaintiff and defendant in the late fall to run a band of lambs as partners until they became yearlings (in the spring following) and if they should then take a "notion" they would continue the arrangement, was wholly optional with the parties and might have been fully executed within 1 year and hence was not invalid under this section. Miles v. Miles, 76 M 375, 247 P 328 (1926).

Evidence of Oral Agreement: An oral agreement which by its terms is not to be performed within 1 year from its making is void for any purpose, and part performance does not take it out of the statute; hence it was error to permit evidence of the terms of such an agreement to be introduced in an action to recover the reasonable value of services rendered in pursuance of the agreement. Dreidlein v. Manger, 69 M 155, 220 P 1107 (1923), distinguished in Besse v. McHenry, 89 M 520, 300 P 199 (1931).

Agreement to Be Performed Within a Year: An agreement to be performed within 1 year need not be in writing. Awbery v. Schmidt, 65 M 265, 211 P 346 (1922).

Revenues to Pay Cost of Building: Where a contract between plaintiff and defendant as tenants in common provided for the erection of a house on the common property by defendant at his own expense, requiring him to make an equal division of the rents between them when the rents received equaled one-half the cost, and there was an immediate performance by plaintiff by his surrender to defendant of the entire control of the property, with all revenues to be derived from it, until the stipulated rent should pay for the erection of the building, the contract was enforceable irrespective of the provisions of subsection (1) of this section. Ayotte v. Nadeau, 32 M 498, 81 P 145 (1905).

AGREEMENTS TO ANSWER FOR ANOTHER'S DEBT

Statute of Frauds Inapplicable to Theories of Liabilities Based on Fraud or Negligent Misrepresentation: A feed company sought information from debtor's banker regarding debtor's ability to pay his extremely large feed bill. The banker made affirmative statements that debtor could pay and that even if payment was not made, the company would have an automatic feed lien that would be paid first. The company relied on the statement and extended credit, but when the banker was called later to confirm that a $40,000 check would be paid, he advised that the check would not be honored. The company filed a complaint against the bank, alleging fraud or negligent representation. The bank contended that the cause should be dismissed pursuant to this section because the company alleged in its complaint that the bank failed to honor the check. However, the statute of frauds applies to liabilities based on contract, and because the case in tort was not based on a written agreement, this section did not apply. Phil-Co Feeds, Inc. v. First Nat'l Bank in Havre, 238 M 414, 777 P2d 1306, 46 St. Rep. 1380 (1989).

Vendor's Agreement to Pay Vendee's Debt to Mortgagee as Part of the Consideration for Return of the Property: Where a vendor orally agreed with vendee to pay off vendee's mortgage for a loan with which vendee erected a filling station on the property, as part of the consideration for return of the property (including the newly erected improvement), vendor's oral agreement was not within the Statute of Frauds. Downing v. Crippen, 114 M 436, 138 P2d 575 (1943).

Oral Insurance Policy Neither "Special" Nor "General" Guaranty Within Statute of Frauds: The insolvency and direct suit clause under an oral insurance contract for public liability is not a special guaranty because no special promise is made by the insolvency or direct suit clause to the particular injured third party who sues upon a judgment against the insured, nor is it a general guaranty so worded that anyone to whom it is presented accepts a general promise to be answerable for a debt or duty in case of failure or default of another person who is liable in the first instance. Its primary intent is to protect the insured rather than the third person, and its purpose is indemnity rather than guaranty. Austin v. New Brunswick Fire Ins. Co., 111 M 192, 108 P2d 1036 (1940).

Guaranty Contract: "Guaranty" is a collateral agreement or undertaking on the part of one person called the guarantor to pay a debt or perform an obligation in the event of the failure of the principal, who is himself liable in the first instance for such payment or performance to a third person called the guarantee; it must be in writing and based upon a consideration. Doorly v. Goodman, 71 M 529, 230 P 779 (1924).

Interpretation of Language Used in Agreement: If the language employed in making a promise to pay the debt of another is such that by immemorial usage and common custom it has but one meaning, the character of the promise is to be determined as a question of law; where, however, it is such that reasonable minds might differ as to the meaning intended to be conveyed, its character is to be determined as a question of fact. Breidenbach v. Upper Valley Orchards Co., 57 M 247, 187 P 1008 (1920).

Parent Company as Guarantor of Independent Contractor: Where goods were ordered by and delivered to an independent contractor performing work for defendant company, and charged to him on plaintiff's books, and plaintiff in a former action to recover their price brought suit against the contractor alone, looking to him primarily and the company only as guarantor, the promise of the manager of the company to see that plaintiff "got his money" was a collateral one which, not being in writing, was void under the Statute of Frauds. Breidenbach v. Upper Valley Orchards Co., 57 M 247, 187 P 1008 (1920).

Main Purpose of Promise: Wherever the main purpose and object of the promise is not to answer for another, but to subserve some purpose of promisor's own, his promise is not within the statute, although it may be in form a promise to pay the debt of another, and although the performance of it may incidentally have the effect of extinguishing the liability of another. McGowan Commercial Co. v. Midland Coal & Lumber Co., 41 M 211, 108 P 655 (1910); Carothers v. Connolly, 1 M 433 (1871).

Contract to Pay Debt: A contract to pay another's debt must be in writing. McGowan Commercial Co. v. Midland Coal & Lumber Co., 41 M 211, 108 P 655 (1910).

Payment to Third Person: As the law stood in 1895, the oral acceptance of a written order, whereby a creditor requested his debtor to pay the amount of his debt to a third person, was not deemed to be within the Statute of Frauds as constituting a promise to pay the debt of another. An agreement by such third person not to file a lien upon the debtor's premises would be a good consideration for such acceptance. Lavell v. Frost, 16 M 93, 40 P 146 (1895).

What Constitutes Agreement: A letter containing the following: "You will please make out the record in the P. case, and we will guaranty the payment of your fees by him, P." expresses an agreement within the meaning of the statute. O'Bannon v. Chumasero, 3 M 419 (1879).

Oral Agreement to Pay Lien: The verbal promise of a party who has a claim against a ditch, to pay the lien of another against the ditch, is not within the Statute of Frauds. Carothers v. Connolly, 1 M 433 (1871).

AGREEMENTS TO LEASE FOR MORE THAN A YEAR

Presumption of Yearly Lease — Partial Performance: The parties entered into an oral agreement for lease of grazing land with monthly payments. When a dispute arose, the plaintiff claimed the lease was month-to-month, and the defendants claimed the lease was a 3-year lease. The jury was instructed, pursuant to 70-26-201, that when the terms of a lease are not specified, the lease is presumed to be for 1 year. The jury found in favor of a yearly lease and awarded damages to the defendants. The Supreme Court affirmed. The partial performance of an oral lease for a term beyond that allowed by the Statute of Frauds will take it out of the operation of the statute. Hill v. Turley, 218 M 511, 710 P2d 50, 42 St. Rep. 1783 (1985).

Evidence Not Admissible: An oral lease for more than a year is invalid and evidence of the agreement and secondary evidence of its contents cannot be introduced. Roseneau Foods, Inc. v. Coleman, 140 M 572, 374 P2d 87 (1962).

Lease for One Year: A 1-year oral lease under 70-26-201 is not within the Statute of Frauds, and a continuous renewal thereof under 70-26-204 would also not be within the Statute. Roseneau Foods, Inc. v. Coleman, 140 M 572, 374 P2d 87 (1962).

Term of Lease Where No Time Stated: Under 70-26-201 it is possible to have an oral lease for at least 1 year without an expression as to time therein. Roseneau Foods, Inc. v. Coleman, 140 M 572, 374 P2d 87 (1962).

Application to Executed Part: Statute of Frauds has no application to executed portion of oral lease. Roseneau Foods, Inc., v. Coleman, 140 M 572, 374 P2d 87 (1962).

When Statute May Not Be Invoked: Under an oral contract of lease of a tract of land for a term of 2 years, the lessee remained in possession for the entire term. In an action to recover a balance of $275 of the total rent of $300 stipulated for, the lessee's defense was that the contract was void under the Statute of Frauds because not in writing. Held, that the landlord having fully performed his part of the agreement and the tenant having occupied the premises for the full term, the contract was taken out of the Statute and the tenant was not in position to invoke its invalidity to shield him from payment of the rent. Besse v. McHenry, 89 M 520, 300 P 199 (1931).

Requirements: An agreement for the leasing of real property for a period longer than 1 year must be in writing under this section, and an agreement which must be in writing is not valid if executed by an agent unless the latter is authorized in writing to enter into it, in the absence of ratification by his principal. Sunburst Oil & Gas Co. v. Neville, 79 M 550, 257 P 1016 (1927).

Effect of Part Performance: Part performance of a parol lease of real property for a term beyond that allowed by the Statute of Frauds takes it out of the operation of the Statute, and taking possession, making alterations in the building, and paying the rent agreed upon for a considerable period of time constitute part performance. Kettlekamp v. Watkins, 70 M 391, 225 P 1003 (1924).

What Constitutes Part Performance: Plaintiff's acts in relinquishing his option on a new business location on the oral promise of the defendant, his landlord, that if he would do so he (defendant) would renew the lease plaintiff then held for an additional 3 years, a provision which rendered the promise void under the Statute of Frauds, was such a part performance as removed the agreement from the operation of the Statute. McIntyre v. Dawes, 71 M 367, 229 P 846 (1924).

What Constitutes Lease Agreement: A contract between tenants in common for the erection of a house on the common property by one of them at his own expense, and requiring him to make an equal division of the rents when the rents received equaled one-half the cost, is not a contract of leasing within the meaning of subsection (1)(d) of this section. Ayotte v. Nadeau, 32 M 498, 81 P 145 (1905).

Extension of Lease Agreement: Where one of several lessors of a building had no written authority to sign an extension agreement containing an agreement for a conveyance of the land, for one of the other lessors, as required by subsection (1)(d) of this section, such extension agreement, which was for more than a year, was invalid. Landt v. Schneider, 31 M 15, 77 P 307 (1904).

AGREEMENTS TO SELL INTEREST IN REAL PROPERTY

District Court Error in Finding Purchaser Did Not Act in Good Faith — Summary Judgment Awarded: The plaintiff company filed a quiet title action to mineral rights it had purchased from a personal representative. Heirs of the estate objected, claiming that 72-3-618 did not protect the plaintiff's purchase because the plaintiff failed to act in good faith when it did not locate the will disposing of the estate. The District Court granted summary judgment in favor of the heirs. The plaintiff appealed to the Supreme Court, which reversed, ruling that because the plaintiff had no actual knowledge of any restrictions on the personal representative's authority, the purchase had been made in good faith and was therefore protected under 72-3-618. The Supreme Court ordered the District Court to enter summary judgment on behalf of the plaintiff. Northland Royalty Corp. v. Engel, 2014 MT 295, 377 Mont. 11, 339 P.3d 599.

Letters of Offer and Acceptance on Real Property Sale Exchanged — Terms of Response Immaterial — Contract for Sale Enforced by Specific Performance: Two sisters owned 78 acres as tenants in common. The defendant sister, who held a majority interest, sent a letter to the plaintiff sister, offering to sell her the majority interest or to purchase the minority interest. The letter set a deadline for a response and requested it be sent to a specified third party. Before the deadline expired, the plaintiff sister wrote back directly to her sister and agreed to purchase the majority interest. However, the defendant sister claimed she had decided to sell the property to their brother. The plaintiff sister sued, seeking specific performance of the contract. The defendant sister argued that the plaintiff had not accepted the original offer because she had not responded to the third party as requested. The District Court concluded that, as phrased in the letter, the request to direct the response to the third party was not a condition precedent to acceptance. On appeal, the Supreme Court agreed that the letters exchanged by the sisters formed a contract and that the mode of acceptance was not a condition precedent. The court affirmed the District Court's grant of specific performance ordering the defendant sister to sell her majority interest to the plaintiff. Olsen v. Johnston, 2013 MT 25, 368 Mont. 347, 301 P.3d 791.

Representation of Contract to Another Party — Use of Statute of Frauds to Later Deny Contract in Real Estate Transaction Precluded: The Kluvers and McRaes commenced a lawsuit alleging that several power companies had contaminated their ground water. A mediation session between the parties ended with an e-mail detailing a memorandum of understanding for a settlement agreement from the Kluvers' attorney to an attorney for the power companies, including the transfer of real estate between the parties. Although Karson Kluver expressed relief to the McRaes that the case was over, the Kluvers later claimed that the settlement agreement was tentative and invalid. Although there was no signed writing to show the Kluvers assented to the agreement prepared by their attorney at the mediation conference, because Karson Kluver later represented that a settlement had been reached to another party, he could not invoke the statute of frauds to deny the agreement. Kluver v. PPL Montana, LLC, 2012 MT 321, 368 Mont. 101, 293 P.3d 817.

Purchase of Property — Statute of Frauds — Claim Regarding Interest in Property Dismissed: Plaintiffs contended they had an oral agreement to lease and purchase real property from the defendants and demanded a portion of insurance proceeds paid to the defendants after a fire destroyed the real property at issue. The parties stipulated that there was no written contract between them to enter a lease for a period longer than 1 year or to purchase the property. Because the statute of frauds requires both leases for a period longer than 1 year and agreements to purchase the property to be in writing, the Supreme Court affirmed the District Court's grant of summary judgment in favor of the defendants. Hinebauch v. McRae, 2011 MT 270, 362 Mont. 358, 264 P.3d 1098.

Agreement for Commission for Sale of Real Estate Not in Writing — Summary Judgment Denying Commission Affirmed: Andersen assisted in the sale of Schenk's ranch, and although Schenk allegedly told Andersen that Andersen would receive a commission on the sale, no listing agreement was ever reduced to writing. The District Court granted summary judgment for Schenk on the commission issue because 28-2-903 provides that a real estate agreement authorizing an agent to transact for a commission is invalid if it is not in writing. Even though Schenk allegedly told Andersen that a commission would be earned if the ranch sold for at least $10 million, the sale price was $6.5 million, so Andersen could not hold Schenk to an agreement that Schenk never made. Absent a genuine issue of material fact, summary judgment for Schenk was affirmed. Andersen v. Schenk, 2009 MT 399, 353 M 424, 220 P3d 675 (2009).

No Evidence of Contract to Sell Real Property — Specific Performance Precluded: Zier and Lewis entered negotiations for Zier to buy Lewis's Montana ranch. Negotiations broke down after Zier's counteroffer was rejected. Nevertheless, Zier contended that Lewis had agreed to sell the property through Lewis's business manager, and that Zier was entitled to specific performance. The District Court concluded that no contract existed and granted summary judgment for Lewis. On appeal, the Supreme Court affirmed. A valid contract requires mutual consent of both parties, and the parties must agree on the same thing. Acceptance of an offer on terms varying from those offered is a rejection of the offer and puts an end to negotiations unless there is assent to the new terms. In this case there was no contract because there was no consent to the terms of a contract. Without a valid and binding contract, a party may not obtain specific performance. Therefore, the District Court did not err in granting summary judgment for Lewis. Zier v. Lewis, 2009 MT 266, 352 M 76, 218 P3d 465 (2009). See also Austin v. Cash, 274 M 54, 906 P2d 669 (1995).

Ratification of Void Deeds — Authority of Agent to Convey Property — Title Properly Quieted: Defendant third party raised three challenges to a District Court's conclusion that deeds voided by forgery during transfer were nevertheless ratified by subsequent actions of the parties and contended that the court erred by quieting title to plaintiff. The first argument dealt with the fact that one of the parties never received proper written authority to convey the property to plaintiff, so ratification was voided under the statute of frauds. The Supreme Court noted that an agreement to sell an interest in property must be in writing and that an agent's authority to sell property must also be in writing. However, the agency relationship may arise either by precedent authorization or by subsequent ratification. In this case, the warranty deeds constituted subsequent written authority for conveyance of the property, so the statute of frauds was not violated for want of written authorization. The second argument was that the criteria for ratification were not satisfied, but after examining the chain of title, the Supreme Court found that the personal actions of the principal ratified the deed and that the criteria for ratification were satisfied. The third argument was that defendant was prejudiced as a third party by ratification, but that argument did not prevail because defendant could not have been prejudiced since defendant's interest in the property was invalid both prior to and after ratification and defendant could have become aware of the void deeds by conducting a title check and avoiding the problem. Lastly, title was properly quieted in plaintiff because defendants with prior interests in the property stipulated that they no longer claimed any right, title, or interest in the property. Plaintiff's deed was superior because it was the first to be recorded and had been ratified, and plaintiff was therefore entitled to have quiet title to the property. The District Court was affirmed. Erler v. Creative Fin. & Inv., LLC, 2009 MT 36, 349 M 207, 203 P3d 744 (2009). See also U.S. v. Heinszen, 206 US 370 (1907), Audit Serv., Inc. v. Francis Tindall Constr., 183 M 474, 600 P2d 811 (1979), Safeco Ins. Co. v. Lovely Agency, 200 M 447, 652 P2d 1160 (1982), and Moore v. Adolph, 242 M 221, 789 P2d 1239 (1990).

Timely Exercise of Third-Party Option to Purchase Real Property — No Breach of Buy-Sell Agreement: A provision in a buy-sell agreement between Palmer and Bahm allowed a third party 72 hours after the Palmer-Bahm agreement was signed to decide whether to purchase a strip of land from Bahm that was contained in the parcel covered by the agreement. Although the third party did not complete the transaction or enter into a separate buy-sell agreement within 72 hours, the buy-sell agreement required only that a purchase decision be made within 72 hours. Uncontroverted evidence showed that the third party made a timely decision to purchase the strip and communicated that decision to Bahm, so Bahm did not violate the agreement with Palmer or break the covenant of good faith and fair dealing by selling the strip to the third party. Palmer v. Bahm, 2006 MT 29, 331 M 105, 128 P3d 1031 (2006).

Landowner Subdivision Rights Precluded by Restrictive Covenants — No Oral Contract Without Consideration — Statute of Frauds Applied: Plaintiffs subdivided about 80 acres into a 40-acre water ski lake and five residential lots. Restrictive covenants provided that no more than six landowners would be allowed to use the lake, that five landowners would be owners of lots in the subdivision, and that one landowner would be the owner of a single family dwelling built on property immediately west of the lake. Plaintiffs initially intended to build on the west side of the lake and become the sixth landowner but changed their minds, sold the west side property, and decided to build on the south side instead. Four of the five landowners filed an affidavit that when they purchased their lots, they understood that plaintiffs would be the sixth landowner and that they had orally approved the relocation of plaintiffs' residence to the south shore. After plaintiffs' home was built on the south side, they sought a declaratory judgment that they were the sixth landowner under the restrictive covenants and thus had the right to use the lake. One dissenting landowner opposed the declaratory judgment and moved for summary judgment on grounds that the restrictive covenants prohibited plaintiffs from use of the lake. The District Court agreed and granted summary judgment. On appeal, the Supreme Court agreed that there was no evidence of consideration given to the landowners for modification of the covenants and that as a result, the modification benefited plaintiffs only. The right to use the lake ran with the land and was therefore a real property interest, and under the statute of frauds, any transfer of the right from one parcel to another had to be in writing or altered by an executed oral agreement. However, without consideration, there could be no oral contract, and without an oral contract, there could be no executed oral contract. Plaintiffs' argument that because they relied on oral agreements, equitable estoppel should prohibit defendants from denying plaintiffs' use of the lake also failed because equitable estoppel does not apply under the statute of frauds except when the statute would operate to perpetuate a fraud. The District Court was affirmed. Hanson v. Water Ski Mania Estates, 2005 MT 47, 326 M 154, 108 P3d 481 (2005).

Attempted Sale of Parcel in Violation of Contract — Plantiff Allowed to Block Sale: Defendants contracted to purchase several parcels of property from plaintiff. When defendants ended up in default, defendants decided to sell one of the parcels to pay off part of the contract balance. Plaintiff attempted to block the sale, and the District Court confirmed plaintiff's ability to do so under the terms of the contract. Defendants appealed, but the Supreme Court affirmed. A provision of the contract allowed the subsequent sale of the parcels by defendants, but only after the principal balance was paid. Because defendants were in default when the attempted sale was made, sale of the tract was not permitted by the terms of the contract. The District Court did not err in holding that plaintiff had a contractual right to block the sale. Weter v. Archambault, 2002 MT 336, 313 M 284, 61 P3d 771 (2002).

Defaulting Buyer Under Unambiguous Written Contract Cannot Rely Upon Expectations Not Covered by Contract to Avoid Contract — Disposition of Downpayment Amounts Paid and Due — County Not Liable for Negligent Misrepresentation as to Recordability of Deeds and Seller's Title Insurer Not Liable for Loss in Marketability: Documents for the sale and purchase of two sections of land unambiguously showed, and it was undisputed, that the resale of 20-acre parcels by the buyer, the immediate acceptance by the county of 20-acre resale deeds of a type that would make subdivision review unnecessary, and the ability to resell without having to undergo subdivision review were not parts of the bargain. The parties knew that these things were contemplated, but the documents did not refer to them or make them a part of the contract. Before the contract was made, the county indicated that it would accept the 20-acre resale deeds. The deal fell through when the county changed its position after the contract was signed. The buyer failed to pay the whole downpayment, and the seller terminated the contract and kept the paid portion of the downpayment. Precontract discussions on the matter must be disregarded as parol evidence because the documents were unambiguous and did not refer to the matter. The buyer was not entitled to rescind the contract and have the paid portion of the downpayment returned based on mutual mistake or failure of consideration. There was no mutual mistake because the parties knew that it was not a certainty that the county would accept the deeds. There was no failure of consideration because the resale, county acceptance of the deeds, and avoidance of subdivision review were not part of the written contract. In addition, the need for a subdivision review would not make the land unmarketable; at most, its market value decreased and it would take longer to sell it. Furthermore, a party in default is not entitled to rescission. The seller was entitled to terminate the contract. The seller was also entitled to keep an amount of the paid portion of the downpayment equal to the amount by which the contract price for the land exceeded the market value of the land at the time of the breach. The seller was not entitled to keep the remainder of the paid portion of the downpayment or to a judgment for the unpaid portion of the downpayment because the contract did not provide for that remedy. The county was not liable in tort to the seller for negligent misrepresentation, and the buyer's title insurance company was not liable to the seller for the loss in the marketability of the land caused by the need for subdivision review. Yellowstone II Dev. Group, Inc. v. First Am. Title Ins. Co., 2001 MT 41, 304 M 223, 20 P3d 755 (2001), overruled in Mary J. Baker Revocable Trust v. Cenex Harvest St., Cooperatives, Inc., 2007 MT 159, 338 M 41, 164 P3d 851 (2007), to the extent that Yellowstone II held that the determination of whether a term in a contract is ambiguous is not a question involving parol evidence.

Possession of Real Property Insufficient to Grant Title Against Good Faith Purchasers — No Adverse Possession Shown: In 1989, the Luloffs bought part of a ranch from the Manweilers by a deed that excluded "Tract B". The Luloffs mistakenly assumed that Tract B was the part of the ranch that had been occupied by the Blackburns for approximately 4 years. When the Luloffs later discovered that Tract B was another part of the ranch, they brought an action to have the Blackburns evicted, and the District Court granted summary judgment. The Supreme Court held that summary judgment was correctly granted because there was no contract between the Manweilers and the Blackburns satisfying the statute of frauds for the sale of the property to the Blackburns. The Supreme Court held that the Blackburns' mere possession was insufficient against the Luloffs, who had purchased the ranch as bona fide purchasers in good faith, because they were without notice of any claim of title by the Blackburns. The Supreme Court noted that the Blackburns could not make a claim of title because they had mere possession, which did not satisfy the requirements for adverse possession because the Blackburns had not paid taxes upon the property. Luloff v. Blackburn, 274 M 64, 906 P2d 189, 52 St. Rep. 1124 (1995).

Failure of Counteroffer Under Statute of Frauds — Handwritten Additions by Sellers' Agent Not Subscribed by Sellers — Part Performance and Equitable Estoppel Inapplicable: After Austin rejected a counteroffer on property that he was interested in buying, the agent, Everett, went to the office of the listing agent, Young, who contacted one of the two owners of the property by telephone. That owner, Cash, said that she would consider sale of the property for an additional $5,000 but that she would first have to discuss it with her brother, the other owner. Everett then added a handwritten paragraph to the rejected counteroffer, noting the sale of all of the property for $115,000 and faxed it back to Austin. When Austin received the revised counteroffer, he believed that it had been signed by Cash and, believing that a binding contract had been made, lowered the sale price of other property that he owned in California. Cash and her brother subsequently received and accepted an offer for their property from a different buyer, whereupon the Austins filed a lis pendens against Cash's property, preventing its sale to the other buyer. The Supreme Court held that because neither the sellers nor their agents signed or initialed the handwritten addition to the counteroffer, the contract was not properly subscribed by the sellers or their agents and therefore did not satisfy the statute of frauds. The Supreme Court also held that the action of the Austins in reducing the sale price of their California properties was an act in contemplation of eventual performance of the contract and not an act of part performance itself. For this reason, part performance did not excuse the application of the statute of frauds. The Supreme Court also held that in order for a court to order specific performance of a contract, there had to be a binding contract in the first place and held that because the additional language to the sale contract had not been subscribed, no contract existed. Finally, the Supreme Court held that promissory estoppel is inapplicable when a contract is clearly within the statute of frauds. Austin v. Cash, 274 M 54, 906 P2d 669, 52 St. Rep. 1119 (1995).

Inducement to Purchase Property Based on Promise of Road Improvements — Directed Verdict Improper: Plaintiffs claimed they were fraudulently induced to enter contracts to purchase land when seller orally promised to improve access roads to county grade. The District Court granted defendants a directed verdict, relying on Kelly v. Ellis, 39 M 597, 104 P 873 (1909), in holding that when there was no allegation of failure to keep all promises made in the written agreement, the statute of frauds precluded admission of evidence of an oral promise directly related to the contents of the contract. However, plaintiffs relied on a certificate of survey that showed county grade easements, a letter from defendants' attorney agreeing to hold a title insurance company harmless from any claims arising from purchasers' access problems, and the representation by a realtor that roads would be upgraded to county road standards. These representations constituted a conflict in evidence precluding directed verdict, and the District Court erred in taking from the jury the issue of whether plaintiffs were fraudulently induced to enter the contracts. Dew v. Dower, 237 M 476, 774 P2d 989, 46 St. Rep. 981 (1989), following Majers v. Shining Mtn., 230 M 373, 750 P2d 449, 45 St. Rep. 283 (1988), Majers v. Shining Mtn., 219 M 366, 711 P2d 1375, 43 St. Rep. 16 (1986), Dodds v. Gibson Prod. Co., 181 M 373, 593 P2d 1022 (1979), and Goggans v. Winkley, 154 M 451, 465 P2d 326 (1970). Following a trial subsequent to Dew, infra., the District Court determined that defendant did fraudulently induce plaintiffs to purchase property by misrepresenting the quality of the road that she intended to build as access to the property and further awarded monetary damages to each plaintiff. On appeal, defendant contended, among other things, that the trial court erred in admitting, without first requiring plaintiffs to prove intent to defraud, parol evidence that defendant orally promised to improve the road and also erred in determining that defendant intended to defraud plaintiffs by inducing them to enter into contracts for deed. However, defendant waived the right to appeal the parol evidence question by failing to object at trial, and substantial evidence that defendant had no intention to perform the promises to improve the road was sufficient to prove defendant's intent to defraud. Dew v. Dower, 258 M 114, 852 P2d 549, 50 St. Rep. 454 (1993).

Oral Contract for Purchase of House — Part Performance — Statute of Frauds Inapplicable — No Refund to Purchasers on Default: Defendant agreed to sell home to friends upon a $10,000 downpayment and assumption of defendant's loan. Plaintiffs did not qualify for assumption, so defendant prepared lease for plaintiffs' signature. They refused to sign because it was not a contract for deed. Defendant allowed plaintiffs to take occupancy, and they made sporadic payments for 4 years. Defendant's patience waned when the bank exercised acceleration provision for delinquencies. Plaintiffs sued for refund of payments. The court found an oral contract for deed. The Statute of Frauds was inapplicable because defendant was, at all times, willing to effect sale and transfer of the home. He was not required to refund plaintiffs' payments. Since no lease was ever signed and no rental relationship created, landlord and tenant law was inapplicable. Hayes v. Hartelius, 215 M 391, 697 P2d 1349, 42 St. Rep. 457 (1985).

Attorney Fees — Not Costs — Timeliness: The defendants signed a contract to purchase a tract of land from plaintiffs. The contract provided for attorney fees to the prevailing party in an action commenced on the contract. Plaintiffs filed suit alleging that under the contract and various oral agreements, defendants had agreed to pay a real estate commission to plaintiffs. The trial court granted summary judgment to defendants, holding that written evidence of an agreement to pay a commission did not exist. No notice of entry of judgment was ever filed. Defendants later moved to set an attorney fee award. The trial court ruled that under Title 25, ch. 10, attorney fees were not recoverable costs and that the motion for costs was not timely, as it was not filed within 5 days of judgment. On appeal, the Supreme Court held that attorney fees were awardable under the contract and that defendants' motion was essentially a motion to amend judgment under former Rule 59(g), M.R.Civ.P. (now superseded). The motion was timely made since no notice of entry of judgment was ever filed. Cook v. Harrington, 203 M 479, 661 P2d 1287, 40 St. Rep. 580 (1983), followed in In re Estate of Lande, 1999 MT 179, 295 M 277, 983 P2d 316, 56 St. Rep. 701 (1999).

Equitable Principles — Estopped From Invalidating Agreement Under Statute of Frauds: Agreement between plaintiff and defendant to sell property was valid under the Statute of Frauds even though the written instrument was signed only by the plaintiff and defendant's wife when plaintiff had made an irretrievable change in position and defendant had secured an unconscionable advantage or inflicted an unjust or unconscionable loss upon the plaintiff. Bolz v. Myers, 200 M 286, 651 P2d 606, 39 St. Rep. 1747 (1982).

Performance of Oral Agreement by Party as Precluding Statute of Frauds Defense: The parties were married in 1973. They entered a prenuptial agreement providing that the real and personal property of each would remain separate. In 1974, defendant brought a quiet title action against his sisters. He executed a handwritten agreement with plaintiff that if she would finance the legal expenses of the action he would give her 10% of the land or the value thereof. He was successful, and the parties entered into an oral agreement containing the same provisions for appellate costs. The trial court found that defendant owed plaintiff 20% of the value of the land and that value be determined at the time he elected to pay and be based on 20% of the value of all the land. The defendant contended there was insufficient evidence to support the finding of the oral agreement for the additional 10% of the land. The weight of evidence and credibility of witnesses were for the District Court to determine. There is no preponderance of evidence contrary to the District Court's finding. Defendant contends the oral agreement is barred by the Statute of Frauds because it is an agreement for the sale of real property and could not be performed in a year. The District Court held and the Supreme Court affirmed that the Statute of Frauds does not bar the oral agreement because plaintiff fully performed her part of the bargain. Kartes v. Kartes, 195 M 383, 636 P2d 272, 38 St. Rep. 1941 (1981).

Independent Investigation Clause Not to Preclude Justifiable Reliance on Representations: Defendants owned property in Flathead County. Water for the property came from a neighbor's well for which they paid him $8 per month. No written agreement existed concerning the water supply. Defendants listed the property for sale with Tri-City Real Estate. Inserted in the listing contract in the printed space following "water" were the words "community $8/mo." Plaintiffs were interested in the land and looked at it. They asked both defendants and the realtor about the water supply and were told it came from a community well. Plaintiffs wanted written verification of the interest in the water system. The realtor told them he would obtain a copy of the register of the well for them. Plaintiffs continued asking for the register but never received it. Plaintiffs signed a contract for deed to buy the property which had been prepared by the realtor's attorney. The contract contained an "independent investigation" clause, which stated that plaintiffs had investigated the property and entered the contract based upon that investigation and that there were no other agreements or representations concerning the property. The neighbor stopped supplying water, and plaintiffs were forced to dig their own well. They sought recovery from defendants. It was held that defendants were responsible for the negligence of their agents in the sale as related to the community water interest. The Supreme Court held that the "independent investigation" clause did not preclude a holding that the plaintiffs justifiably relied on the representations of the realtor. Parkhill v. Fuselier, 194 M 415, 632 P2d 1132, 38 St. Rep. 1424 (1981), distinguished in Garrison v. Averill, 282 M 508, 938 P2d 702, 54 St. Rep. 454 (1997).

Change in Roadway — Oral Agreement Barred: An oral agreement to change the pathway of a road established by a written instrument is barred by this section since it involves an agreement to transfer an interest in real property. Silva v. McGuinness, 189 M 252, 615 P2d 879, 37 St. Rep. 1401 (1980).

Validity of Typewritten Signature — Real Estate Contract: The seller of a tract of land negotiated with and made offers to one party, then withdrew the offers and negotiated with a second party. The second party made the seller an offer which the seller accepted by telegram. The first party sued the seller who then made an agreement with the first party and sent a notice of rescission to the second party. The second party then sued both the first party and the seller. On appeal, the narrow issue was whether the typewritten name at the bottom of the telegram of acceptance of a buyer's offer was a sufficient subscription to satisfy the Statute of Frauds. Because the seller must have intended to authenticate her written name on the telegram to satisfy the Statute of Frauds, the court looked to the wording of the acceptance. It found the words "Please consider this my written acceptance. . ." on the telegram, words suggested by the buyer, indicative of a mutual intent to be bound. Hillstrom v. Gosnay, 188 M 388, 614 P2d 466, 37 St. Rep. 1087 (1980).

Adverse Possession — Parol Grant: A parol grant of real property can serve as a foundation for a claim of title by adverse possession, notwithstanding the Statute of Frauds. Swecker v. Dorn, 181 M 436, 593 P2d 1055 (1979).

Part Performance Exception Limited: A contract for the sale of real estate is invalid unless it or some note or memorandum thereof is in writing subscribed by the parties to be charged. Claimed acts of partial performance sufficient to take an otherwise unenforceable contract out of the Statute of Frauds must be unequivocally referable to that contract. Such acts as obtaining financing and making studies of the real property have been held insufficient part performance to preclude the defense of the Statute of Frauds. Schwedes v. Romain, 179 M 466, 587 P2d 388 (1978).

Lease of State Lands: The Statute of Frauds barred testimony of an alleged oral agreement to sell or assign a state lease when written lease agreements provided specifically for a sublease. Montana law is clear that evidence of oral representations, relating directly to the subject matter of a contract, are not admissible to add to or alter the provisions of a written contract. Furthermore, the alleged oral agreement involved an agreement to transfer an interest in real property and thus is required to be in writing. Aye v. Fix, 176 M 474, 580 P2d 97 (1978).

Specific Performance of Agreement to Sell Land: The Statute of Frauds does not abridge the power of any court to compel the specific performance of any agreement for the sale of real property in case of part performance thereof. Dyksterhouse v. Doornbos, 172 M 461, 564 P2d 1293 (1977).

Option Agreement — Full Performance: Evidence of payment of money pursuant to the purchase of real estate for the purpose of persuading seller to hold the deal open for a certain period of time, and the subsequent actions of the seller in holding the property off the market, were sufficient to establish a valid option agreement, as well as to show that the agreement had been fully performed. Lynch v. Shields, 165 M 396, 529 P2d 348 (1974).

Performance or Memorandum Required: Buyer's tender of payment and a conveyance to be executed by seller did not constitute such performance or memorandum as to take an oral agreement to sell land out of the operation of this section, where seller did not accept the tender or execute the conveyance. Myers v. Bendewald, 160 M 338, 502 P2d 412 (1972).

Sale of Stock: In action for breach of contract trial court improperly refused to direct verdict for defendant seller since oral contract for sale of stock in ranch corporation was invalid under this section and equitable estoppel was not applicable since there was no language amounting to representation or concealment of material facts by seller. Mueller v. Svejkovsky, 153 M 416, 458 P2d 265 (1969).

Specific Performance Not Obtainable: Where defendants had never agreed in writing to take less than $1,000 as a down payment on the sale of their ranch, granting of summary judgment against plaintiff who had offered less and sought specific performance of sales contract was proper, especially after plaintiff had failed to reply in time to defendants' demand for admissions. Naegli v. Daniels, 145 M 323, 400 P2d 896 (1965).

Sufficiency of Memorandum: The fact that the memorandum required by this section does not specify when the deed shall be furnished does not defeat the sufficiency of such memorandum because 28-3-601 implies that it must be furnished within a reasonable time after the other party performs. Hughes v. Melby, 135 M 415, 340 P2d 511 (1958).

Written Authorization of Agent Required: An alleged contract to sell realty on monthly installment basis which would require 15 years for performance, allegedly made by owner's agent, was invalid under Statute of Frauds in the absence of a writing signed by owner, either agreeing to sell or authorizing agent to so contract. Mahoney v. Lester, 118 M 551, 168 P2d 339 (1946); O'Neill v. Wall, 103 M 388, 62 P2d 672 (1936).

What May Constitute Memorandum: A letter written by vendee to vendor pending fulfillment of an escrow agreement which was claimed invalid under the Statute of Frauds, in which letter the writer acknowledged he had agreed to purchase the land in question, and that unless the vendor should fulfill the condition of the escrow agreement within a given time the transaction would be called off, was a sufficient memorandum in writing by the party to be charged, to bar the operation of the Statute under this section. Conner v. Helvik, 105 M 437, 73 P2d 541 (1937).

What Constitutes an Interest in Land: A permanent right-of-way across the land of another for ditch purposes constitutes an interest in the real property, an easement, which under this section must be in writing; whereas a license to so use the land does not create such an interest, may be given by parol, and is revocable at will even though the licensee has expended time and money in acting thereon. Rentfro v. Dettwiler, 95 M 391, 26 P2d 992 (1933).

What Constitutes Sufficient Part Performance: Where plaintiff in an action for the cancellation of a promissory note claimed by defendant to have been given in consideration of an oral contract to convey real property never entered into possession, and defendant neither pleaded nor proved that by plaintiff's alleged part performance of the contract consisting of having the property assessed in his name and paying the taxes thereon for several years, he (defendant) had been placed in such a situation that nonperformance would be a fraud upon him, the acts of plaintiff did not constitute such part performance as would take the contract out of the Statute of Frauds. Eccles v. Kendrick, 80 M 120, 259 P 609 (1927).

Promissory Note Not a Memorandum: A promissory note (or mortgage) said to have been given in connection with the oral transfer of real property is not a sufficient memorandum to take the contract out of the operation of the Statute of Frauds, within the meaning of this section, declaring such a contract invalid unless a note or memorandum thereof be in writing and subscribed by the party to be charged. Eccles v. Kendrick, 80 M 120, 259 P 609 (1927).

Exception — Complete Performance: Where an agreement for an exchange of easements such as those involving irrigation ditches has been fully executed, it is valid though not in writing; this section being intended to prevent frauds and not to encourage their perpetration. Babcock v. Gregg, 55 M 317, 178 P 284 (1918).

When Evidence Admissible: Where plaintiff sought to recover money on a demand loan, defendant was properly allowed to introduce testimony tending to show that the money paid him by the former was not a loan, but a partial payment upon the purchase price of real property sold under an oral contract, even though such contract of purchase was invalid and therefore unenforceable under the Statute of Frauds. Perkins v. Allnut, 47 M 13, 130 P 1 (1913).

Grant of Interest in Real Estate: Where the interest acquired by a party under a contract is a right to have a conveyance of land to himself, the transfer of that interest by whatever name called is a grant of interest in real property which must be in writing. Flinner v. McVay, 37 M 306, 96 P 340 (1908).

Part Performance: An oral contract to sell land that has been partly performed is mutual, for both parties are reciprocally bound, the one to convey, and the other to pay the purchase price. Cobban v. Hecklen, 27 M 245, 70 P 805 (1902).

License to Use Land: A license to lay a water main over or through land may be given by parol, as no interest in the land is given, but the license may be revoked at any time, even after it has been executed and money advanced in reliance thereon. Great Falls Water Works Co. v. Great N. Ry., 21 M 487, 54 P 963 (1898).

Express Verbal Contract for Sale of Real Estate: An express verbal contract for the sale of real estate is void under the Statute of Frauds. Ryan v. Dunphy, 4 M 342, 1 P 710 (1882), affirmed in 116 US 491, 29 L Ed 703, 6 S Ct 486 (1886).

AGREEMENTS AUTHORIZING BROKER TO SELL OR PURCHASE REAL ESTATE FOR COMMISSION

Application of Procuring Cause Doctrine to Exclusive Listing Agreements: The procuring cause doctrine, which permits a broker to show that the broker's part of the contract was performed and that the principal reaped a benefit from the efforts, is not confined to consideration of nonexclusive listing agreements. It applies in all situations unless the parties agree otherwise in the listing contract. Lane v. Smith, 255 M 218, 841 P2d 1143, 49 St. Rep. 974 (1992), clarifying Flinders v. Gilbert, 141 M 442, 378 P2d 385 (1963), and followed in Hall & Hall, Inc. v. Hyde, 264 M 190, 870 P2d 1362, 51 St. Rep. 257 (1994).

Date of Lease-Purchase Agreement as Effective Date of Sale in Determining Broker's Commission: When negotiated within the time parameters of a listing agreement, the date on which a lease-purchase agreement is entered into is the effective date of sale for purposes of determining a broker's commission. Lane v. Smith, 255 M 218, 841 P2d 1143, 49 St. Rep. 974 (1992), followed in WRB-West Associates, Inc. v. Madison Addition Inv. Ltd. Partnership, 270 M 498, 893 P2d 340, 52 St. Rep. 329 (1995).

Reliance on Statute of Frauds Not Perpetuation of Fraud Against Broker: Kraft, a broker, alleged that the seller, Hodson, had orally modified their listing agreement in a manner allowing Kraft to negotiate with the ultimate buyer of the property, thereby entitling Kraft to a commission. The Supreme Court held that any modification to the contract had to be in writing or else the statute of frauds would be rendered a nullity. Kraft v. Hodson, 254 M 262, 836 P2d 1234, 49 St. Rep. 792 (1992), followed in WRB-West Associates, Inc. v. Madison Addition Inv. Ltd. Partnership, 270 M 498, 893 P2d 340, 52 St. Rep. 329 (1995).

Failure of Broker to Disclose When Commission Due: A party who contracted with a real estate broker for an exclusive listing was unaware that a transfer of title in lieu of foreclosure would constitute a conveyance entitling broker to a commission, and the broker never informed the party of that fact. Summary judgment was improper where there may have been a genuine issue of material fact as to whether the broker breached a fiduciary duty to disclose. Ellingson Agency, Inc. v. Baltrusch, 228 M 360, 742 P2d 1009, 44 St. Rep. 1598 (1987).

Buyers' Default Irrelevant Under Terms of Contract — Modification of Contract to Be in Writing: Real estate agent arranged sale of defendants' ranch to a partnership consisting of agent's brother and other investors. Sellers received $210,000 from sale before buyers' default. The agent, who had received one-half of his brokerage commission, brought suit to recover remainder of fee under written contract. The District Court granted the agent's motion for summary judgment. The Supreme Court found no material issues of fact in dispute and the District Court's ruling correct as a matter of law and affirmed summary judgment. The Supreme Court held that under the terms of the contract, the broker was entitled to the commission when the sale was made and that a sale was finalized when the sellers entered into a binding sales contract. It was not necessary for the entire purchase price to be paid. The sellers' claim that the broker orally waived the remainder of his commission in return for the opportunity to relist the property is not sufficient to prevent summary judgment because such modification of a written contract must be in writing. Taylor v. Weingart, 214 M 282, 693 P2d 1231, 41 St. Rep. 2474 (1984).

Real Estate Listing — Time Limits Binding: Defendant entered a real estate listing agreement with plaintiff. The agreement was entered June 25, 1979, and was to expire June 25, 1980, with a 180-day grace period for a buyer put in contact with the seller by the realtor. This period ended December 22, 1980. On October 23, 1979, defendant entered a buy/sell agreement with the Gerhardts, who were shown the ranch by a realtor affiliated with the defendant. The agreement was contingent on the Gerhardts' selling their ranch. The Gerhardts occupied defendant's ranch as tenants. Gerhardts were not able to sell their ranch until December 31, 1980, and on January 29, 1981, they bought defendant's ranch. Defendant refused to pay the real estate commission, and this suit followed. It is a generally accepted rule that a buyer is financially "able" only when he can command the necessary funds to complete the purchase within the time allowed by the offer. Here, the buyers were not able to purchase until they sold their ranch. Courts have generally strictly followed the time limits in listing agreements. An exception may occur if surrounding circumstances indicate the time provisions were waived by the parties or if the seller interfered with the sale. Nothing in this case suggests either, and judgment for the defendant was affirmed. Property Brokers, Inc. v. Loyning, 201 M 309, 654 P2d 521, 39 St. Rep. 2128 (1982). See also WRB-West Associates, Inc. v. Madison Addition Inv. Ltd. Partnership, 270 M 498, 893 P2d 340, 52 St. Rep. 329 (1995), distinguishing Snyder v. Schram, 547 P2d 102 (Oreg. 1976).

When Statute Inapplicable: Where an agreement authorizing the plaintiff to sell real estate for a commission was not in writing, as required by this section, but was nevertheless acknowledged by the defendant and acted on by it, this statute was inapplicable. This statute may not be used so as to defeat its purpose to prevent the commission of a fraud. Ryckman v. Wildwood, Inc., 197 M 154, 641 P2d 467, 39 St. Rep. 378 (1982).

Application of Statute to Real Estate Sale — Collection of Agent's Commission: In an action by the plaintiff real estate brokerage firm to recover a real estate sales commission, the District Court did not err in denying the defendant's motion for a directed verdict based upon a failure of the plaintiff to comply with the Statute of Frauds. Even though no contract for deed was ever signed, the "contract" at issue in an action to collect a real estate sales commission is the real estate broker's employment contract or "listing agreement". As the listing agreement was in writing and signed by the defendants, the requirements of the Statute of Frauds have been complied with. Assoc. Agency of Bozeman, Inc. v. Pasha, 191 M 407, 625 P2d 38, 38 St. Rep. 344 (1981).

Jury Instruction Correct as to Statute of Frauds — Instruction Held Unnecessary: In an action by the plaintiff real estate brokerage firm to recover a real estate sales commission from the defendant, the trial court did not err in refusing to give the defendant's requested instruction setting forth the law of the Statute of Frauds. The contract at issue is not an oral contract for deed but the written listing agreement signed by the defendant. As there is no dispute over the listing agreement, the instruction was unnecessary and the defendant was not prejudiced by its refusal. Assoc. Agency of Bozeman, Inc. v. Pasha, 191 M 407, 625 P2d 38, 38 St. Rep. 344 (1981).

Real Estate Commission — Setting Chain in Motion Required to Collect Commission: Defendant contended that the requirements of a listing agreement were not sufficiently met by plaintiff to allow the collection of her commission. Plaintiff placed an ad in the newspaper, which named an erroneous price. As a result of that ad, the eventual buyer called plaintiff and obtained the location and identification of the property and the sellers. Plaintiff called defendant and advised her of this development. Defendant then negotiated with the buyer and closed the sale. A broker is entitled to his commission if his efforts set in motion a chain of events which finally culminate in the sale of the property. Here, plaintiff set that chain in motion. Barrett v. Ballard, 191 M 39, 622 P2d 180, 37 St. Rep. 2038 (1980), followed in Lane v. Smith, 255 M 218, 841 P2d 1143, 49 St. Rep. 974 (1992), and in Hall & Hall, Inc. v. Hyde, 264 M 190, 870 P2d 1362, 51 St. Rep. 257 (1994). See also Adams v. Cheney, 203 M 187, 661 P2d 434, 40 St. Rep. 383 (1983).

Modification of Listing Agreement and Failure to Provide Copy: A seller's alleged verbal consent to a broker's unsubscribed and unexecuted modification of a listing agreement was not a factual issue precluding summary judgment in light of the statutory and decisional law which is uniformly suspicious of such modifications. As a matter of law, the broker's failure to provide the seller with a copy of the listing agreement also supported the granting of summary judgment. Carnell v. Watson, 176 M 344, 578 P2d 308 (1978). See also WRB-West Associates, Inc. v. Madison Addition Inv. Ltd. Partnership, 270 M 498, 893 P2d 340, 52 St. Rep. 329 (1995).

Completing Sale Distinguished From Finding Purchaser: In action to recover broker's commissions purportedly due and owing from sale of property owned by defendant, the Supreme Court held that the defendant was not liable because plaintiff broker failed to perform the terms of the exclusive listing agreement by completing the sale. It was insufficient under this agreement

to merely find a purchaser. Diehl & Associates v. Houtchens, 173 M 372, 567 P2d 930 (1977), followed in Blumfield Agency v. Little Belt, Inc., 203 M 515, 663 P2d 1164, 40 St. Rep. 605 (1983). See also Ehly v. Cady, 212 M 82, 687 P2d 687, 41 St. Rep. 1611 (1984).

Proof of Agency: Where issue was whether defendant was realtor and had listed property for sale, summary judgment for plaintiff was proper when defendant could produce no written document establishing such facts. Pack River Co. v. Young, 162 M 271, 511 P2d 12 (1973).

Subsequent Oral Modification: Even if corporate minutes and subsequent listing agreement constituted written agreement to pay director commission on sale of corporation's real and personal property, alleged oral modification to permit sale to different buyer at lesser price was barred by this section; contract was not removed from bar of statute as an executed oral agreement under 28-2-1602. Hart v. Billings Pub. Stockyards, 157 M 345, 486 P2d 120 (1971).

Agreement Between Brokers: Agreements between real estate brokers to divide commissions are not within the Statute of Frauds so that an oral agreement between them is enforceable. Reilly v. Maw, 146 M 145, 405 P2d 440 (1965).

Listing Contract — Burden of Proof: Plaintiff, in an action to recover a broker's commission for procuring a purchaser for real property, has the burden of showing such a contract as would be valid under this section. Reilly v. Maw, 146 M 145, 405 P2d 440 (1965); Newman v. Dunleavy, 51 M 149, 149 P 970 (1915).

Listing Contract: A listing contract empowering realtors to sell apartment building, being limited to question of sale of the building, was not evidence of any alleged oral agreement providing for management of the building by the realtors. Quitmeyer v. Theroux, 144 M 302, 395 P2d 965 (1964). (Dissenting opinion, 144 M 302, 395 P2d 965 (1964).)

When Writings Sufficient: In action for specific performance of contract for purchase of ranch of defendants, writings were sufficient to take the case out of the Statute of Frauds where instrument giving broker exclusive right for 30 days to sell ranch for $30,000, provided that defendants were to pay broker a $1,000 commission, recited that terms of sale were cash to defendants, possession should be taken by purchaser on named date and that defendants, who retained a 5% royalty, agreed to pay 1953 taxes and transfer all lease land to purchaser, who accepted unqualifiedly in writing accompanied by check as down payment. Ward v. Mattuschek, 134 M 307, 330 P2d 971 (1958).

Application of Subsection: Subsection (1)(e) of this section applies when the subject matter of the agency is real estate as distinguished from personal property and where compensation or a commission is claimed regardless of whether the agent has authority to make a conveyance. Featherman v. Kennedy, 122 M 256, 200 P2d 243 (1948).

Performance of Contract by Buyer and Seller: The fact that the contract between the buyer and seller of real estate has been fully performed has nothing to do with the contract between the seller and the agent claiming a commission and cannot have the effect of removing such contract from the operation of the Statute of Frauds. Featherman v. Kennedy, 122 M 256, 200 P2d 243 (1948).

No Recovery on Quantum Meruit: Where contract with agent for sale of real property is not in writing there can be no recovery of a commission either on the contract or on quantum meruit. Featherman v. Kennedy, 122 M 256, 200 P2d 243 (1948); Roscow v. Bara, 114 M 246, 135 P2d 364 (1943).

Modification Must Be in Writing: Under the Statute of Frauds one who seeks to recover a broker's commission upon an agreement authorizing him to procure a purchaser of real property must be able to show a note or memorandum, subscribed by the party to be charged or his agent, and where the original agreement was modified in its terms, the modification must likewise have been in writing and subscribed, the two being considered together as constituting the note or memorandum required by this section. Roscow v. Bara, 114 M 246, 135 P2d 364 (1943); Gantt v. Harper, 82 M 393, 267 P 296 (1928).

Option Contracts — Not an Interest in Land: The holder of an option to purchase land acquires nothing more than a personal privilege to purchase which does not ripen into an interest in the land itself until the privilege is exercised; hence where the optionee assigned his right to another and entered into an agreement with him whereby he (the assignor) was to find a buyer in consideration of half the profits realized on the sale, his engagement was to perform a service which could lawfully be made orally. O'Neill v. Wall, 103 M 388, 62 P2d 672 (1936); Awbery v. Schmidt, 65 M 265, 211 P 346 (1922).

Employment to Procure Lease: A lease of land is not real estate and therefore a contract employing a broker to procure or sell a lease is not within subsection (1)(e) and therefore need not be in writing. O'Neill v. Wall, 103 M 388, 62 P2d 672 (1936).

Consideration for Agreement: The services rendered by a real estate broker in securing a purchaser constitute the consideration for the commission sought to be recovered by him in his action against the seller; the memorandum evidencing his employment does not require a consideration, and a memorandum executed after the services have been performed is sufficient to satisfy the requirement of the Statute of Frauds. Gantt v. Harper, 86 M 69, 281 P 915 (1929).

Note or Memorandum — What Constitutes: While a brokerage contract sufficient to avoid the Statute of Frauds may be established by an interchange of letters between the broker and the owner of real property sold, a letter written by the secretary-manager of defendant corporation as an individual and not in his official capacity to another of its stockholders stating the attitude of certain holders of stock relative to a sale of the company's real property, the terms to be exacted and commission to be allowed in case sale was made to "anyone", was neither the act of the corporation defendant nor such a note or memorandum as is contemplated by the Statute of Frauds, and therefore plaintiff broker was properly nonsuited in his action to recover commissions for the sale of the property. Skinner v. Red Lodge Brewing Co., 79 M 292, 256 P 173 (1927).

Writing Mandatory: Under this section, which is mandatory, a brokerage contract for the sale of real property as well as any modification in terms must be in writing and subscribed by the party to be charged or his authorized agent, to permit a broker to recover compensation or a commission on sale of the property by the owner. Skinner v. Red Lodge Brewing Co., 79 M 292, 256 P 173 (1927); Hartt v. Jahn, 59 M 173, 196 P 153 (1921).

Testimony Inadmissible: A contract to sell real estate belonging to another for a compensation must under this section be in writing, otherwise it is void. Where such a contract is in parol, testimony in support of a cause of action based upon it is inadmissible. Dick v. King, 73 M 456, 236 P 1093 (1925).

Optionholder — What Constitutes Employment of Broker: Since the person to whom an option to buy land is granted acquires no interest in the property itself until he exercises the privilege granted, a contract between the plaintiff and defendant under which the former was to secure the assignment of an option from the holder thereof to defendant did not amount to an employment of plaintiff as a broker or agent to buy land or an interest in land which, under this section, is required to be in writing, but was one to perform a service which could lawfully be made by parol. Kramer v. Schmidt, 62 M 568, 206 P 620 (1922).

Executed Contracts: Under subsection (1)(e) of this section, an agreement authorizing or employing an agent or broker to sell real estate on commission must be in writing, as must also a subsequent modification of its terms, so long as the contract or modification is executory in character, the rule, however, not applying where the contract has been executed. Cobb v. Warren, 64 M 10, 208 P 928 (1922).

Recovery Barred: Where it did not appear that a broker's contract of employment to sell real estate was in writing, or that any note or memorandum thereof, signed by the party to be charged, had been executed as required by this section, no recovery could be had for services rendered thereon. Marshall v. Trerise, 33 M 28, 81 P 400 (1905); King v. Benson, 22 M 256, 56 P 280 (1899).

ADMISSIBILITY OF EVIDENCE

Allowance of Parol Evidence Rendered Harmless Through Other Evidence: Although a District Court allowed parol evidence to determine the meaning of a "perpetual first option to purchase" in a memorandum of understanding, other evidence in the memorandum was sufficient to reach the same conclusion. Kluver v. PPL Montana, LLC, 2012 MT 321, 368 Mont. 101, 293 P.3d 817.

Failure to Plead: A defendant's failure to mention the Statute of Frauds in the pleadings precludes its consideration. Peretti v. St. Bd. of Educ., 464 F. Supp. 784 (D.C. Mont. 1979).

Memorandum Not Naming Parties: While the Statute of Frauds does not require that the memorandum be contained in a single document, where a memorandum did not name the parties to the alleged contract but referred to them as "we" and "our" and also tended to show that further negotiations were intended by the parties, it was not sufficient to satisfy the Statute. Anderson v. KFBB Broadcasting Corp., 143 M 423, 391 P2d 2 (1964), distinguished in Daley v. Daley, 150 M 432, 436 P2d 88 (1968).

Note May Be Several Writings: The note or memorandum necessary to meet the requirements of this section may consist of several writings, and it is sufficient if it contains all the essentials of the contract, although they are stated in general terms. Hughes v. Melby, 135 M 415, 340 P2d 511 (1958).

What Constitutes Note: An endorsed bank check with the additional words "Payment land" written on it is insufficient to constitute the written "note or memorandum" required by the statutes for it does not contain all the essentials of the agreement. Lewis v. Peterson, 127 M 474, 267 P2d 127 (1954).

Elements of Contract Required: The memorandum must contain all the essentials of the contract but if the material elements are stated in general terms, not all the details or particulars need be stated. Johnson v. Elliot, 123 M 597, 218 P2d 703 (1950).

Pleading: Although a contract to be valid must be in writing, that fact is a matter of proof and need not be alleged in the pleading. Johnson v. Elliot, 123 M 597, 218 P2d 703 (1950).

Presumption of Writing: The law will presume that a contract was in writing in the absence of any statement to the contrary. Johnson v. Elliot, 123 M 597, 218 P2d 703 (1950).

Note or Memorandum — Lack of Elements: Where complaint shows on its face that memorandum of agreement does not contain all essentials of agreement and such essentials cannot be ascertained without resort to oral evidence, demurrer to complaint was properly sustained. Dineen v. Sullivan, 123 M 195, 213 P2d 241 (1950).

Parol Evidence on Memorandum: Parol evidence is admissible to explain ambiguities in note or memorandum relied upon as taking contract out of Statute of Frauds, and to apply the note or memorandum to the subject matter. Johnson v. Ogle, 120 M 176, 181 P2d 789 (1947).

Contract as Evidence to Support Other Pleas: Though an oral contract be invalid under the Statute of Frauds and in an action thereon evidence seeking to establish it is incompetent, it may be received as evidence in support of a plea such as ratification. Arnold v. Genzberger, 96 M 358, 31 P2d 296 (1934).

When Objection Is Waived:

The objection that a contract in suit is invalid under the Statute of Frauds is waived where the point that the contract, to be enforceable must be in writing, was not raised either in the pleadings or by objection to the introduction of evidence. Alley v. Peeso, 88 M 1, 290 P 238 (1930).

Though a contract may have been executed in contravention of this section, it will not be declared void where the statute is not pleaded. Mitchell v. Henderson, 37 M 515, 97 P 942 (1908).

Void Contract Not Admissible: Unless a contract void under the Statute of Frauds because not in writing is removed from the operation of the Statute by an exception, it is not only unenforceable but evidence of it may not be received. McIntyre v. Dawes, 71 M 367, 229 P 846 (1924).

Burden of Proof: The rule is well settled that though a contract to be valid under the statute must be evidenced by a writing and subscribed by the party to be charged or his agent, the fact that it is in writing is a matter of proof and not of allegation in pleading. Blankenship v. Decker, 34 M 292, 85 P 1035 (1906); Hefferlin v. Karlman, 29 M 139, 74 P 201 (1903); Mayger v. Cruse, 5 M 485, 6 P 333 (1885); Sweetland v. Barrett, 4 M 217, 1 P 745 (1882).

Preponderance of Evidence Required: Where the value of property involved in a sale is sufficient to bring the contract of sale within the provisions of section 74-201, R.C.M. 1947 (since repealed), the burden is on plaintiff, in an action for breach of the contract, to establish by a preponderance of evidence that a valid contract under the statutes was entered into between the parties, together with a breach of such contract, and the consequent damages. Brophy v. Idaho Produce & Provision Co., 31 M 279, 78 P 493 (1904).

Law Review Articles

Real Estate Contracts to Sell, Written Agency Agreement Given by Landowner to Realtor Constitutes a Sufficient Memorandum of Contract to Satisfy the Statute of Frauds, 20 Mont. L. Rev. 240 (1958).

28-2-904. Effect of written contract on oral agreements.

Case Notes

Parol Evidence 252
Oral Negotiations Superseded 256
Contracts Required to Be in Writing 258
Miscellaneous 259

PAROL EVIDENCE

Statute of Frauds and Parol Evidence Rule Not Bar to Alleged Oral Contract — Genuine Issue of Material Fact Regarding Intent — Written Agreement Did Not Clearly Evidence Final Expression — Uniform Commercial Code Applied: The District Court did not err in denying the defendant's motion for summary judgment based on the defendant's assertion that an alleged oral contract was barred by the statute of frauds or the parol evidence rule. The agreement between the parties involved the sale of brake linings from the defendant to the plaintiff and the sale of remanufactured brakes from the plaintiff to another party. The brake linings and remanufactured brakes constituted moveable goods under 30-2-105, making the alleged oral contract within the ambit of the Montana Uniform Commercial Code's statute of frauds provision in 30-2-201. Because the parties entered into a written agreement and one party asserted the existence of an additional oral contract, the parol evidence rule provided for in 30-2-202 was applied. After the District Court made an initial determination under 30-2-202 that the program agreement did not clearly evidence a final expression of the parties' agreement, it properly denied summary judgment and allowed the jury to consider evidence to elucidate the true nature of the parties' agreement. S & P Brake Supply, Inc. v. STEMCO LP, 2016 MT 324, 385 Mont. 488, 385 P.3d 567, following Norwest Bank Billings v. Murnion, 210 Mont. 417, 684 P.2d 1067 (1984).

Claims of Oral Misrepresentations Precluded by Terms of Written Contract — Applicability of Parol Evidence Rule: An agreement for the sale of a trailer park contained multiple written terms, including plaintiff's agreement that he had not relied on any assurances as to the condition of the property. In a subsequent disagreement over the condition of the trailer park water system, plaintiff sought to introduce evidence of oral statements made by the seller that the water system was in good or fine condition and that plaintiff had relied on the statements to his detriment. The District Court properly applied the parol evidence rule to exclude the evidence. Plaintiff could not claim that, pursuant to the written contract, he had not relied on any assurances and then claim that he was misled by oral statements contradictory to the contract. Deschamps v. Treasure St. Trailer Ct., Ltd., 2010 MT 74, 356 Mont. 1, 230 P.3d 800, distinguishing Jenkins v. Hillard, 199 Mont. 1, 647 P.2d 354.

Failure to Bring Fraud Action Within Time Claim Accrues — Statute of Limitations Precluding Fraud Action: Plaintiff discovered or reasonably should have discovered within 6 months of purchasing a trailer park in May 2003 that a fraud may have been perpetrated regarding the profitability of the park and the condition of the park water system, but plaintiff did not bring a fraud or misrepresentation claim until 2007. The actual and constructive fraud claims were therefore precluded by the statute of limitations in 27-2-203, which requires an action for fraud to be commenced within 2 years. Plaintiff's claims were properly dismissed as untimely. Deschamps v. Treasure St. Trailer Ct., Ltd., 2010 MT 74, 356 Mont. 1, 230 P.3d 800.

No Ambiguity in Complete, Final Sales Agreement — Parol Evidence Inadmissible: The parties entered a sale agreement for a ready-mix concrete plant. Plaintiff subsequently filed an action alleging that defendant violated the agreement by breaching the covenant to not compete and the covenant of good faith and fair dealing, which constituted malice resulting in lost profits, sales, and goodwill. The District Court granted summary judgment to defendant and plaintiff appealed, but the Supreme Court affirmed. The District Court correctly concluded that the sales agreement constituted a complete, final agreement and unambiguously did not include a noncompetition provision, but in fact provided that plaintiff would sell concrete to defendant for use in the area. The intention of the parties was ascertainable from the writing alone, and the agreement was presumed to represent all transactions regarding elements extrinsic to the agreement and was thus considered complete and final, so parol evidence was inadmissible. Richards v. JTL Group, Inc., 2009 MT 173, 350 M 516, 212 P3d 264 (2009). See also Lindey's, Inc. v. Professional Consultants, Inc., 244 M 238, 797 P2d 920 (1990), and Mary J. Baker Revocable Trust v. Cenex Harvest States, Cooperatives, Inc., 2007 MT 159, 338 M 41, 164 P3d 851 (2007).

Refusal to Enforce Unsubstantiated Oral Agreement to Dismiss Claim for Prescriptive Easement — Parol Evidence Rule and Statute of Frauds Inapplicable: Defendant contended that the District Court erred in failing to estop plaintiff from asserting claims for a prescriptive easement across defendant's property because an agent of plaintiff orally agreed to dismiss the claims and defendant relied on the promise to defendant's detriment. The District Court held that the parol evidence rule and the statute of frauds prohibited admission of evidence of an oral agreement to dismiss the case because there were written temporary access agreements in place and that defendant did not offer sufficient evidence to meet either a fraud or estoppel exception to the parol evidence rule. The Supreme Court found that the trial court reached the correct result, albeit for the wrongs reasons, by automatically applying the parol evidence rule and the statute of frauds without determining whether either rule applied. Actually neither rule barred admission of the evidence in this case, so the trial court was free to consider the merits of the existence of an oral contract without defendant having to prove the elements of fraud or detrimental reliance. Nevertheless, the trial court found defendant's story of an oral agreement to be unsubstantiated and correctly refused to enforce an oral agreement based on the facts before it. Brimstone Min., Inc. v. Glaus, 2003 MT 236, 317 M 236, 77 P3d 175 (2003).

Application of Parol Evidence Rule to Stranger to Contract — Stranger to Contract Exception Clarified: Habets bought a 7-mile stretch of buried pipeline from Cenex and, upon attempting to recover the pipeline from the ground pursuant to the contract of sale, was refused access to part of the pipeline by the Swansons, who claimed that they had previously purchased a section of the same pipeline from Cenex. Habets brought an action against the Swansons for access to the pipeline, and the Swansons sought to introduce extrinsic parol evidence to show that under their contract with Cenex, which did not show the purchase of the segment of the pipeline in question, they had in fact purchased the segment of the pipeline in question. The District Court excluded the extrinsic parol evidence because of the parol evidence rule, and the Supreme Court affirmed the exclusion of that evidence. The Supreme Court examined the "stranger exception" to the parol evidence rule, which seemed to indicate that extrinsic parol evidence could be introduced by a person not a party to the contract to vary the terms of the contract. The Supreme Court distinguished its previous opinions in Read v. Lewis & Clark County, 55 M 412, 178 P 177 (1919), Greening v. Gazette Printing Co., 108 M 158, 88 P2d 862 (1939), and Fillinger v. NW. Agency, Inc., of Great Falls, 283 M 71, 938 P2d 1347 (1997), raised by the Swansons in support of that exception. The Supreme Court held that the parol evidence rule applies to exclude evidence extrinsic to an unambiguous contract in any situation involving either parties or strangers to the contract when rights and duties created by the contract are the dispositive issue. Habets v. Swanson, 2000 MT 367, 303 M 410, 16 P3d 1035, 57 St. Rep. 1567 (2000).

Rights Under Written Contract Not Obliterated by Implied Obligation — Nonrenewal of Term Contract: Farris was hired under a term contract that lasted 1 year. The contract provided for nonrenewal with adequate notice. After signing term contracts for 3 consecutive years, Farris was notified that employment would be discontinued. Farris sought to invoke the implied covenant of good faith and fair dealing, contending that the employer's oral negotiations implied permanent employment and objective manifestations of job security. However, consideration of the oral negotiations was barred by the parol evidence rule of this section, under which oral stipulations are superseded by a written contract. Consideration of representations of permanent employment made after the contract was signed was barred by 28-2-1602, which allows only written or executed oral agreement to affect the validity of a written contract. The Supreme Court cited Carma Developers v. Marathon Dev. Calif., Inc., 826 P2d 710 (Calif. 1992), for the proposition that no obligation can be implied that would result in the obliteration of a right expressly given under a written contract. In interpreting a contract, an implication should not be made when the contrary is indicated in clear and express words. Farris v. Hutchinson, 254 M 334, 838 P2d 374, 49 St. Rep. 717 (1992), distinguishing at-will dismissal under a written contract in Stark v. Circle K Corp., 230 M 468, 751 P2d 162 (1988), and Prout v. Sears, Roebuck & Co., 236 M 152, 772 P2d 288 (1989), and followed in Talley v. Flathead Valley Community College, 259 M 479, 857 P2d 701, 50 St. Rep. 889 (1993).

Summary Judgment Proper: Plaintiff, a subcontractor, submitted a bid for excavation, relying on a statement by defendants' representative that there were 25,000 cubic yards of excavation to be performed. The bid was accepted, and work was begun before a final contract was signed using the figure of 25,000 cubic yards. The actual excavation turned out to be about 50,000 cubic yards. Defendants were granted summary judgment, and the Supreme Court affirmed. Under the parol evidence rule, plaintiff could not introduce evidence of the alleged oral misrepresentations. Sherrodd, Inc. v. Morrison-Knudsen Co., 249 M 282, 815 P2d 1135, 48 St. Rep. 671 (1991), followed in Savik v. Entech, Inc., 278 M 152, 923 P2d 1091, 53 St. Rep. 894 (1996), and Richards v. JTL Group, Inc., 2009 MT 173, 350 M 516, 212 P3d 264 (2009).

Test for Determining Whether Parol Testimony Varies Writing: In determining whether or not the terms of a written instrument are varied by parol testimony, the most satisfactory test is found in the circumstance whether or not the particular element of the alleged extrinsic negotiation is dealt with at all in the writing; if it is mentioned, covered, or dealt with in the writing, then presumably the writing was meant to represent all of the transactions on that element. Lindey's, Inc. v. Professional Consultants, Inc., 244 M 238, 797 P2d 920, 47 St. Rep. 1570 (1990); Cont. Oil Co. v. Bell, 94 M 123, 21 P2d 65 (1933); Hosch v. Howe, 92 M 405, 16 P2d 699 (1932).

Water Well Use Agreement Not Subject to Modification by Parol Evidence: The parties entered into an agreement regulating the use of water from a well owned by the plaintiffs. In their counterclaim, the defendants alleged that the reason the agreement provided that the plaintiffs did not have to extend use of the water to any subsequent purchaser of the defendants' property was in order to assure plaintiffs some say regarding the kind of people who bought the defendants' property. The defendants asserted that the plaintiffs had assured them orally that they would not unreasonably withhold use of the well from subsequent buyers of the defendants' property. The Supreme Court overruled the lower court and held that the agreement was clear on its face and that the parol evidence rule excluded any extrinsic evidence concerning the water use agreement. The defendants were unable to show a breach of the terms of the agreement, and therefore there could be no finding of a violation of the covenant of good faith and fair dealing. Baker v. Bailey, 240 M 139, 782 P2d 1286, 46 St. Rep. 2005 (1989).

Unambiguous Contract Description — Applicability of Parol Evidence Rule — Unilateral Mistake: Since a 1971 written agreement was not ambiguous with respect to the land it affected, the parol evidence rule prevented admission of evidence of a 1967 oral agreement to show intent of the parties as to what land was involved. Admission of the oral agreement would only have provided evidence of unilateral mistake, which is not grounds for reforming a written contract. Haggerty v. Gallatin County, 221 M 109, 717 P2d 550, 43 St. Rep. 674 (1986), followed in Carelli v. Hall, 279 M 202, 926 P2d 756, 53 St. Rep. 1116 (1996). Carelli was followed in Habets v. Swanson, 2000 MT 367, 303 M 410, 16 P3d 1035, 57 St. Rep. 1567 (2000).

Prior Discussion Did Not Vary Terms of Written Contract: The discussion between the employer and employee concerning the employee's other job, which took place before a written employment contract was entered into, was not considered to have varied the terms of the contract. There was nothing in the written contract to suggest an intent to incorporate the prior discussion. Therefore, the jury was free to conclude that the conversation did not vary the contract. Wilkerson v. School District, 216 M 203, 700 P2d 617, 42 St. Rep. 745 (1985).

Parol Evidence Rules Substantive, Not Procedural — Subject to Rules of Evidence and Common-Law Exceptions: The Montana Uniform Commercial Code's parol evidence rule contained in 30-2-202 continues the operation of the traditional law of contracts parol evidence rule, though with some modifications. Each is a principle of substantive law, not a procedural rule of evidence. Thus, the admissibility of any evidence is ultimately subject to the provisions of the Montana Rules of Evidence, and the traditional common-law exceptions to the contract law parol evidence rule, such as proof of fraud, misrepresentation, or mistake, remain exceptions to the parol evidence rule in the Montana Uniform Commercial Code. Norwest Bank Billings v. Murnion, 210 M 417, 684 P2d 1067, 41 St. Rep. 1132 (1984). See also Webcor Electronics, Inc. v. Home Electronics, Inc., 231 M 377, 754 P2d 491, 45 St. Rep. 695 (1988).

Sale of Front-End Loader — Applicable Parol Evidence Rule: Front-end loader that buyer purchased from seller was within the definition of "goods" set out in 30-2-105. Therefore, the sale was governed by the Montana Uniform Commercial Code, and any Code provisions addressing a parol evidence question controlled the answer to the question, with the contract law parol evidence rule of 28-2-904 being used only to supplement the Code. Norwest Bank Billings v. Murnion, 210 M 417, 684 P2d 1067, 41 St. Rep. 1132 (1984).

Contract Part Oral, Part Written — Bid Not Contract — Parol Evidence Rule Inapplicable — Time of Essence by Oral Agreement: The plaintiff in a breach of contract case obtained a bid on a job building a basement. The defendant contractors on appeal argued: (1) that their bid constituted a contract and therefore the parol evidence rule barred testimony concerning a completion date not contained in the writing; and (2) time was not of the essence unless expressly provided in the writing. The Supreme Court said that the bid was an offer and that a purported acceptance which varied or added to the terms of the offer was not an acceptance but a counteroffer. The trial court's finding that the parties had agreed orally to a specific completion date was not clearly erroneous. The contract was partially written and partially oral. Because there was not a final, complete written document intended by the parties to contain all of the terms of the contract, the parol evidence rule did not apply. By agreeing to the completion date with the knowledge that the plaintiff considered the date essential because of approaching cold weather, the defendants agreed that time was of the essence. Therefore, the defendants were in substantial breach on the agreed date. Carriger v. Ballenger, 192 M 479, 628 P2d 1106, 38 St. Rep. 864 (1981), distinguishing Higby v. Hooper, 124 M 331, 221 P2d 1043 (1950).

Parol Evidence Rule Precluding Testimony on Destroyed Copy With Notation: Buechler entered into a contract with Payne, granting him the right to sell Buechler's property. Payne's copy of the contract stated that the listing was exclusive. Buechler offered parol evidence that Payne had written "nonexclusive" on her copy of the contract. Her copy was destroyed and therefore was not entered into evidence. The Supreme Court held that the parol evidence directly contradicts the plain and unambiguous language of the written instrument; it does not fall within any recognized exception permitting its admission in evidence and is clearly inadmissible. Payne v. Buechler, 192 M 311, 628 P2d 646, 38 St. Rep. 799 (1981).

Businessman Neglecting to Read Contract — Oral Testimony Not Admissible: A real estate developer who failed to exercise the care and prudence of a reasonable and cautious businessman by neglecting or failing to read contracts for deeds that he signed may not rely upon 28-2-905, concerning admissibility of extrinsic evidence about a mistake in the instrument, to allow oral testimony to be admissible because this section is given the greater weight when the proffered evidence, as here, is insufficient to establish mistake. Silva v. McGuinness, 189 M 252, 615 P2d 879, 37 St. Rep. 1401 (1980).

Parol Evidence Rule: Where the correspondence of the parties which constituted the written memoranda for an agreement for the sale of a truck crane did not provide that the time of delivery of the crane was of the essence in the contract, it was error to admit parol evidence regarding that term. Martel Constr., Inc. v. Gleason Equip., Inc., 166 M 479, 534 P2d 883 (1975).

Parol Inadmissible Where Terms Unambiguous: Contract between husband and wife for payment of $10,000 in purchase of partnership interest, which stated that the parties released each other from any further liability, was not ambiguous and could not be varied by parol evidence. Merritt v. Merritt, 165 M 172, 526 P2d 1375 (1974).

Change in Legal Effect: Where the consideration expressed in the written instrument is contractual in its nature, oral evidence is inadmissible to show a different consideration because then it changes the legal effect of the instrument. Warner v. Johns, 122 M 283, 201 P2d 986 (1949), followed, with regard to contractual interpretation, in Trustees of the Wash.-Idaho-Mont. Carpenters-Employers Retirement Trust Fund v. Galleria Partnership, 239 M 250, 780 P2d 608, 46 St. Rep. 1661 (1989).

Ambiguous Terms: In an action to recover the purchase price of merchandise (sewing machines) claimed to have been sold to defendants but alleged by them to have been delivered on consignment, plaintiff introduced in evidence a printed order for the goods obtained by its agent, which under the subject "Terms" contained the words "Finance Plan". Defendants, contending that the contract did not contain all the terms agreed upon and that the words "Finance Plan" rendered the contract ambiguous, were permitted to introduce parol evidence to explain the term. The evidence was properly admitted, in that the meaning of the term is not so free from doubt that it may be said, as a matter of law, that it furnishes its own interpretation. New Home Sewing Mach. Co. v. Songer, 91 M 127, 7 P2d 238 (1931).

Object of Parties: The parol testimony rule does not forbid an inquiry into the object of the parties in executing and receiving the instrument sued upon; while its language cannot be qualified or varied from its natural import, the circumstances under which it was entered into and the real intention of the parties may be shown by parol to prevent either of the parties to it from committing a fraud on the other by claiming it to be what it in fact is not. Bridges & Co., Inc. v. Bank of Fergus County, 77 M 524, 251 P 1057 (1926).

Representations of Agent: In an action for damages for breach of a clause of a written contract of sale of a threshing machine warranting it as being as well made of good material and that with proper use and management it would do as good work as any other machine of the same size manufactured for the like purpose, evidence of statements made by defendant's agent in making the sale that it would thresh and clean alfalfa as well as any other machine of the same size, etc., was properly rejected as an attempt to vary the terms of the written instrument by parol. Rowe v. Emerson-Brantingham Implement Co., 61 M 73, 201 P 316 (1921).

Interpretation of Instrument: Where an agreement to furnish automobiles to be sold on commission did not furnish its own interpretation, parol evidence was properly admitted to determine the intention of the parties. Brockway v. Blair, 53 M 531, 165 P 455 (1917).

Error to Admit Parol to Vary Written Terms: Admission of parol evidence to vary and contradict the terms of a written contract is error. Pritchett v. Jenkins, 52 M 81, 155 P 974 (1916).

No Conflict of Evidence: A conversation between buyer and seller had prior to the execution of a bill of sale, with the terms of which it was not in conflict and which was material to show the circumstances under which the writing was executed, was admissible in evidence and not open to the objection that it varied the written agreement. Sutherland v. Green, 49 M 379, 142 P 636 (1914).

ORAL NEGOTIATIONS SUPERSEDED

Sale of Property Contingent on Financing — Financing Contingent on Grant of Contract — Oral Agreement to Purchase Additional Property Contingent on Initial Sale — Summary Judgment Proper Absent Genuine Issue of Fact: Community, Counseling, and Correctional Services, Inc. (Community), agreed to purchase Albright's property for a prerelease center. An additional oral agreement provided that Community would also purchase furnishings on the property when the sale was completed. The sale was contingent on Community's ability to obtain financing, and financing was contingent upon a grant for the prerelease center to Community from the Department of Corrections. Ultimately, the Department declined to issue the contract for prerelease services, Community was unable to obtain financing, and Albright was unable to sell the property or furnishings. Albright sued Community for breach of contract. The District

Court granted summary judgment to Community, holding that under the plain language of the contract, the offer terminated when the Department did not issue the contract. Albright appealed, but the Supreme Court affirmed. No question of fact existed with respect to the conditions for the agreement because the agreement conditioned formation of any contract to buy the real property on Community's ability to obtain financing and Community could not obtain financing without the Department contract. Further, Albright's own affidavit stated that the oral agreement to purchase the furnishings was contingent on purchase of the property, so no issue of fact existed regarding the sale of the furnishings either, and that issue was also properly disposed of by summary judgment. Albright v. Community, Counseling, & Correctional Serv., Inc., 2001 MT 272, 307 M 289, 37 P3d 675 (2001).

Negative Easement Based on Oral Agreement — Statute of Frauds Inapplicable: Appellants claimed an oral agreement made in 1967 subjected land known as the Base Area Chalet to a negative easement that restricted the property to noncommercial activities. The Supreme Court found that a written 1971 agreement only contracted to convey property described as "sellers' land" which had been "subject to ski easement"; however, the chalet property was conveyed away by appellants in 1967 and had never been subject to the ski easement. Since the Base Area Chalet did not belong to "sellers" and was not subject to the easement in 1971, the 1971 agreement had no effect on the chalet property. For the same reason, the 1971 agreement could not satisfy the Statute of Frauds for any alleged oral agreement that would create a negative easement on the chalet property. Haggerty v. Gallatin County, 221 M 109, 717 P2d 550, 43 St. Rep. 674 (1986).

Consolidation and Extension of Agreement Between Lender and Borrowers: Defendants argued that a consolidation and extension agreement with the plaintiff bank lacked consideration. They contended that certain oral negotiations previously entered into by the parties had been fully performed by defendants, thus depriving the subsequent written agreement of any new consideration. The Supreme Court agreed with the District Court's conclusion that the execution of the written agreement in effect superseded and controlled all of the earlier oral agreements. First Nat'l Bank of Missoula v. McGuinness, 217 M 409, 705 P2d 579, 42 St. Rep. 1288 (1985). See also Shiplet v. First Sec. Bank of Livingston, Inc., 234 M 166, 762 P2d 242, 45 St. Rep. 1816 (1988), and Lachenmaier v. First Bank Sys., Inc., 246 M 26, 803 P2d 614, 47 St. Rep. 2244 (1990).

Final Written Agreement as Precluding Oral Warranty: Plaintiffs and defendant entered an agreement whereby defendant would lease condominiums from the plaintiffs and would sell plaintiffs her home. The lease of one of the condominiums contained an option for defendant to purchase the unit by forgiving plaintiffs their obligation under the promissory note on the home. Plaintiffs discovered that the floors in the home sloped north at a rate of 5½ inches over 30 feet. Plaintiffs sought to rescind the contract, and defendant sought specific performance. Plaintiff contended that defendant stated that there were no problems whatsoever with the house and that this statement created an express warranty. Defendant denied making the statement. The contract between the parties contained a clause which stated that the written agreement constituted the entire agreement and superseded and waived all oral representations, so no express warranty existed. Woodahl v. Matthews, 196 M 445, 639 P2d 1165, 39 St. Rep. 238 (1982).

Effect of Oral Agreement on Written Agreement — Contract for Deed: In this case concerning a contract for deed, one issue on appeal was the effect of an oral agreement on written instruments that followed. The Supreme Court held that it was clear that the written instruments superseded the oral agreement. Stoddard v. Grokin, 191 M 495, 625 P2d 529, 38 St. Rep. 326 (1981).

Issue of Fact as to Whether a Written Agreement Supersedes an Oral Agreement: Plaintiff's motion for summary judgment was properly denied where there was some question of fact as to whether one written agreement signed by plaintiff as agent for his company, by the company vice-president, and by defendant entitling defendant to a salary advance supersedes a prior oral agreement allegedly made between plaintiff and defendant in which plaintiff personally guaranteed a salary to defendant. Reviewing the relationship of the two agreements in the light most favorable to the defendant, the alleged oral agreement is collateral to the written contract, is distinct, involves a different party, and is able to stand independent of the other. Reaves v. Reinbold, 189 M 284, 615 P2d 896, 37 St. Rep. 1500 (1980).

Written Agreement Presumed to Encompass Prior Oral Agreements: A written agreement must be considered as containing all prior oral ones concerning its subject matter, and its terms may therefore not be varied by oral testimony. Biering v. Ringling, 78 M 145, 252 P 872 (1927); Peterson v. Nelson, 77 M 539, 252 P 368 (1926); Swan v. LeClair, 77 M 422, 251 P 155 (1926); Wheeler v. James, 70 M 37, 223 P 900 (1924); Morehouse v. N. Land Co., 68 M 96, 216 P 792

(1923); Webber v. Killorn, 66 M 130, 212 P 852 (1923); Leigland v. Rundle Land & Abstract Co., 64 M 154, 208 P 1075 (1922); Helena Light & Ry. v. N. Pac. Ry., 57 M 93, 186 P 702 (1920).

Resting and Feeding of Livestock: Prior oral negotiations and directions as to points at which livestock should be stopped for resting and feeding were merged in the contract of shipment, where it and the waybills bore notations stating the points at which stops were to be made, and therefore parol testimony of directions to make other stops was incompetent as an attempt to vary the terms of the written contract. Cook v. N. Pac. Ry., 61 M 573, 203 P 512 (1921).

Written Control Supersedes: A written contract supersedes any oral negotiations theretofore had relative to the subject matter of it and must be considered as containing all of its terms agreed upon at the time it was executed. Arnold v. Fraser, 43 M 540, 117 P 1064 (1911).

Application of Section: This section applies to oral negotiations or stipulations concerning the matter of the agreement; if one of the parties was induced to sign the writing by reason of the other's fraud or deceit with respect to some collateral matter, then he might be heard to complain. Kelly v. Ellis, 39 M 597, 104 P 873 (1909).

Oral Negotiations and Stipulations: A contract in writing supersedes all the prior or contemporaneous oral negotiations and stipulations relating to the subject matter of the agreement between the contracting parties. Therefore a party to it will not be heard to complain that there were other stipulations, unless they pertain to some collateral matter which operated as an inducement to his entering into the principal agreement. Kelly v. Ellis, 39 M 597, 104 P 873 (1909).

Evidence of Conversations Incompetent: Evidence of negotiations and conversations immediately preceding the execution of a written contract is incompetent to show an agreement concerning its matter made by one claimed to be bound thereby. Largey v. Leggat, 30 M 148, 75 P 950 (1904).

Oral Promises: Evidence of oral promises or agreements made prior to or contemporaneously with the execution of a written contract purporting to embrace all its terms, which contradict, change, add to, or subtract from the express terms, is inadmissible. Riddell v. Peck-Williamson Heating & Ventilating Co., 27 M 44, 69 P 241 (1902). See State ex rel. W. Accident & Indem. Co. v. District Court, 55 M 330, 176 P 613 (1918).

CONTRACTS REQUIRED TO BE IN WRITING

Goodwill as Intangible Asset of Business: A contract for sale of a radio station that transferred "all fixed and other assets tangible and intangible" was presumed to include goodwill though goodwill was not specifically mentioned in the contract. Goodwill is considered an intangible asset of a business. W. Media, Inc. v. Merrick, 224 M 28, 727 P2d 547, 43 St. Rep. 1991 (1986), citing Baldwin v. Stuber, 182 M 501, 597 P2d 1135 (1979).

Variation of Terms of Written Contract Held Improper — Evidentiary Rule as Procedural Rule Only: In an action to collect the amount due under a promissory note, the District Court erred in allowing the plaintiff to prove that the terms of a written contract concerning only the terms of sale of a bar also applied to a previous sale of another business. Rule 106, Montana Rules of Evidence, relied on by the District Court to vary the clear terms of the parties' written agreement, is a procedural rule concerning the introduction of only a portion of a whole agreement and cannot be used to affect the substance of the existing law of parol evidence. Spraggins v. Elvidge, 192 M 8, 625 P2d 1151, 38 St. Rep. 493 (1981).

Sale of a Business — Automatic Passing of Goodwill: Seller operated a barber shop in leased premises. He agreed to sell the shop to the defendant. The selling agreement referred to the permanent fixtures and furniture, the shop name, and the phone number. The agreement did not mention goodwill. A dispute arose when the buyer refused to pay the seller. In response the seller removed all his fixtures, disconnected the phone, and brought suit. The court held that even though the buyer received none of the items referred to in the contract, he received goodwill and was therefore liable for the reasonable value of the goodwill. The rule is that if goodwill is not expressly reserved or excepted, it passes automatically to the purchaser of a business. Baldwin v. Stuber, 182 M 501, 597 P2d 1135 (1979).

Lease of State Lands: The Statute of Frauds barred testimony of an alleged oral agreement to sell or assign a state lease when written lease agreements provided specifically for a sublease. Montana law is clear that evidence of oral representations, relating directly to the subject matter of a contract, are not admissible to add to or alter the provisions of a written contract. Furthermore, the alleged oral agreement involved an agreement to transfer an interest in real property and thus is required to be in writing. Aye v. Fix, 176 M 474, 580 P2d 97 (1978).

Completeness of Instrument: Where the evidence showed that a written buy-sell agreement contained all the oral agreements of the parties, that the seller's agent prepared the agreement, and that it was certain in all essential matters, the agreement was specifically enforceable. Maxted v. Stenberg, 166 M 460, 534 P2d 864 (1975).

Two or More Instruments: If a release or quitclaim deed containing a statement of consideration as $1 and other considerations was the only instrument involved, oral testimony could be admissible to explain the "other considerations", but where the quitclaim deed was signed the same time as a property settlement agreement and the two instruments were part of the same transaction, oral evidence was inadmissible to show a different consideration. Warner v. Johns, 122 M 283, 201 P2d 986 (1949).

Fraud: Where plaintiff alleged mistake and fraud and the evidence disclosed that the inducement held out to plaintiff to sign an agreement was based on fraudulent representations of defendants that a lease need not be mentioned in a contract of sale of a business and the lease, the evidence was admissible to show the purchase of the lease and defendants' fraudulent conduct, over objection that it varied the contract. Sathre v. Rolfe, 31 M 85, 77 P 431 (1904).

Contemporaneous Agreement: Evidence of a contemporaneous agreement between the parties to a written sublease of a lode mining claim, that in case the sublessors should buy the property the lease would be extended, is inadmissible. Armington v. Stelle, 27 M 13, 69 P 115 (1902). See Kelly v. Ellis, 39 M 597, 104 P 873 (1909).

MISCELLANEOUS

Sufficient Evidence of Written Fixed Price Contract and Subsequent Binding Oral Agreements for Additional Construction Work: Defendant contracted in writing to perform concrete work at plaintiff's construction project, and the parties also orally agreed that additional concrete work would be done. A dispute arose concerning the existence of the contracts, the amount owed to defendant, and whether plaintiff had waived deficiencies in the work. The Supreme Court affirmed the existence of a written fixed price contract for the initial work and subsequent binding oral agreements for additional work. Defendant's completion of the work entitled him to the full amount called for in the written contract less an amount granted to plaintiff for repair of deficiencies in the work. As for the oral agreements, defendant's billing was the correct amount due for the additional services provided. The trial court also correctly apportioned the amount due to plaintiff for correcting deficiencies in the work, given that plaintiff waived or caused many of the deficiencies by accepting the work, making improper additions to the work, and issuing hasty and ill-conceived commands. Weimar v. Lyons, 2007 MT 182, 338 M 242, 164 P3d 922 (2007).

Court Finds Series of Executed Contracts — Not Subsequent Modifications: The Supreme Court, in dicta, held that a series of agreements, both oral and written, entered into by the parties were separate, fully performed contracts and not subsequent modifications of the original agreement. C. Haydon Ltd. v. Mont. Min. Properties, Inc., 286 M 138, 951 P2d 46, 54 St. Rep. 1341 (1997).

Agreement to Modify: In cattle-raising venture oral agreement between partnership and defendant that subsequent written contract would be modified when experience showed that each would profit by the change did not alter the terms of the written agreement under the rule of construction of this section. Heckman & Shell v. Wilson, 158 M 47, 487 P2d 1141 (1971).

Separate and Distinct Agreement: Testimony of a separate and distinct oral agreement can be received only when it does not conflict with or contradict or add to what is contained in the written contract. Warner v. Johns, 122 M 283, 201 P2d 986 (1949).

What Constitutes Oral Collateral Agreement Within Exception to Rule: An oral agreement, to be collateral within the meaning of the exception to the parol testimony rule (this section and 28-2-905) and as such admissible in evidence as against the objection that it varies a written instrument, must relate to a subject distinct from that to which the writing applies; the writing must remain intact after the reception of the parol testimony. Cont. Oil Co. v. Bell, 94 M 123, 21 P2d 65 (1933).

Obligations Assumed: Where a party seeks to recover on a written contract of sale, resort must be had to it alone, under this section, in determining the obligations assumed by defendant in attaching his name to it. Lewis v. Aronow, 77 M 348, 251 P 146 (1926).

Railroad Passenger Ticket: Plaintiff, having been compelled to purchase a passenger ticket to enable him to ride on freight train with his horse, was entitled to the benefit of such contract and could not be limited to the conditions of the shipping contract as to the amount of damages recoverable or as to the time within which his claim for damages for personal injuries was required to be presented under it. Jepsen v. Gallatin Valley Ry., 59 M 125, 195 P 550 (1921).

Attorney General's Opinions

Termination of Payments in Lieu of Participation in Group Health Plan for Nonunion County Employee: The Board of County Commissioners may terminate payments in lieu of participation in a group health plan for a nonunion county employee only if termination is consistent with the county's employment agreement with the employee. 51 A.G. Op. 11 (2005).

28-2-905. When extrinsic evidence concerning a written agreement may be considered.

Case Notes

Writing Presumed to Contain All Terms 260
Contemporaneous Oral Agreements 263
Mistake or Imperfection of Writing 266
Validity of Agreement Disputed 267
Circumstances of Execution 271
Ambiguity 275
Fraud 280
Miscellaneous 282

WRITING PRESUMED TO CONTAIN ALL TERMS

Claims of Oral Misrepresentations Precluded by Terms of Written Contract — Applicability of Parol Evidence Rule: An agreement for the sale of a trailer park contained multiple written terms, including plaintiff's agreement that he had not relied on any assurances as to the condition of the property. In a subsequent disagreement over the condition of the trailer park water system, plaintiff sought to introduce evidence of oral statements made by the seller that the water system was in good or fine condition and that plaintiff had relied on the statements to his detriment. The District Court properly applied the parol evidence rule to exclude the evidence. Plaintiff could not claim that, pursuant to the written contract, he had not relied on any assurances and then claim that he was misled by oral statements contradictory to the contract. Deschamps v. Treasure St. Trailer Ct., Ltd., 2010 MT 74, 356 Mont. 1, 230 P.3d 800, distinguishing Jenkins v. Hillard, 199 Mont. 1, 647 P.2d 354.

No Ambiguity in Complete, Final Sales Agreement — Parol Evidence Inadmissible: The parties entered a sale agreement for a ready-mix concrete plant. Plaintiff subsequently filed an action alleging that defendant violated the agreement by breaching the covenant to not compete and the covenant of good faith and fair dealing, which constituted malice resulting in lost profits, sales, and goodwill. The District Court granted summary judgment to defendant and plaintiff appealed, but the Supreme Court affirmed. The District Court correctly concluded that the sales agreement constituted a complete, final agreement and unambiguously did not include a noncompetition provision, but in fact provided that plaintiff would sell concrete to defendant for use in the area. The intention of the parties was ascertainable from the writing alone, and the agreement was presumed to represent all transactions regarding elements extrinsic to the agreement and was thus considered complete and final, so parol evidence was inadmissible. Richards v. JTL Group, Inc., 2009 MT 173, 350 M 516, 212 P3d 264 (2009). See also Lindey's, Inc. v. Professional Consultants, Inc., 244 M 238, 797 P2d 920 (1990), and Mary J. Baker Revocable Trust v. Cenex Harvest States, Cooperatives, Inc., 2007 MT 159, 338 M 41, 164 P3d 851 (2007).

Clear and Unambiguous Easement Language — Contract Principles Applied to Interpretation of Easement: After an initial conveyance of property, Tract A-1 was burdened by three easements: (1) an existing driveway; (2) an alternative drainfield easement; and (3) a trapezoid-shaped parcel called the trapezoid easement, which was designated as an easement for access to a seepage pit and alternative drainfield for an adjoining tract entitled "Tract 1". Following the subdivision of Tract 1 into Tract 1-A and Tract 1-B, the Linfords conveyed Tract 1-B to the Bings, but still continued to possess Tract 1-A and continued to benefit from the access easement. When Tract 1-A was later conveyed to the Bings, they acquired the same right to use easements appurtenant to the dominant estate that the Linfords previously enjoyed. A dispute then arose with the Mularonis, the owners of Tract 1-A, who contested the validity of the trapezoid easement, arguing that when the Bings took title to Tract A-1 from the Linfords, a merger of titles occurred that extinguished the easements. The District Court impliedly rejected the merger argument by holding that the easement burdening Tract A-1 benefited both Tract 1-A and Tract 1-B, and the Supreme Court concurred. In order to extinguish an easement by merger, there must be unity of title or ownership, coextensive in validity, quality, and all other circumstances of right. The language describing the trapezoid easement as an easement for access was clear and unambiguous and created a general access easement. Applying principles of contract interpretation to the transfer of property, the Supreme Court held that the incorporation of the certificate of survey into the deeds conveying the tracts to the Bings clearly and effectively described the easements in question and that the District Court did not err in finding that the Bings were entitled to general access across the trapezoid easement. Mularoni v. Bing, 2001 MT 215, 306 M 405, 34 P3d 497 (2001).

Bridle Path Easement — Express Easement by Reservation Versus Implied Easement — Extrinsic Evidence Regarding Parties' Intent Inadmissible: Purchasers in a subdivision had language in their deeds creating an express easement for a bridle path in the subdivision. The bridle path was never built, and over the years, the easement was obstructed by improvements on the lots of several subdivision residents. Eventually, the subdivision association attempted to extinguish the easement at a meeting of the board of directors. Some residents asked the District Court to establish the validity of the easement and to restrain obstruction of the easement, and their request was granted by partial summary judgment. On appeal, the Supreme Court noted the difference between an implied easement, which is a creature of equity dependent on the intent of the parties, and an express easement by reservation, which is a creature of the documents of conveyance and the record. An express easement by reservation arises when the purchaser's deed refers to the plat where the easement is clearly depicted and labeled. In this case, the intent of the parties to create a bridle path easement was manifested through the language in the deeds and the plat, so under this section, extrinsic evidence regarding the intent of the parties was inadmissible. Further, the subdivision association was given oversight of the easement, but not ownership of it, and so lacked authority to extinguish the easement. The lower court's finding that a valid bridle path easement existed was affirmed. Pearson v. Virginia City Ranches Ass'n, 2000 MT 12, 298 M 52, 993 P2d 688, 57 St. Rep. 65 (2000), following Missoula v. Mix, 123 M 365, 214 P2d 212 (1950), Bache v. Owens, 267 M 279, 883 P2d 817 (1994), Halverson v. Turner, 268 M 168, 885 P2d 1285 (1994), and Tungsten Holdings, Inc. v. Parker, 282 M 387, 938 P2d 641, 54 St. Rep. 399 (1997), and distinguishing White v. Landerdahl, 191 M 554, 625 P2d 1145, 38 St. Rep. 412 (1981).

Goodwill as Intangible Asset of Business: A contract for sale of a radio station that transferred "all fixed and other assets tangible and intangible" was presumed to include goodwill though goodwill was not specifically mentioned in the contract. Goodwill is considered an intangible asset of a business. W. Media, Inc. v. Merrick, 224 M 28, 727 P2d 547, 43 St. Rep. 1991 (1986), citing Baldwin v. Stuber, 182 M 501, 597 P2d 1135 (1979).

Merger of Prior Agreement Into Deed — No Presumption of Surrender of Covenants: Appellants contended that since there was no express language in deeds recorded in 1972 that the parties intended to merge the restrictive provisions of a 1971 agreement into the deeds, the commercial use restrictions in the 1971 agreement still applied, regardless of being left out of the deeds. The Supreme Court, recalling its decision in Story v. Montforton, 112 M 24, 113 P2d 507 (1941), noted that "whether or not there has been a merger depends on the intention of the parties". The court applied this principle in Thisted v. Country Club Tower Corp., 146 M 87, 405 P2d 432 (1965), quoting Reid v. Sykes, 27 Ohio St. 285: "... evidence of that intention may exist in or out of the deed. There is no presumption that a party, in giving or accepting a deed, intends to give up the covenants of which the deed is not a performance or satisfaction." In the present case, the court found strong evidence that the deeds contained all of the restrictions on the lands that were intended by the parties and that the contract had merged in the deeds. Haggerty v. Gallatin County, 221 M 109, 717 P2d 550, 43 St. Rep. 674 (1986).

Retail Installment Sale — Evidence Supporting — Allowable Interest: Defendant failed to make payment for materials supplied by plaintiff. The invoices of purchase stated that an interest rate of 1.5% a month would be levied on past due accounts. Plaintiff filed a mechanics' lien (now construction lien) representing the amount due and the service charge of 1.5% a month. Plaintiff sued to foreclose the lien. Defendant filed a confession of judgment for the full amount of purchase, plus interest at a legal rate. Plaintiff rejected the confession of judgment. Judgment was entered in favor of plaintiff for the amount of purchase, plus interest at a rate of 10% a year. Plaintiff appealed, seeking interest at the 1.5% a month rate. The Supreme Court held that the invoices, two of which were signed by both parties, describing the material purchased and stating the amount, including the interest rate to be charged, were sufficient to obligate defendant to pay the 1.5% charge on the unpaid balance. Although the invoices did not meet all the requirements of a retail installment contract, defendant's admission as to their authenticity and confession of judgment more than adequately evidenced that the purchases were retail installment sales. O'Neil Lumber Co. v. Nickelodeon Co., 190 M 25, 617 P2d 1291, 37 St. Rep. 1731 (1980).

Sale of a Business — Automatic Passing of Goodwill: Seller operated a barber shop in leased premises. He agreed to sell the shop to the defendant. The selling agreement referred to the permanent fixtures and furniture, the shop name, and the phone number. The agreement did not mention goodwill. A dispute arose when the buyer refused to pay the seller. In response the seller removed all his fixtures, disconnected the phone, and brought suit. The Court held that even though the buyer received none of the items referred to in the contract, he received goodwill and was therefore liable for the reasonable value of the goodwill. The rule is that if goodwill is not expressly reserved or excepted, it passes automatically to the purchaser of a business. Baldwin v. Stuber, 182 M 501, 597 P2d 1135 (1979).

Lease of State Lands: The Statute of Frauds barred testimony of an alleged oral agreement to sell or assign a state lease when written lease agreements provided specifically for a sublease. Montana law is clear that evidence of oral representations, relating directly to the subject matter of a contract, are not admissible to add to or alter the provisions of a written contract. Furthermore, the alleged oral agreement involved an agreement to transfer an interest in real property and thus is required to be in writing. Aye v. Fix, 176 M 474, 580 P2d 97 (1978).

Written Contract Controlling: Statements made by various agency personnel in regard to continued use of defendant's office building were not admissible under parol evidence rule to alter or contradict terms of express written contract since such statements and assurances did not come within any recognized exception to rule and since defendant admitted that he knew written contract would be controlling. U.S. v. Willard E. Fraser Co., 308 F. Supp. 557 (D.C. Mont. 1970), affirmed U.S. v. Willard E. Fraser Co., 459 F2d 483 (9th Cir. 1972).

Joint Venture Agreement: Trial court could have excluded evidence relating to an agreement for a joint venture, none of which was in writing, as being designed to alter or vary the terms of a note made by one joint venturer and held by the other. Barrett v. Morton, 137 M 190, 351 P2d 601 (1960).

Escrow Agreement: Where escrow agreement in connection with sale of land required $700 to be paid by a certain date, oral evidence could not be received to show that there had been an extension of time. Herman v. Herman, 123 M 39, 207 P2d 1155 (1949), distinguished in Dalakow v. Geery, 132 M 457, 318 P2d 253 (1957).

Correspondence Constituting Contract: An instruction in an action for breach of contract based largely upon correspondence between the parties that all papers or other instruments made by the parties at the same time and relating to the same subject matter should be considered by the jury as constituting one contract, if the preponderance of the evidence so showed, was proper. W. J. Lake & Co. v. Mont. Horse Prod. Co., 109 M 434, 97 P2d 590 (1939).

Corroborative Evidence: Where a contract whereunder the buyer was to receive one-half the freight refunds was established by a properly admitted copy of one of a number of letters, the fact that copies of the others may have been improperly admitted would not require a reversal of the judgment for plaintiff, where they were only corroborative, in the absence of substantial evidence refuting existence of the contract. W. J. Lake & Co. v. Mont. Horse Prod. Co., 109 M 434, 97 P2d 590 (1939).

Completeness of Writing: In determining whether parol testimony varied a written contract a satisfactory test is: Was the matter testified to mentioned, covered, or dealt with in the writing? If it was, then presumably, the writing was meant to represent the entire transaction, and the testimony was inadmissible. Cont. Oil Co. v. Bell, 94 M 123, 21 P2d 65 (1933).

Waiver of Rule by Introduction of Evidence: Where one party to an action on a written contract is permitted to introduce evidence of preceding oral negotiations leading up to the making of the writing, thus varying its terms, his opponent may properly give oral testimony as to the same matter, over an objection that the testimony offered tends to contradict the writing. Peterson v. Nelson, 77 M 539, 252 P 368 (1926).

Conveyance of Land: All oral negotiations relative to the covenant of seizin on a sale of land were superseded by the deed and a contemporaneous writing executed with relation thereto. Morehouse v. N. Land Co., 68 M 96, 216 P 792 (1923).

Prior Agreements Superseded:

Under this section and 28-2-904, when a contract has been reduced to writing its contents cannot be added to, contradicted, altered, or varied by parol or extrinsic evidence, and the writing supersedes all oral negotiations concerning its matter which preceded, accompanied, or led up to its execution. Webber v. Killorn, 66 M 130, 212 P 852 (1923).

Testimony concerning an alleged oral agreement between vendor and vendee that the latter bought the land subject to the right of possession of a tenant, in contravention of the recital in the deed, was inadmissible under the rule that execution and delivery of the deed supersede all former oral agreements. Adams v. Durfee, 67 M 315, 215 P 664 (1923).

Parol testimony to show the understanding of the parties that no interest was to be paid on a promissory note which provided for the payment of interest but did not specify the rate was properly excluded. Burnett v. Burnett, 68 M 546, 219 P 831 (1923).

A written agreement must be considered as containing all prior oral ones concerning its subject matter and its terms may therefore not be varied by oral testimony. Leigland v. Rundle Land & Abstract Co., 64 M 154, 208 P 1075 (1922).

Negotiations Prior to Contract:

In an action for damages for breach of a clause of a written contract of sale of a threshing machine warranting it as being well made of good material and that with proper use and management it would do as good work as any other machine of the same size manufactured for the like purpose, evidence of statements made by defendant's agent in making the sale that it would thresh and clean alfalfa as well as any other machine of the same size, etc., was properly rejected as an attempt to vary the terms of the written instruments by parol. Rowe v. Emerson-Brantingham Implement Co., 61 M 73, 201 P 316 (1921).

Prior oral negotiations and directions as to points at which livestock should be stopped for resting and feeding were merged in the contract of shipment, where it and the waybills bore notations stating the points at which stops were to be made, and therefore parol testimony of directions to make other stops was incompetent as an attempt to vary the terms of the written contract. Cook v. N. Pac. Ry., 61 M 573, 203 P 512 (1921).

A written contract supersedes any oral negotiations theretofore had relative to the subject matter of it, and must be considered as containing all of its terms agreed upon at the time it was executed. Arnold v. Fraser, 43 M 540, 117 P 1064 (1911).

Clear Language: Where in an action on a written contract, there was not any issue of fraud or mistake in the execution of it, or any imperfection in the writing, but the provisions of such instrument were plain and unambiguous, parol evidence, the tendency of which was to vary the terms thereof, was properly excluded. W. Loan & Sav. Co. v. Smith, 42 M 442, 113 P 475 (1911). See also Beebe v. Bd. of Directors of the Bridger Creek Subdivision Community Ass'n, 2015 MT 183, 379 Mont. 484, 352 P.3d 1094, holding that failure to identify ambiguity in an association's bylaws excluded consideration of extrinsic evidence.

Common-Law Rule: This section merely declares the common-law rule. Riddell v. Peck-Williamson Heating & Ventilating Co., 27 M 44, 69 P 241 (1902); Gaffney Mercantile Co. v. Hopkins, 21 M 13, 52 P 561 (1898).

CONTEMPORANEOUS ORAL AGREEMENTS

Sufficient Evidence of Written Fixed Price Contract and Subsequent Binding Oral Agreements for Additional Construction Work: Defendant contracted in writing to perform concrete work at plaintiff's construction project, and the parties also orally agreed that additional concrete work would be done. A dispute arose concerning the existence of the contracts, the amount owed to defendant, and whether plaintiff had waived deficiencies in the work. The Supreme Court affirmed the existence of a written fixed price contract for the initial work and subsequent binding oral agreements for additional work. Defendant's completion of the work entitled him to the full amount called for in the written contract less an amount granted to plaintiff for repair of deficiencies in the work. As for the oral agreements, defendant's billing was the correct amount due for the additional services provided. The trial court also correctly apportioned the amount due to plaintiff for correcting deficiencies in the work, given that plaintiff waived or caused many of the deficiencies by accepting the work, making improper additions to the work, and issuing hasty and ill-conceived commands. Weimar v. Lyons, 2007 MT 182, 338 M 242, 164 P3d 922 (2007).

Refusal to Enforce Unsubstantiated Oral Agreement to Dismiss Claim for Prescriptive Easement — Parol Evidence Rule and Statute of Frauds Inapplicable: Defendant contended that the District Court erred in failing to estop plaintiff from asserting claims for a prescriptive easement across defendant's property because an agent of plaintiff orally agreed to dismiss the claims and defendant relied on the promise to defendant's detriment. The District Court held that the parol evidence rule and the statute of frauds prohibited admission of evidence of an oral agreement to dismiss the case because there were written temporary access agreements in place and that defendant did not offer sufficient evidence to meet either a fraud or estoppel exception to the parol evidence rule. The Supreme Court found that the trial court reached the correct result, albeit for the wrongs reasons, by automatically applying the parol evidence rule and the statute of frauds without determining whether either rule applied. Actually neither rule barred admission of the evidence in this case, so the trial court was free to consider the merits of the existence of an oral contract without defendant having to prove the elements of fraud or detrimental reliance. Nevertheless, the trial court found defendant's story of an oral agreement to be unsubstantiated and correctly refused to enforce an oral agreement based on the facts before it. Brimstone Min., Inc. v. Glaus, 2003 MT 236, 317 M 236, 77 P3d 175 (2003).

Defaulting Buyer Under Unambiguous Written Contract Cannot Rely Upon Expectations Not Covered by Contract to Avoid Contract — Disposition of Downpayment Amounts Paid and Due — County Not Liable for Negligent Misrepresentation as to Recordability of Deeds and Seller's Title Insurer Not Liable for Loss in Marketability: Documents for the sale and purchase of two sections of land unambiguously showed, and it was undisputed, that the resale of 20-acre parcels by the buyer, the immediate acceptance by the county of 20-acre resale deeds of a type that would make subdivision review unnecessary, and the ability to resell without having to undergo subdivision review were not parts of the bargain. The parties knew that these things were contemplated, but the documents did not refer to them or make them a part of the contract. Before the contract was made, the county indicated that it would accept the 20-acre resale deeds. The deal fell through when the county changed its position after the contract was signed. The buyer failed to pay the whole downpayment, and the seller terminated the contract and kept the paid portion of the downpayment. Precontract discussions on the matter must be disregarded as parol evidence because the documents were unambiguous and did not refer to the matter. The buyer was not entitled to rescind the contract and have the paid portion of the downpayment returned based on mutual mistake or failure of consideration. There was no mutual mistake because the parties knew that it was not a certainty that the county would accept the deeds. There was no failure of consideration because the resale, county acceptance of the deeds, and avoidance of subdivision review were not part of the written contract. In addition, the need for a subdivision review would not make the land unmarketable; at most, its market value decreased and it would take longer to sell it. Furthermore, a party in default is not entitled to rescission. The seller was entitled to terminate the contract. The seller was also entitled to keep an amount of the paid portion of the downpayment equal to the amount by which the contract price for the land exceeded the market value of the land at the time of the breach. The seller was not entitled to keep the remainder of the paid portion of the downpayment or to a judgment for the unpaid portion of the downpayment because the contract did not provide for that remedy. The county was not liable in tort to the seller for negligent misrepresentation, and the buyer's title insurance company was not liable to the seller for the loss in the marketability of the land caused by the need for subdivision review. Yellowstone II Dev. Group, Inc. v. First Am. Title Ins. Co., 2001 MT 41, 304 M 223, 20 P3d 755 (2001), overruled in Mary J. Baker Revocable Trust v. Cenex Harvest St., Cooperatives, Inc., 2007 MT 159, 338 M 41, 164 P3d 851 (2007), to the extent that Yellowstone II held that the determination of whether a term in a contract is ambiguous is not a question involving parol evidence.

Parol Evidence by Insureds Against Their Insurance Agent in Regard to Contract That Agent Was to Procure Between Insureds and Insurer: The parol evidence rule is applicable only between the parties to a written contract and parties who are privy to the contract and cannot be invoked either by or against a stranger to the contract. An insurance agency had an agent contract with the insureds to procure insurance for them but did not have an agency contract with the insurer and was not a party or privy to the contract between the insureds and the insurer. Therefore, in a breach of contract and negligence action by the insureds against the agency, the court properly allowed the insureds to introduce parol evidence of negotiations between the insureds and the agent and of the agent's oral representations. Furthermore, although the insureds and the insurer had a written contract, the insureds and the agency did not. Fillinger v. NW. Agency, Inc., of Great Falls, 283 M 71, 938 P2d 1347, 54 St. Rep. 500 (1997), distinguished in Habets v. Swanson, 2000 MT 367, 303 M 410, 16 P3d 1035, 57 St. Rep. 1567 (2000). See also Bailey v. St. Farm Mut. Auto. Ins. Co., 2013 MT 119, 370 Mont. 73, 300 P.3d 1149, in which the Supreme Court concluded that because the insureds placed the validity of the insurance application at issue by representing that they did not fill it out or understand its terms and that the application did not contain the coverage that they requested, evidence of the insureds' statements during the application process was not barred by the parol evidence rule.

Contract for Elk Sale — Telephone Conversations Occurring After Contract Admissible — Oral Agreement Extending Contract Cutoff Dates Inadmissible but Promise Enforced: Seller appealed a District Court judgment awarding buyer damages after seller breached contracts for the sale of elk. Seller entered into contracts agreeing to deliver elk before April 1 and May 1 and in subsequent telephone conversations promised to deliver elk after these contract cutoff dates. While the parol evidence rule bars prior or contemporaneous oral agreements, the Supreme Court affirmed the District Court decision allowing testimony regarding telephone conversations that occurred after the written agreements. The buyer, to his detriment, entered into third-party contracts to resell the elk in reliance on the seller's promise that the elk would be available and delivered after the contract cutoff dates. The Supreme Court ruled that enforcing the oral agreement extending the cutoff dates of the contract avoided an injustice to the buyer. Trad Indus., Ltd. v. Brogan, 246 M 439, 805 P2d 54, 48 St. Rep. 51 (1991).

Contract Silent on Payment Procedure — Evidence of Supplemental Agreement Admissible: Defendant entered a lease agreement with Town Pump, Incorporated to operate a gas station. The monthly rental agreement was detailed in a written lease agreement. At trial, the District Court allowed employees of Town Pump to testify that Town Pump required defendant to make daily payment for all gasoline sold. Defendant objected to this testimony based on the parol evidence rule. Before a party to a contract can claim applicability of the parol evidence rule, there must be a showing that the written instrument is a complete and final document intended by the parties to contain all the terms of the contract. The lease agreement was silent on payment procedure and even contained a provision allowing the parties to mutually agree on payment terms and conditions. The parol evidence rule was inapplicable. St. v. Frederick, 208 M 112, 676 P2d 213, 41 St. Rep. 207 (1984). See also In re Estate of Stukey, 2004 MT 279, 323 M 241, 100 P3d 114 (2004).

Refund Agreement: In an action to recover the balance due under a contract of sale of gasoline to a dealer under a written contract fixing the price, parol testimony of defendant tending to prove an oral contract to refund a portion of the price was held inadmissible under the rule. Cont. Oil Co. v. Bell, 94 M 123, 21 P2d 65 (1933).

Collateral Agreement: An oral agreement, to be collateral within the meaning of the exception to the parol testimony rule, and as such admissible in evidence as against the objection that it varies a written instrument, must relate to a subject distinct from that to which the writing applies; the writing must remain intact after the reception of the parol testimony. Cont. Oil Co. v. Bell, 94 M 123, 21 P2d 65 (1933).

Time or Method of Payment: Parol evidence of an oral agreement, made contemporaneously with a promissory note which contains an absolute promise to pay at a specified time, is not admissible to extend the time of payment or to provide for payment in any other way than that so specified, or to make it depend upon condition. Hosch v. Howe, 92 M 405, 16 P2d 699 (1932).

Extension of Time: Where in an action by a building contractor to foreclose a mechanics' lien (now construction lien) defendant set up a counterclaim for damages for failure to complete the building within the time stipulated, but the contract provided that no additional time should be allowed unless request therefor was presented in writing to the architect, and plaintiff failed to make such request though the owner had directed alterations, he was precluded from asserting that before signing the contract defendant had orally agreed that the penalty therein provided for would not be enforced. Leigland v. Rundle Land & Abstract Co., 64 M 154, 208 P 1075 (1922).

Execution Before Contract: The mere execution of a bill of sale by the seller does not exclude proof of a parol agreement for the sale of an animal offered by the buyer, the terms of which had been agreed upon and the purchase price paid before the execution of the bill. Sutherland v. Green, 49 M 379, 142 P 636 (1914).

Usage and Custom: Evidence that at the time a written contract was made an oral contract was entered into that payments should be made in conformity with a usage and custom, as the work was done and materials furnished, was not admissible. Riddell v. Peck-Williamson Heating & Ventilating Co., 27 M 44, 69 P 241 (1902).

Mining Claim: Testimony by lessees that they would not have signed the lease of a lode mining claim but for an understanding that the time would be extended was not admissible to show a contemporaneous agreement to extend. Evidence of a contemporaneous agreement between the parties to a written sublease of said claim that in case the sublessors should buy the property the lease would be extended was inadmissible. Armington v. Stelle, 27 M 13, 69 P 115 (1902), distinguished in Orem v. Hansen Packing Co., 91 M 222, 7 P2d 546 (1932). See also Kelly v. Ellis, 39 M 597, 104 P 873 (1909), distinguished in Orem v. Hansen Packing Co., 91 M 222, 7 P2d 546 (1932).

Construction of Terms: Where it was alleged that at the time of the execution of a written agreement it was agreed that a particular construction should be given to the terms of the writing, to the effect that it meant that the collateral security should be exhausted before an action was commenced on the notes, such contemporaneous construction was within the purview of this section. Fisher v. Briscoe, 10 M 124, 25 P 30 (1890). See also Bohn Mfg. Co. v. Harrison, 13 M 293, 34 P 313 (1893).

Principal to Be Paid First: Evidence of a parol agreement, at the time of the making of a promissory note, that in case the same was not paid at maturity, subsequent payments might be applied upon the principal first and the interest afterward, is improper. Anderson v. Perkins, 10 M 154, 25 P 92 (1890). See also Gaffney Mercantile Co. v. Hopkins, 21 M 13, 52 P 561 (1898); York v. Steward, 21 M 515, 55 P 29 (1898).

MISTAKE OR IMPERFECTION OF WRITING

Extrinsic Evidence Permissible Based on Parties' Intent — Intent Defeated by Mistakes in Vital Facts: The District Court did not err by considering extrinsic evidence to interpret and reform the parties' contract. Generally, when the terms of an agreement are reduced to writing by the parties, the writing is considered as containing all those terms and there can be no evidence of the terms of the agreement other than the contents of the writing. However, an exception to this rule permits extrinsic evidence to be admitted when a mistake or other imperfection of the writing is put at issue. The District Court correctly concluded that the recorded agreement did not reflect the parties' intent. The mistakes in the agreement constituted "vital facts" that defeated the parties' contractual intentions. It was therefore appropriate for the District Court to consider extrinsic evidence and to reform the contract to reflect the parties' true intent. In re Platt, 2018 MT 43, 390 Mont. 338, 413 P.3d 818.

Reformation of Insurance Policy Not Permitted — Clear and Explicit Language Used — Lack of Due Diligence in Discovering Error Not Justifying Reformation: An insurer attempted to reform an insurance policy on the ground that the policy should not cover property near a structure that was specifically exempted from the policy. However, the policy specifically included property within 1,000 feet of other insured property, including property around the exempted structure. The District Court applied 33-15-302 and determined that it was prohibited from reforming insurance policies. On appeal, the Supreme Court also declined to reform the contract, as the language was clear and explicit, due diligence would have uncovered the error, and the insurer failed to establish that its insurance policy expressed something other than what the parties mutually intended. Lincoln County Port Authority v. Allianz Global Risks US Ins. Co., 2013 MT 365, 373 Mont. 60, 315 P.3d 934.

Extrinsic Evidence Properly Admitted to Prove Original Contract Intent — Reformation of Warranty Deed Based on Mutual Mistake Proper: Extrinsic evidence provided by plaintiffs to prove the parties' original intent in entering a buy-sell agreement proved that, by virtue of a mutual mistake, the deed did not contain agreed-upon restrictions. The evidence was squarely within the exception to the parol evidence rule, and the District Court did not err in admitting the parol evidence or in reforming the deed to include the restrictions and enforcing the restrictions against defendants. Thibodeau v. Bechtold, 2008 MT 412, 347 M 277, 198 P3d 785 (2008), following Interstate Prod. Credit Ass'n v. DeSaye, 250 M 320, 820 P2d 1285 (1991).

Parol Evidence on Month and Day of Contract Admissible Where Parties Themselves Presented Parol Evidence on Year of Contract: Buyer failed to pay entire purchase price for irrigation system, and seller sued. Since buyer counterclaimed for crop losses allegedly resulting from seller's failure to install system within a reasonable time of contract, the exact date of the contract was an issue at trial. Seller submitted a copy of the contract dated May 20, 1976. Both parties agreed that the year was incorrect, as the transaction had actually taken place in 1977. However, the buyer claimed that the contract had been made in April, not May, and the District Court permitted him to present evidence in support of this. Seller appealed, claiming it was improper to allow the admission of parol evidence in contradiction of the terms of the contract. The Supreme Court held that since parol evidence had been allowed on the year of the contract, it was allowable for the month and day also. Ag Sales v. Klose, 199 M 400, 649 P2d 447, 39 St. Rep. 1482 (1982).

Businessman Neglecting to Read Contract — Not a Mistake: A real estate developer who failed to exercise the care and prudence of a reasonable and cautious businessman by neglecting or failing to read contracts for deeds that he signed may not rely upon this section to allow admission of oral testimony because 28-2-904, concerning the written instrument superseding negotiations, is to be given the greater weight when the proffered evidence, as here, is insufficient to establish mistake. Silva v. McGuinness, 189 M 252, 615 P2d 879, 37 St. Rep. 1401 (1980).

Clear Language: Parol testimony was not admissible to extend the term of a permissive easement beyond the expiration date set in a written agreement that clearly contained no mistake, imperfection, or ambiguity. Larson v. Burnett, 158 M 421, 492 P2d 921 (1972).

Pleadings Varying Terms of Agreement: In action by sellers of hotel business, including personal property, against buyers for balance due on contract, answer setting up affirmative defenses which pleaded mistake and invalidity based on representations and warranties of seller concerning the leasing of the premises on which the buyers relied was sufficiently clear to comply with this section as against motion to strike on the ground that the allegations tended to vary the terms of a written contract. Swecker v. Badura, 141 M 329, 377 P2d 752 (1963).

Misunderstanding of Conversations: Where a land contract required of the vendor the execution of a deed without reservations and the deed deposited in escrow excepted from its operation the timber growing thereon, parol evidence to the effect that the witness understood from conversations with the vendee that the latter was buying the land without the timber was inadmissible under this section. Hollensteiner v. Anderson, 78 M 122, 252 P 796 (1927).

Manner of Payment: Where the signers of a promissory note unqualifiedly bound themselves to pay a certain sum of money at a specified time, parol evidence was inadmissible for the purpose of showing that the payee in an oral contemporaneous stipulation had agreed that payment could be made in a certain manner; such oral agreement was superseded by the writing, and the evidence erroneously admitted tended to vary and contradict the writing, contrary to the provisions of this section, where the validity of the note was not attacked and a mistake or imperfection in the writing was not pleaded. Swan v. LeClair, 77 M 422, 251 P 155 (1926).

Endorsement on Instrument: In an action on a promissory note which had never been previously negotiated and was overdue when plaintiff acquired it by assignment, so that he was not a holder in due course, parol evidence was admissible to show that defendants with plaintiff's knowledge had endorsed the note with the understanding that each was doing so as representative of an association and not in his personal capacity. Anderson v. Border, 75 M 516, 244 P 494 (1926), distinguished in Swan v. LeClair, 77 M 422, 251 P 155 (1926).

Guaranty Agreement: An offer of proof by defendant directors, who had guaranteed payment of an account as represented by a note of the corporation, that it was their understanding that the guaranty was to be deemed merely an assurance on their part that plaintiff's account was recognized as a valid claim against the company was properly rejected under this section as contradicting the terms of the writing. Schauer v. Morgan, 67 M 455, 216 P 347 (1923).

Stranger as Party to Action: The rule that parol evidence cannot be introduced to vary, enlarge, or contradict its terms, except where a mistake or imperfection therein is put in issue by the pleadings, or when the validity of the contract is the fact in dispute, does not apply in a controversy between a party to the contract and a stranger; as against such stranger, a party may assert that the agreement was other or different in any respect from that which the writing expresses. Read v. Lewis & Clark County, 55 M 412, 178 P 177 (1919), distinguished in Habets v. Swanson, 2000 MT 367, 303 M 410, 16 P3d 1035, 57 St. Rep. 1567 (2000).

Purpose of Contract: Where a contract supplemental to one made for the sale of lands recited that it was made for the purpose of granting the buyer additional time in which to make payment, it precluded the idea that it was made for any other purpose, and in the absence of allegation of mistake or other imperfection, the presumption is conclusive that the writing contained all the engagements then made by the parties. Crawford v. Pierse, 56 M 371, 185 P 315 (1919).

Bill of Sale: Parol evidence that parties did not intend to include buildings described in a bill of sale was inadmissible. Hogan v. Kelly, 29 M 485, 75 P 81 (1904).

VALIDITY OF AGREEMENT DISPUTED

No Improper Reliance on Extrinsic Evidence in Finding of Valid and Enforceable Express 60-Foot Easement for Subdivision: Defendant acquired certain property after an express easement across the property was created by the former owner. Defendant refused to allow the building of an access road across the property, contending that the easement agreement was invalid on several grounds. The District Court examined the agreement and concluded that the easement was valid and enforceable and granted summary judgment for plaintiffs. On appeal, defendant asserted that the District Court erroneously relied on facts outside the agreement, making summary judgment inappropriate, but the Supreme Court affirmed. For purposes of interpreting a writing granting an interest in real property, evidence of the surrounding circumstances, including the situation of the property and the context of the parties' agreement, may be shown so that the judge is placed in the position of those whose language the judge is to interpret. However, to comply with the statute of frauds and the recording system, the writing itself must ultimately stand on its own and meet the formal requirements for granting a property interest. In this case, the District Court was allowed to consider various facts not contained in the easement agreement for purposes of understanding the situation, but the court's analysis of the easement's validity apparently was limited to the face of the agreement, so the court did not erroneously rely on extrinsic facts. The easement agreement satisfied the formal requirements for expressly granting an easement and created a valid 60-foot emergency public access and utility easement that was enforceable against defendant. Additionally, the District Court properly concluded that because there was no dominant tenement, the easement was in gross and could be used by members of the public to travel between the subdivision and the public highway for emergency purposes and to provide utility services. There being no questions of material fact, summary judgment was proper. Broadwater Dev., LLC v. Nelson, 2009 MT 317, 352 M 401, 219 P3d 492 (2009), distinguishing Blazer v. Wall, 2008 MT 145, 343 M 173, 183 P3d 84 (2008). See also Kuhlman v. Rivera, 216 M 353, 701 P2d 982 (1985).

Promissory Note Not Considered Contract of Adhesion: Plaintiff read and signed a promissory note to secure a loan for a friend who subsequently went bankrupt. The promissory note provided that plaintiff waived the right to rely on the defense of impairment. Nevertheless, after defendant bank foreclosed on the property that plaintiff used to secure the loan, plaintiff claimed impairment, arguing that the waiver constituted a contract of adhesion that was unenforceable. The District Court disagreed, and plaintiff appealed. The Supreme Court noted that a contract of adhesion is a contract whose terms are dictated by one party to another who has no voice in the contract's formulation and that the contract is unenforceable if it is not within the expectations of the weaker party or if the contract terms are unduly oppressive, unconscionable, or against public policy. Plaintiff was a sophisticated businessman who did not attempt to negotiate the contract terms and who studied the contract prior to signing and thus could not later claim that he was unaware of the waiver provision and that it was not within his reasonable expectations. Although the bank prepared the contract, the transaction was entered solely at plaintiff's behest, and plaintiff voluntarily waived the defense of collateral impairment under 30-3-607. Therefore, the Supreme Court concluded that the promissory note was not a contract of adhesion, nor were the contract's general provisions outside of plaintiff's reasonable expectations. The District Court was affirmed. Denton v. First Interstate Bank of Commerce, 2006 MT 193, 333 M 169, 142 P3d 797 (2006), following Kloss v. Edward D. Jones & Co., 2002 MT 129, 310 M 123, 54 P3d 1 (2002).

Investment Agreement Containing Arbitration Clause Considered Contract of Adhesion — Remand for Consideration of Investor's Reasonable Expectations and Potential Contract Formation Defenses: Zigrang entered an investment agreement with defendant investment company. The agreement contained an arbitration provision. When Zigrang learned that defendant frequently traded securities in Zigrang's account without permission, Zigrang filed a complaint, which was one of 23 suits filed by investors alleging defendant's mismanagement of accounts. Defendant moved to compel arbitration pursuant to the agreement. A panel of three judges sat en banc to hear evidence common to all 23 cases. Defendant's motion to compel arbitration was denied, but the order contained common findings of fact that did not apply to Zigrang, including a mischaracterization of Zigrang's investment agreement. Defendant appealed. The Supreme Court noted that the agreement constituted a contract of adhesion that supported other contract formation defenses, but did not in itself constitute a sufficient basis for invalidating the agreement. The Supreme Court was unable to completely examine Zigrang's contract formation defenses, including unconscionability, waiver, and reasonable expectations, because the District Court's order relied on the mistaken finding of fact. Thus, the court remanded for further findings of fact related to Zigrang's investment agreement, noting that an inquiry into Zigrang's expectations should consist only of an analysis of Zigrang's objectively reasonable expectations regarding the agreement from Zigrang's perspective and that Zigrang's expectations might negate the arbitration provisions. Zigrang v. U.S. Bancorp Piper Jaffray, Inc., 2005 MT 282, 329 M 239, 123 P3d 237 (2005). See also Iwen v. U.S. W. Direct, 1999 MT 63, 293 M 512, 977 P2d 989 (1999), and Kloss v. Edward D. Jones & Co., 2002 MT 129, 310 M 123, 54 P3d 1 (2002).

Predispute Arbitration Provisions Unenforceable — Motion to Compel Arbitration Properly Denied: Plaintiff opened several Piper Automatic Transfer Accounts and later brought an action alleging defendants' mismanagement of the accounts. Defendants sought to compel arbitration based on predispute arbitration clauses in the account agreements requiring that any dispute be resolved by arbitration. The motion to compel arbitration was denied, and defendants appealed. The Supreme Court held that because the agreements granted defendants' brokers the discretion to buy and sell securities, a fiduciary duty was created that defendants breached by failing to explain the consequences of the arbitration provision prior to formation of the contract. The predispute arbitration provisions were therefore unenforceable, and denial of the motion to compel arbitration was affirmed. Willems v. U.S. Bancorp Piper Jaffray, Inc., 2005 MT 37, 326 M

103, 107 P3d 465 (2005), following Kloss v. Edward D. Jones & Co., 2002 MT 129, 310 M 123, 54 P3d 1 (2002). See also Chor v. Piper, Jaffray & Hopwood, 261 M 143, 862 P2d 26 (1993).

Collective Bargaining Agreement Not Considered Contract of Adhesion: When plaintiff filed a wrongful discharge claim, defendant pointed out that the employment was covered by a union collective bargaining agreement (CBA) and that 39-2-912 precludes an employee covered by a CBA from seeking relief under the Wrongful Discharge From Employment Act. At argument in District Court on defendant's motion for summary judgment, plaintiff argued that the CBA was a contract of adhesion. The District Court held that the CBA was not a contract of adhesion and granted summary judgment, and on appeal the Supreme Court agreed. A contract of adhesion is a contract with terms dictated by one contracting party to another party who has no voice in the contract's formulation, and such contracts are unenforceable if they are not within the reasonable expectations of the weaker party or if they are unduly oppressive, unconscionable, or against public policy. Because CBAs arise only after a public employer and a union representative have bargained collectively and in good faith, it cannot be said that one party dictates the terms of a CBA to another, so a CBA cannot be considered a contract of adhesion. The court noted that under Kloss v. Edward D. Jones & Co., 2002 MT 129, 310 M 123, 54 P3d 1 (2002), a contract of adhesion may also be found in cases when an contract arbitration provision is presented on a standardized form without the opportunity for negotiation. Arbitration provisions are also negotiated in a CBA rather than dictated by standardized form, so Kloss did not apply. Summary judgment was affirmed. LaFournaise v. Mont. Developmental Center, 2003 MT 240, 317 M 283, 77 P3d 202 (2003).

Security Brokerage Contracts — Contract of Adhesion Rendering Arbitration Clause Unenforceable: Kloss opened a full-service brokerage account with defendant, which permitted Kloss to purchase securities and maintain a money market account and which included a living trust account. The account did well, and Kloss decided to set up a charitable trust with the bond proceeds. The initial account and the living trust agreement contained a mandatory arbitration clause, and the charitable trust incorporated the arbitration clause by reference. Kloss then had second thoughts about the charitable trust and petitioned to revoke it. Defendant moved to compel arbitration, and the District Court granted the motion, citing Chor v. Piper, Jaffray & Hopwood, 261 M 143, 862 P2d 26 (1993), and Iwen v. U.S. W. Direct, 1999 MT 63, 293 M 512, 977 P2d 989 (1999), for the holding that defendant had no obligation to explain the terms of the contract because it was within Kloss's reasonable expectations and that even if the contract was considered a contract of adhesion, it was not unenforceable because it was not unconscionable. Kloss appealed, arguing that the arbitration clause was part of a contract of adhesion and that waiver of the constitutional right to jury trial should not be presumed from the signing of a contract of adhesion. Defendant maintained that form contracts prepared by securities brokers are not contracts of adhesion dictated by one party to another who has no voice in its formulation, and that arbitration clauses contained in the contracts are not unconscionable. The Supreme Court examined Passage v. Prudential-Bache Sec., Inc., 223 M 60, 727 P2d 1298 (1986), for an explanation of contracts of adhesion in the securities context and the circumstances under which they are unenforceable. The court distinguished both Chor and Passage, finding that the contracts in this case were clearly contracts of adhesion because they were standardized forms containing terms that Kloss had no opportunity to negotiate if wishing to invest with defendant. Further, the arbitration clause by which Kloss waived the right to access to state courts, the right to jury trial, the right to reasonable discovery, the right to findings of fact based on the evidence, and the right to enforce the law by way of appeal was clearly not within Kloss's reasonable expectations. The arbitration clause was never explained by defendant, and Kloss was not aware of the arbitration provision in the contract. Thus, the District Court committed reversible error when it concluded that the arbitration clause was enforceable. Kloss v. Edward D. Jones & Co., 2002 MT 129, 310 M 123, 54 P3d 1 (2002), followed in Larsen v. W. St. Ins. Agency, Inc., 2007 MT 270, 339 M 407, 170 P3d 956 (2007), with regard to factors to be applied in determining a contract of adhesion.

Extrinsic Evidence on Testamentary Intent Raising Genuine Issue of Material Fact — Summary Judgment Improper: Kuralt gifted Shannon with 20 acres along the Big Hole River, disguising the transaction as a sale. Shortly before he died, he sent Shannon a letter, which constituted a holographic will, suggesting that he intended to do the same with another 90 acres. The District Court allowed introduction of the letter as extrinsic evidence regarding testamentary intent, then granted summary judgment to the estate after finding that the letter contemplated a separate testamentary instrument not yet in existence to accomplish the transfer of the Montana property. Nevertheless, the letter raised a fundamental disagreement as to a genuine material fact—namely, whether Kuralt intended that the letter effect a posthumous disposition of the property. Regardless of whether the court admitted the evidence because it considered the letter ambiguous or because it agreed with Shannon that extrinsic evidence may be discretionarily admitted in holographic will disputes, the court nevertheless improperly resolved contested issues by granting summary judgment. The Supreme Court reversed and remanded the case for trial. In re Estate of Kuralt, 1999 MT 111, 294 M 354, 981 P2d 771, 56 St. Rep. 460 (1999).

Arbitration Clause in Standardized Form Advertising Agreement — Lack of Mutuality of Obligation and Meaningful Choice Considered Unconscionable Contract of Adhesion: Iwen sued U.S. West Direct for damages for negligent construction of a yellow pages advertisement, infliction of emotional distress, and punitive damages. The District Court held that the parties were bound by the arbitration clause in the directory advertising order. The advertising order was a standardized form, the terms of which Iwen was unable to negotiate and for which Iwen's only choice was to accept or reject, constituting an agreement of adhesion. The arbitration provision lacked mutuality of obligation, was one-sided, and contained terms that were unreasonably favorable to U.S. West Direct, leaving Iwen, as the weaker bargaining party, no meaningful choice regarding acceptance of its provisions. Viewed from the perspective of consumer Iwen, the arbitration clause was held to be unconscionable, and the Supreme Court reversed, striking the arbitration clause, pursuant to 30-2-302, and remanding for further proceedings. Iwen v. U.S. W. Direct, 1999 MT 63, 293 M 512, 977 P2d 989, 56 St. Rep. 263 (1999), following Passage v. Prudential-Bache Sec., Inc., 223 M 60, 727 P2d 1298, 43 St. Rep. 1532 (1986), and Leibrand v. Nat'l Farmers Union Property & Cas. Co., 272 M 1, 898 P2d 1220, 52 St. Rep. 557 (1995), and distinguishing Snap-on Tools Corp. v. Vetter, 838 F. Supp. 468 (D.C. Mont. 1993). See also Global Client Solutions, LLC v. Ossello, 2016 MT 50, 382 Mont. 345, 367 P.3d 361.

Sufficient Evidence to Establish Contract for Line of Credit: The execution of a promissory note and the procurement by the bank of a contract of guarantee issued by the Farmers Home Administration (FmHA) pointed to and confirmed an agreement between plaintiffs and the bank for a line of credit, despite bank's contention that the contract of guarantee was between the bank and FmHA and created no obligation on bank's part to loan money to plaintiffs. Weinberg v. Farmers St. Bank of Worden, 231 M 10, 752 P2d 719, 45 St. Rep. 391 (1988), distinguished in Shiplet v. First Sec. Bank of Livingston, Inc., 234 M 166, 762 P2d 242, 45 St. Rep. 1816 (1988).

Performance Combined With Terms — Valid Contract: An agreement for development of a mineral interest did not include every item that might have been included with respect to operational aspects; however, the parties performed under the agreement for 3 years. The Supreme Court cited Wilkerson v. School District, 216 M 203, 700 P2d 617, 42 St. Rep. 745 (1985), in holding that a contract is not invalid simply because it does not contain all the provisions or conditions the parties might have incorporated into it. Therefore, performance under the agreement, combined with the actual terms provided, demonstrated the existence of a valid contract. Somont Oil Co., Inc. v. Nutter, 228 M 467, 743 P2d 1016, 44 St. Rep. 1685 (1987).

Enforceability of Arbitration Clause in Adhesion Contract: Plaintiffs contended that an arbitration clause in a brokerage agreement should have been declared unenforceable because it appeared in a contract of adhesion. The Supreme Court found nothing in the record to indicate that the arbitration clause was not within the parties' expectations or that the clause was oppressive or unconscionable. The court noted that federal case law demonstrates that arbitration clauses are common and enforceable in brokerage agreements (citing Finkle & Ross v. A.G. Becker Paribas, Inc., 622 F. Supp. 1505 (D.C. N.Y. 1985), and Southland Corp. v. Keating, 465 US 1, 79 L Ed 2d 1, 104 S Ct 852 (1984)) and held that even if the customer agreement form was an adhesion contract, the arbitration clause was enforceable. Passage v. Prudential-Bache Sec., Inc., 223 M 60, 727 P2d 1298, 43 St. Rep. 1532 (1986), followed in Chor v. Piper, Jaffray & Hopwood, 261 M 143, 862 P2d 26, 50 St. Rep. 1234 (1993), and Iwen v. U.S. W. Direct, 1999 MT 63, 293 M 512, 977 P2d 989, 56 St. Rep. 263 (1999). See also Cohen v. Wedbush, Noble, Cooke, Inc., 841 F2d 282 (9th Cir. 1988).

Waiver of Provision in Collective Bargaining Agreement Not Properly Before Court: A declaratory judgment action was brought to construe a collective bargaining agreement. The plaintiff filed a motion for summary judgment. The defendant opposed the motion and filed an affidavit in support of its opposition. The plaintiff argued that the affidavit submitted by defendant was inadmissible as a violation of the parol evidence rule. The trial court concluded that no material factual issue existed but denied the motion because of waiver by the plaintiff. The waiver issue was addressed in the affidavit but not in any of the other pleadings. The Supreme Court held that the waiver issue was not properly before the trial court and ordered the trial court to reconsider its denial of the motion for summary judgment. The Supreme Court also said that the defendant could amend its answer to affirmatively plead waiver. Butte Teachers' Union v. Bd. of Trustees, 201 M 482, 655 P2d 146, 39 St. Rep. 2248 (1982).

Validity of Agreements Underlying Purchase Contract: In a case involving a contract for the sale of land referring to the licenses of cabin owners occupying a portion of the land where validity of the terms of the license agreements are a fact in dispute, parol evidence was admissible, not to vary the terms of the agreement but to show that those agreements which appear on their face as valid binding contracts are in fact not binding. Rase v. Castle Mtn. Ranch, Inc., 193 M 209, 631 P2d 680, 38 St. Rep. 992 (1981).

Exception to Parol Evidence Rule — Harmless Error: The defendant appealed from a judgment granting specific performance of an option agreement to the plaintiff and ordering the property involved conveyed to the plaintiff. The defendant argued that the judgment should be reversed because the trial court erred in excluding his testimony on matters going to the validity of the contract. He claimed he had no authority to sign the agreement, he had no intent to sign a contract, and he raised the question whether anyone had directed that a writing be made. The trial court had excluded the offered evidence as a violation of the parol evidence rule. The offered testimony went to the validity of the contract and therefore constituted an exception to the rule under 28-2-905, but no prejudice occurred because such testimony was admitted later in the trial. Van Atta v. Schillinger, 191 M 472, 625 P2d 73, 38 St. Rep. 426 (1981).

Failure of Consideration Exception: Defendant's testimony that he did not receive $24,000 recited in a bill of sale given by him to plaintiff was not admissible under the failure of consideration exception to the Parol Evidence Rule because such recitation was more than the acknowledgement of payment of money consideration. It constituted the central element of the contract. Additionally, defendant was not attempting to compel payment but rather to escape the legal effect of the bill of sale. Kinjerski v. Lamey, 185 M 111, 604 P2d 782 (1979).

Lease Effective Upon FHA Approval: Parol evidence could be received to show that a lease agreement was intended to be effective only if the FHA approved a loan to the lessee, since this question went to the validity of the agreement itself. Platt v. Clark, 141 M 376, 378 P2d 235 (1963).

Offer to Build: Parol evidence was admissible to show that a contractor's letter estimating the cost of a building was not intended as an offer to build at that price, but rather that the parties intended a cost plus contract. Hammond v. Knievel, 141 M 433, 378 P2d 388 (1963).

Lease Agreement: Where, in an action to recover damages for breach of a contract of lease for failure of the lessee to gain possession, a defense of the lessor was that the contract was entered into with the express understanding that it should not become effective until and unless a tenant in possession would relinquish possession or could be ousted, parol testimony was admissible to show that what appeared to be a valid and binding contract was in reality not such, under the exception provided for in this section, that where the validity of the agreement is the fact in issue, such testimony may be admitted. Smith v. Fergus County, 98 M 377, 39 P2d 193 (1934), distinguished in Wilkerson v. School District, 216 M 203, 700 P2d 617, 42 St. Rep. 745 (1985), and followed in Thornton v. Songstad, 263 M 390, 868 P2d 633, 51 St. Rep. 104 (1994).

Object of Parties: The rule excluding parol testimony to contradict or vary a written instrument does not forbid inquiry into the object the parties had in executing, delivering, and receiving instruments made the basis of an action for breach of grain buying contracts, which defendant claimed were to be used merely as memoranda to complete plaintiff's office files and not to hold him personally liable for delivery of the grain. McCaull-Dinsmore Co. v. Stevens, 59 M 206, 194 P 213 (1921), distinguished in Hosch v. Howe, 92 M 405, 16 P2d 699 (1932).

Warehouse Receipts: Warehouse receipts for grain stored in an elevator issued under the provisions of the grain elevator law constituted binding contracts between the bailor and bailee which could not be varied or contradicted by parol testimony, the effect of which was to show that the transaction amounted to a sale and not a bailment. State ex rel. Broadwater Farms Co. v. Broadwater Elev. Co., 61 M 215, 201 P 687 (1921).

Consideration for Contract: Where there was nothing in a contract signed by a third party which showed a consideration affecting him or inducing him to become a party to it, or an intent on his part to be bound as surety for or joint promisor with one of the parties efficiently bound, parol evidence may not be resorted to for the purpose of furnishing the basis of an inference that he was or was not bound. Henry O. Shepard Co. v. Freeman, 40 M 144, 105 P 484 (1909).

CIRCUMSTANCES OF EXECUTION

Arbitration Provision in Adhesive Contract Enforceable — Noncompetition Clause Within Weaker Party's Reasonable Expectation: Larsen asserted that an employment contract containing a noncompetition clause was a contract of adhesion and that the arbitration clause in the contract was unenforceable. The Supreme Court applied the factors in Kloss v. Edward D. Jones & Co., 2002 MT 129, 310 M 123, 54 P3d 1 (2002), and determined that the contract was indeed adhesive. However, simply being adhesive does not render a contract invalid and unenforceable under Kloss. The contract must also either fall outside the weaker party's reasonable expectation or be unconscionable. In this case, Larsen had 20 years' experience in the insurance industry and had entered various similar employment agreements that contained arbitration clauses during those years, and the arbitration provision was stated in bold letters on the first page of the agreement. These facts constituted sufficient grounds to support the conclusion that the arbitration clause fell within Larsen's reasonable expectations and was therefore enforceable. However, once the District Court determined the validity of the arbitration clause, the court exceeded its authority in deciding additional substantive issues under the agreement that should have been decided by an arbitrator, so the case was remanded for arbitration. Larsen v. W. St. Ins. Agency, Inc., 2007 MT 270, 339 M 407, 170 P3d 956 (2007), following Martz v. Beneficial Mont., Inc., 2006 MT 94, 332 M 93, 135 P3d 790 (2006).

Evidence of Circumstances Under Which Instrument Made Admissible for Determining Ambiguity: As a general rule, evidence of the circumstances under which an instrument was made may not be considered when the language of the instrument is clear and certain in its terms. However, objective evidence of those circumstances, including the situation of the subject of the instrument and the parties to it, may be shown and considered to aid the court in determining, as a preliminary matter, whether the instrument contains an ambiguity. If the court determines that no ambiguity exists, then the extrinsic evidence may not be considered further, but if the court determines that an ambiguity is present in the instrument, then the extrinsic evidence may be introduced at trial to allow the trier of fact to determine the intent of the parties in entering into the contract. In the present case, both parties agreed that language in a right-of-way contract was unambiguous, so the trial court did not err in refusing to consider the circumstances under which the contract was made. Mary J. Baker Revocable Trust v. Cenex Harvest St., Cooperatives, Inc., 2007 MT 159, 338 M 41, 164 P3d 851 (2007). See 11 Williston on Contracts, 33:39 (4th Ed. 1999). See also Beebe v. Bd. of Directors of the Bridger Creek Subdivision Community Ass'n, 2015 MT 183, 379 Mont. 484, 352 P.3d 1094, holding that failure to identify ambiguity in an association's bylaws excluded consideration of extrinsic evidence.

Defaulting Buyer Under Unambiguous Written Contract Cannot Rely Upon Expectations Not Covered by Contract to Avoid Contract — Disposition of Downpayment Amounts Paid and Due — County Not Liable for Negligent Misrepresentation as to Recordability of Deeds and Seller's Title Insurer Not Liable for Loss in Marketability: Documents for the sale and purchase of two sections of land unambiguously showed, and it was undisputed, that the resale of 20-acre parcels by the buyer, the immediate acceptance by the county of 20-acre resale deeds of a type that would make subdivision review unnecessary, and the ability to resell without having to undergo subdivision review were not parts of the bargain. The parties knew that these things were contemplated, but the documents did not refer to them or make them a part of the contract. Before the contract was made, the county indicated that it would accept the 20-acre resale deeds. The deal fell through when the county changed its position after the contract was signed. The buyer failed to pay the whole downpayment, and the seller terminated the contract and kept the paid portion of the downpayment. Precontract discussions on the matter must be disregarded as parol evidence because the documents were unambiguous and did not refer to the matter. The buyer was not entitled to rescind the contract and have the paid portion of the downpayment returned based on mutual mistake or failure of consideration. There was no mutual mistake because the parties knew that it was not a certainty that the county would accept the deeds. There was no failure of consideration because the resale, county acceptance of the deeds, and avoidance of subdivision review were not part of the written contract. In addition, the need for a subdivision review would not make the land unmarketable; at most, its market value decreased and it would take longer to sell it. Furthermore, a party in default is not entitled to rescission. The seller was entitled to terminate the contract. The seller was also entitled to keep an amount of the paid portion of the downpayment equal to the amount by which the contract price for the land exceeded the market value of the land at the time of the breach. The seller was not entitled to keep the remainder of the paid portion of the downpayment or to a judgment for the unpaid portion of the downpayment because the contract did not provide for that remedy. The county was not liable in tort to the seller for negligent misrepresentation, and the buyer's title insurance company was not liable to the seller for the loss in the marketability of the land caused by the need for subdivision review. Yellowstone II Dev. Group, Inc. v. First Am. Title Ins. Co., 2001 MT 41, 304 M 223, 20 P3d 755

(2001), overruled in Mary J. Baker Revocable Trust v. Cenex Harvest St., Cooperatives, Inc., 2007 MT 159, 338 M 41, 164 P3d 851 (2007), to the extent that Yellowstone II held that the determination of whether a term in a contract is ambiguous is not a question involving parol evidence.

Contents of Safe Deposit Box Not Considered Jointly Held Asset: Silver directed his son to lease a safe deposit box for Silver's cash and signed a statement authorizing his son's access to the box. The lease form was prepared by a bank employee, who indicated that it was a joint agreement. Without Silver's direction, consent, or knowledge, the son subsequently removed the cash and placed it in his own safe deposit box in the same bank. Silver died 8 days later, and the personal representative sought to recover the cash, a substantial portion of which Silver had bequeathed to a charitable foundation. The District Court allowed the personal representative and a family friend to testify regarding statements that Silver made to them about the cash and its disposition. The court also admitted extrinsic evidence regarding the safe deposit box lease, holding that the fact that the lease form was prepared by a bank employee was relevant to interpretation of the document. The son alleged error on both issues, contending that the cash was a jointly held asset. The Supreme Court, citing Thompson v. Steinkamp, 120 M 475, 187 P2d 1018 (1947), and Anderson v. Baker, 196 M 494, 641 P2d 1035 (1982), found that the contested testimony put into context Silver's lease of the box and constituted evidence of Silver's intent to retain ownership of the cash. The fact that Silver did not select the form of lease or check the box on the lease form was supported by substantial credible evidence and was not clearly erroneous. Nevertheless, the son cited 70-1-308 for the contention that the cash was a jointly held asset. However, both the lease agreement and the statute provided for joint access to and possession of the safe deposit box and its contents, but not for joint ownership of the contents. Moreover, the language regarding the rights of surviving joint tenants did not apply here because Silver was still alive when the cash was removed. Thus, the District Court correctly concluded that the cash was not a jointly held asset by virtue of the agreement or the statute. The son could cite no contract theory under which he could be declared the owner of the cash, so the District Court did not err in applying gift theory rather than contract theory in determining ownership of the contents of the box or in concluding that the cash was not a gift to the son, based on the fact that Silver retained ownership. The District Court properly awarded the contents of the box to the estate. In re Estate of Silver, 2000 MT 127, 299 M 506, 1 P3d 358, 57 St. Rep. 526 (2000), distinguishing Malek v. Patten, 208 M 237, 678 P2d 201 (1984).

Loan of Title Based Upon Exchange of Deeds Upheld — Oral Extrinsic Evidence Controlling: Johnson agreed to loan Anderson the title to several lots that Johnson owned on Flathead Lake so that Anderson could mortgage the lots and use the proceeds for a business venture. Johnson and Anderson both executed deeds to the property, and Anderson occupied the property pursuant to a lease agreement. Later, the agreement was breached when Anderson conveyed his interest to a third party and cut trees from the property. Both parties sought a declaration of ownership in a quiet title action. The District Court admitted oral evidence showing that nothing more than a loan of title evidenced by an exchange of deeds was intended. The Supreme Court held that the timing of the execution and delivery of the two deeds was not controlling and that the deed conveying the property back to Johnson, even though it may have been signed and delivered first, was controlling in light of the circumstances of the transaction. The Supreme Court held that the deed conveying the property back to Johnson was valid as between the parties even though it was not recorded until later. Anderson v. Johnson, 264 M 66, 870 P2d 59, 51 St. Rep. 149 (1994).

Recovery on Written Instrument Absent Defense — Parol Evidence Not Allowed: Under Montana's Uniform Commercial Code, when signatures to an instrument are admitted or established, production of the instrument entitles the holder to recover on it unless the defendant establishes a defense. Parol evidence will not be allowed to contradict, alter, or vary a contract that has been reduced to a writing. Niemen v. Howell, 234 M 471, 764 P2d 854, 45 St. Rep. 2058 (1988).

Testimony on Contract Negotiations Disallowed: The distinction between waiver and parol evidence allowed to establish a variance from contract terms explained and justified a lower court decision to sustain plaintiff's objection to witness testimony regarding contract negotiations. Pipe Indus. Ins. Fund Trust v. Consol. Pipe Trades Trust, 233 M 162, 760 P2d 711, 45 St. Rep. 1392 (1988).

Letter Relating to Execution of Lease — Properly Accepted Parol Evidence: In reviewing the trial court's interpretation of the heating cost provisions of a 5-year lease, the Supreme Court held that a letter containing a payment schedule and testimony relating to the schedule was properly accepted parol testimony to explain circumstances surrounding the lease agreement.

The letter and testimony aided in resolving the ambiguity existing in the instrument as permitted by 28-2-905(2). The role of the judge is to construe an instrument according to its terms or its substance, not to insert or omit terms. The judge, however, may consider circumstances surrounding the execution, including the situation of the subject of the instrument and of the parties, to place himself in a position to interpret the language. In construing terms, evidence is admissible to show a local, technical, or otherwise peculiar signification used and understood by the parties. Martin v. Laurel Cable TV, Inc., 215 M 229, 696 P2d 454, 42 St. Rep. 314 (1985).

Construction of Terms of Agreement — Factual Issue Precluding Summary Judgment: A June 1976 agreement between the parties provided that plaintiff would advance money for the downpayment in the purchase of real property in Billings and would receive certain benefits, including a 50% interest in the property, in return. Plaintiff was to control any contractual arrangements until defendant had contributed, by payment of the monthly installments, a sum equal to the downpayment. In 1977, prior to the equalization of contributions, plaintiff entered negotiations to sell the property. No agreement between plaintiff and defendant was reached regarding the sale, and plaintiff filed suit seeking specific performance of the agreement. Plaintiff was granted summary judgment allowing him exclusive control of contract negotiations concerning the land for 1 year. Defendant contended on appeal that summary judgment was improper as there were factual controversies as to whether he had ever received an offer to sell the property and whether "control of any contractual arrangements" contemplated selling the property. Where, as here, the written agreement was imprecise and not artfully drawn, reference to extrinsic evidence indicating the intention of the parties would be proper, particularly since the same attorney represented both parties. Factual issues existed, and the case was remanded for trial on the merits. Downs v. Smyk, 200 M 334, 651 P2d 1238, 39 St. Rep. 1786 (1982).

Commodity Account Agreement: A stock brokerage firm explained to a customer the risk involved in a commodity straddle for tax deferral purposes and also had the customer sign a written agreement acknowledging the high degree of risk involved. Oral statements regarding the risk involved did not violate the parol evidence rule as they were evidence of the circumstances under which the written agreement was made. This evidence should be considered in determining whether to grant a motion for summary judgment. Brown v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 197 M 1, 640 P2d 453, 39 St. Rep. 305 (1982).

Savings Account Signature Card: A son was added as a joint tenant on his mother's savings accounts by signing the savings institution's signature card. The card contained language declaring one-half the deposit a gift to the joint tenant. The mother later brought an action against her son, asserting that she never intended to gift any portion of the accounts to her son but merely to allow him to withdraw money for her expenses if needed. The parol evidence rule was not an obstacle to the introduction of evidence extrinsic to the language on the signature card. Anderson v. Baker, 196 M 494, 641 P2d 1035, 39 St. Rep. 273 (1982).

Intent of Contracting Parties — Parol Evidence Admissible to Show Knowledge of Agent: In an action by the plaintiff contractor against the defendant motor carrier for breach of contract caused by the defendant's refusal to haul fabricated silo sections, the court did not err in finding that a memorandum of the agreement by the defendant's employee was sufficiently clear to form a valid contract. Parol evidence is admissible to apply the memorandum to the subject matter of the contract. The evidence showed that agents of the defendant knew the subject matter of the contract and that knowledge is imputed to the defendant and will be applied to the memorandum to determine the intent of the defendant as to the subject matter of the contract. Empire Steel Mfg. Co. v. Carlson, 191 M 189, 622 P2d 1016, 38 St. Rep. 101 (1981).

Waiver of Mechanics' Lien (Now Construction Lien): The circumstances of the parties to a transaction and their real purpose in executing instruments relating thereto is subject to interpretation and may be proved by parol testimony. Plaintiff retained lien rights for money owing to him despite his execution of a series of lien releases written in general terms when each release was executed upon the payment of an amount of money and uncontradicted parol testimony indicated that the parties regarded the lien waivers to be releases only as to amounts paid and not general releases of lien rights. Fillbach v. Inland Constr. Corp., 178 M 374, 584 P2d 1274 (1978).

Witness Testimony:

Under this section testimony of witnesses who were present at the time a contract of lease of oil lands was entered into, or just prior thereto, as to statements made by officers of the lessors in connection with conversations had with an officer of defendant with relation to offers received for drilling wells on the lands in question, was properly admissible in explanation of the circumstances under which the contract was made. Brown v. Homestake Exploration Co., 98 M 305, 39 P2d 168 (1934).

The parol testimony rule does not forbid an inquiry into the object of the parties in executing and receiving the instrument sued upon; while its language cannot be qualified or varied from its natural import, the circumstances under which it was entered into and the real intention of the parties may be shown by parol to prevent either of the parties to it from committing a fraud on the other by claiming it to be what it in fact is not. Bridges & Co. v. Bank of Fergus County, 77 M 524, 251 P 1057 (1926).

No Conflict of Terms: A conversation between buyer and seller had prior to the execution of a bill of sale, with the terms of which it was not in conflict, and which was material to show the circumstances under which the writing was executed, was admissible in evidence and not open to the objection that it varied the written agreement. Sutherland v. Green, 49 M 379, 142 P 636 (1914).

AMBIGUITY

Use of Extrinsic Evidence to Determine Scope of Servitude: The defendants disputed the plaintiff's right to a private road over their property that stemmed from an "access" easement. The District Court found in favor of the plaintiff, using extrinsic evidence to do so. The Supreme Court affirmed, stating that ambiguity in the plat description necessitated an examination of extrinsic evidence. Whitefish Congregation of Jehovah's Witnesses, Inc. v. Caltabiano, 2019 MT 228, 397 Mont. 284, 449 P.3d 812.

Port Authority Insured Under County Insurance Policy — Extrinsic Evidence Considered — Policy Construed Against Drafter — Insurer Not Immune From Suit as Reinsurer: After a port authority building was destroyed by a fire, the port claimed that it qualified as an insured under a county insurance company policy that included county members and any other county entities that receive insurance through a county joint insurance authority. The insurance company claimed that the language in the policy did not extend to county entities such as the port. Additionally, the insurance company claimed that it was a reinsurer and therefore it was improper for the port to bring a direct claim against it. The Supreme Court held that the port qualified as an insured under terms of the policy and that a direct claim was proper. In reaching a conclusion that was contrary to the language of the policy, the court gave meaning to the entire contract, considered extrinsic evidence, and construed ambiguous language in the policy against the insurer as the drafter. In determining that a direct claim was proper, the court reasoned that the port dealt directly with the insurance company, and therefore the insurer was an excess insurance carrier, rather than a reinsurer. Lincoln County Port Authority v. Allianz Global Risks US Ins. Co., 2013 MT 365, 373 Mont. 60, 315 P.3d 934.

Insurance Coverage for Intentional Dumping of Hazardous Waste Denied Under Policy Exclusion: For more than 3 years, defendant disposed of hazardous waste solvents into a sanitary landfill. The solvents migrated into the ground water, and neighbors sued defendant for personal injury and property damages. Defendant sought coverage from plaintiff insurer to remediate the damages and costs for the third-party suits, and the insurer eventually sought a declaration that it owed no duty to provide insurance coverage and defense costs for the environmental claims. Defendant's insurance policy contained a pollution exclusion that barred coverage for environmental damage unless the pollution was sudden or accidental. The District Court granted plaintiff summary judgment, and defendant appealed. The Supreme Court applied general rules of contract law, strictly construing the policy provisions in favor of defendant, but affirmed summary judgment absent ambiguity in the policy language. Under the policy, the initial disposal, rather than the migration and any resulting damages, had to be sudden and accidental in order to fall within the pollution exclusion clause. Defendant's routine intentional disposal of waste over a period of years could not be considered sudden or accidental, so defendant was unable to establish that the claims fell within the basic scope of coverage. Thus, plaintiff had no duty to defend defendant, and summary judgment for plaintiff was proper. Travelers Cas. & Sur. Co. v. Ribi Immunochem Research, Inc., 2005 MT 50, 326 M 174, 108 P3d 469 (2005). See also Bozeman v. AIU Ins. Co., 272 M 349, 900 P2d 929 (1995), and Makarka v. Great Am. Ins. Co, 14 P3d 964 (Alaska 2000).

Ambiguous Deeds of Conveyance — Intent of Parties Properly Considered: A dispute arose in a quiet title action based on subdivision surveys that differed from the original government survey. The District Court held that the property belonged to defendants, and the Supreme Court affirmed. Inconsistencies between the original plat and the location of the subdivision surveyor's monuments created an ambiguity. References to quarter section lines and quarter corners in the original survey were definite and ascertainable, and the subdivision surveyor's improperly placed monuments were considered false particulars frustrating the conveyance. The District Court properly applied Brown's Boundary Control and Legal Principles (4th Ed. 1995) to determine that the subdivision surveyor's monuments conflicted with the government's original monument and correctly considered the intent of the parties in interpreting the surveys and conveyances. Further, the original plat was part of the deeds of conveyance in defendants' chain of title, so the District Court correctly allowed the certificate of dedication into evidence. Olson v. Jude, 2003 MT 186, 316 M 438, 73 P3d 809 (2003).

Wendell Test Applied to Determination of Whether Bodily Injury Caused by Accident "Resulting From the Use" of Insured Vehicle: Defendant's son was injured in a hunting accident after riding to the hunt in a vehicle owned by Wajahuski and insured by plaintiff. The insurance policy provided for coverage resulting from the use of a vehicle. The District Court applied the test in Wendell v. St. Farm Mut. Auto. Ins. Co., 1999 MT 17, 293 M 140, 974 P2d 623 (1999), and held that the automobile insurance policy did not provide liability coverage with respect to defendant's claims for bodily injury. Defendant appealed. The Supreme Court affirmed. Even though the Wendell test was originally applied in an uninsured motorist case, the expansive, fact-intensive test also applied here. The phrase "resulting from the use" was ambiguous, so the contract terms were construed in a light most favorable to the insured or other beneficiary. The accident could have occurred in any location, regardless of how the hunters reached their destination. The fact that that particular vehicle was used to transport the hunters and assist in the hunt provided no connection between the use of the vehicle and the hunting accident. Thus, the District Court did not err in holding that the personal injuries were not caused by an accident resulting from the use of the insured motor vehicle. St. Farm Mut. Auto. Ins. Co. v. Ferrin, 2002 MT 196, 311 M 155, 54 P3d 21 (2002).

Ambiguity Regarding Whether Settlement Contingent on Alternate Financing — Summary Judgment Improper: Plaintiff sought to foreclose on a loan made to defendant, alleging that defendant's liabilities exceeded the value of the collateral, resulting in default pursuant to the terms of the note. The parties made several attempts to settle the issue, resulting in defendant's payoff to plaintiff, but in an amount that the plaintiff claimed was insufficient. The District Court granted summary judgment to plaintiff and ordered enforcement of the settlement agreement. However, a letter memorializing the settlement agreement, when considered with the parties' other correspondence, created an ambiguity regarding whether the settlement was contingent on alternate financing. Because there was more than one reasonable interpretation regarding the parties' intention, the parties' affidavits and testimony were admissible to determine intention and raised an issue of fact that precluded summary judgment. The case was remanded for further proceedings. Stockman Bank v. Potts, 2002 MT 178, 311 M 12, 52 P3d 920 (2002).

Modification of Nonexistent Contract Impossible — Minutes of Preconstruction Meeting Inadmissible Extrinsic Evidence Absent Ambiguity in Subsequent Contract: Keeney Construction (Keeney) subcontracted to perform certain construction work for James Talcott Construction Co., Inc. (Talcott). The subcontract stated that time was of the essence, but contained no specific date of completion, Rather, Keeney was to complete the work as directed by Talcott and on Talcott's completion schedule. Keeney asserted that the parties intended a 1996 completion date, but the project was not finished until 1997. Keeney sued for damages for delay and extra work, contending that extrinsic evidence in the form of minutes from a preconstruction meeting, held 2 days before the contract was finalized, would verify the parties' intent and represented an executed oral agreement that modified the written contract. The Supreme Court found no ambiguity in the written contract to warrant further examination of the intent of the parties. Because the intent of the contract was clear, the extrinsic evidence was inadmissible to support the contention that a specific completion date was intended. Keeney could not assert a claim for damages based on Talcott's direction of the timing of the completion of the project when the contract authorized Talcott to do so. Further, because an oral agreement cannot modify a contract that does not yet exist, the meeting and conversations held prior to the contract signing could not be interpreted as a modification of the subsequent written contract. Keeney Constr. v. James Talcott Constr. Co., Inc., 2002 MT 69, 309 M 226, 45 P3d 19 (2002).

Interpretation of Latent Ambiguity in Marital Property Settlement Agreement — Wife Entitled to Value of Improvements to Real Property Made Between Time of Dissolution and Time of Sale: A property settlement agreement provided that the wife would receive the family home subject to the debt owed upon it (although no debt was owing) and that when she sold it, she would return one-half of the proceeds of the sale of the house to the husband. The wife's subsequent improvements to the home increased its value from $55,500 at the time of dissolution to $75,000 at the time of sale. The wife requested an interpretation of the settlement agreement to address the division of proceeds in light of her substantial improvements to the property, as well as her payment of all property taxes since the date of dissolution. The District Court concluded that the property settlement agreement created a latent ambiguity by failing to address what would happen to the expenditures of one party that were for neither maintenance nor repairs. The court concluded that the agreement contemplated that the wife would maintain the value of the home at the time of dissolution and divide that value when the house was sold and that the property taxes were an item of maintenance that the wife was responsible for pursuant to the agreement. The Supreme Court affirmed. In light of the latent ambiguity in the agreement, the District Court did not introduce an additional provision to the agreement that deprived the husband of his contractual rights, but merely interpreted the agreement to clarify what was meant by "one-half of the proceeds of the sale of the house" in the context of nonmaintenance expenditures. Upon finding a latent ambiguity, the District Court properly admitted parol evidence to interpret the agreement and correctly allowed the wife to retain the proceeds from the sale of the house attributable to her expenditures for improvements beyond maintenance and repairs. In re Marriage of Holloway, 2000 MT 104, 299 M 291, 999 P2d 980, 57 St. Rep. 418 (2000).

"Arising Out of" Ambiguous — Coverage for Liability Not Excluded: Pablos were injured in a vehicle accident involving Moore, who was transporting a landscaping tractor for his employer. The employer was covered by a commercial general liability insurance policy that provided liability insurance for negligent acts of the corporation and its employees. Pablos contended that the employer was negligent in the hiring, training, and supervision of Moore. The employer conceded that the claim arose during the policy period and fell within the definitions of "bodily injury" and "occurrence" and that the policy would provide coverage unless coverage was denied by an exclusion but contended that coverage was excluded under both the exclusion for damages "arising out of" the use of an automobile and the exclusion for damages "arising out of" the transportation of mobile equipment. The District Court held that the term "arising out of" was ambiguous and, construing the instrument against the drafter-insurer, ruled that coverage for Pablos' accident was not excluded under the policy language. Noting that the phrase "arising out of" has been declared ambiguous in another insurance context in Wendell v. St. Farm Mut. Auto. Ins. Co., 1999 MT 17, 293 M 140, 974 P2d 623 (1999), the Supreme Court applied a similar rationale to the phrase in both exclusionary clauses at issue in the present case. The phrase was reasonably subject to more than one interpretation and thus ambiguous. Pursuant to Head v. Cent. Reserve Life of N. America Ins. Co., 256 M 188, 845 P2d 735, 50 St. Rep. 20 (1993), if the terms of an insurance policy are ambiguous, obscure, or open to different constructions, the construction most favorable to the insured or other beneficiary must prevail, particularly if an ambiguous provision attempts to exclude the liability of the insurer. Here, the policy did not clearly and unambiguously exclude coverage for the theories of liability pleaded by Pablos, and the District Court's summary judgment that coverage was owed on Pablos' claims for negligent hiring, training, and supervision of Moore was affirmed. Pablo v. Moore, 2000 MT 48, 298 M 393, 995 P2d 460, 57 St. Rep. 231 (2000), following Marquis v. St. Farm Fire & Cas. Co., 961 P2d 1213 (Kans. 1998).

Parol Evidence of Circumstances Under Which Bid Prepared Proper in Interpreting Uncertain Contract Provisions: Bid estimates on a road building project contained vague and ambiguous project requirements, and testimony at trial regarding the height of the finished road was conflicting. Thus, the District Court, in interpreting provisions of the contract that appeared ambiguous or uncertain, properly considered parol evidence of the circumstances under which the bid was prepared. The court found more credible the contractor's testimony that there was not agreement that a subroad would be constructed of pit run gravel 6 inches above field grade, and that determination was affirmed on appeal. DeNiro v. Gasvoda, 1999 MT 129, 294 M 478, 982 P2d 1002, 56 St. Rep. 521 (1999).

Extrinsic Evidence on Testamentary Intent Raising Genuine Issue of Material Fact — Summary Judgment Improper: Kuralt gifted Shannon with 20 acres along the Big Hole River, disguising the transaction as a sale. Shortly before he died, he sent Shannon a letter, which constituted a holographic will, suggesting that he intended to do the same with another 90 acres. The District Court allowed introduction of the letter as extrinsic evidence regarding testamentary intent, then granted summary judgment to the estate after finding that the letter contemplated a separate testamentary instrument not yet in existence to accomplish the transfer of the Montana property. Nevertheless, the letter raised a fundamental disagreement as to a genuine material fact—namely, whether Kuralt intended that the letter effect a posthumous disposition of the property. Regardless of whether the court admitted the evidence because it considered the letter ambiguous or because it agreed with Shannon that extrinsic evidence may be discretionarily admitted in holographic will disputes, the court nevertheless improperly resolved contested issues by granting summary judgment. The Supreme Court reversed and remanded the case for trial. In re Estate of Kuralt, 1999 MT 111, 294 M 354, 981 P2d 771, 56 St. Rep. 460 (1999).

Ambiguity of Draft Purporting to Be Release That Is Also Receipt — Summary Judgment Improper: The District Court improperly granted summary judgment for an insurance company after finding plaintiff had signed a release from suit. The Supreme Court found a contractual ambiguity existed because the release language was contained in a $1,500 draft that purported to be a release but was also a receipt in certain situations. The District Court adopted verbatim the proposed findings and conclusions presented by the insurer, which put it in the position of a trier of factual issues rather than determining whether genuine issues of material fact existed on the motion for summary judgment. Existence of ambiguity precluded summary judgment. Buskirk v. Nelson, 237 M 455, 774 P2d 398, 46 St. Rep. 964 (1989).

Commission as Evidence of Fiduciary Relationship — Rescission by Principal: The District Court did not err in relying on the explicit definition of the word "commission" in finding that a real estate agent who was granted a commission for the sale of a resort while intending to be one of the ultimate purchasers was acting in a fiduciary capacity in his relationship with the principal. Because the relationship existed, the sales agreement was voidable and subject to rescission by the principal. Boyne, U.S.A., Inc. v. Mallas, 236 M 305, 769 P2d 1235, 46 St. Rep. 380 (1989).

Contracts — Sufficient Ambiguity as Question of Law: In the interpretation of contracts, it is a question of law whether there is an ambiguity sufficient to submit the issue to a jury. Monte Vista Co. v. The Anaconda Co., 231 M 522, 755 P2d 1358, 45 St. Rep. 809 (1988), citing Nordlund v. School District, 227 M 402, 738 P2d 1299, 44 St. Rep. 1183 (1987), and followed in Audit Serv., Inc. v. Systad, 252 M 62, 826 P2d 549, 49 St. Rep. 137 (1992), Doble v. Bernhard, 1998 MT 124, 289 M 80, 959 P2d 488, 55 St. Rep. 489 (1998), and, with regard to admissibility of parol evidence in determining the intent of the parties when ambiguities exist in a contract, Molerway Freight Lines, Inc. v. Rite-Line Transp. Serv., Inc., 273 M 95, 902 P2d 9, 52 St. Rep. 839 (1995). See also Johnson v. Nyhart, 269 M 379, 889 P2d 1170, 52 St. Rep. 37 (1995), and Rich v. Ellingson, 2007 MT 346, 340 M 285, 174 P3d 491 (2007).

No Ambiguity in Oil Drilling Contract — Personal Liability When Escrow Unfunded: Defendant corporation was to ensure that a drilling company was paid either by funding an escrow or by making the payments itself. Defendant contended that contract provisions created an ambiguity by requiring the "operator" and the third-party escrow company to make required payments. The Supreme Court noted that: (1) the contract did not state that the corporation's payment was conditioned on escrow being set up; and (2) even if the escrow provision was a condition precedent waived by the drilling company, such waiver did not release the corporation from its payment obligation. The escrow provision was waived when adequate funds were not deposited. The remaining provision specifically stated the corporation's liability to pay, and failure to do so was breach of contract. Drilcon, Inc. v. Roil Energy Corp., Inc., 230 M 166, 749 P2d 1058, 45 St. Rep. 114 (1988).

Ambiguous Language Regarding Conduct of Mineral Development Operations: An agreement implementing development of a mineral interest indicated that the parties would operate the venture as joint operators, but it was ambiguous as to who would conduct the day-to-day operations of the property, seemingly implying that daily operations would be conducted by the oil company. Evidence indicated that lessor worked as an employee in the operations, so the District Court properly granted the company authority to conduct daily operations subject to a right of inspection by the lessor. Somont Oil Co., Inc. v. Nutter, 228 M 467, 743 P2d 1016, 44 St. Rep. 1685 (1987).

Parol Evidence Necessary to Determine Intention When Latent Ambiguity Exists: A party transferred property back to sellers in lieu of foreclosure. The transfer arguably constituted a technical conveyance. "Conveyance" had different meanings for the parties and therefore was to be interpreted in accord with the manifest intent of the parties. Parol evidence was necessarily admissible to demonstrate and explain this latent ambiguity, and summary judgment on the issue was improper. Ellingson Agency, Inc. v. Baltrusch, 228 M 360, 742 P2d 1009, 44 St. Rep. 1598 (1987), followed in Fox Grain & Cattle Co. v. Maxwell, 267 M 528, 885 P2d 432, 51 St. Rep. 1136 (1994).

Construction of "Cash and Savings" Clause in Will and Subsequent Agreement — Parol Evidence Admissible: In broadly construing a clause in a will leaving "cash and savings" to the wife and when the clause was also used in a subsequent agreement wherein the parties more clearly delineated the division of property, the trial court properly granted to the wife a promissory note, a diamond ring, partnership interests, and corporate shares. A residuary clause bequeathing to a brother the remainder of the estate, "including but not limited to my ranch and any livestock and machinery", properly included all personal property and assets connected with the ranch, including patronage and capital credits in electric, telephone, and farming cooperatives. The "cash and savings" clause as used in the subsequent agreement did not alter the will and was properly construed in the context of the will. Further, it was not error for the lower court to admit parol evidence relative to the parties' intent as to the agreement in interpreting ambiguous language in the agreement. In re Estate of Flasted, 228 M 85, 741 P2d 750, 44 St. Rep. 1362 (1987).

Ambiguity in Reservation — Summary Judgment Improper: In a 1944 deed, the grantor reserved "six percent of all royalties received for oil and gas removed from the above-described property". In 1968, the mineral owners leased the property subject to a one-eighth landowner's royalty (12½% of oil and gas produced). In a subsequent suit, the royalty owners claimed they were entitled to 6% of production and the mineral owners claimed that the royalty owners were entitled to 6% of the landowner's royalty of 12½% of production. The District Court granted summary judgment for the mineral owners. The Supreme Court reversed on the grounds that the reservation language is ambiguous and the true intent of the parties is discernible only with reference to extrinsic evidence, not from the deed alone; therefore, summary judgment was inappropriate. Proctor v. Werk, 220 M 246, 714 P2d 171, 43 St. Rep. 333 (1986).

Ambiguous Assignment — Construction of Document as a Whole: Peterson sold property to the Blairs under a contract for deed that reserved one-half the mineral rights in Peterson. Peterson then assigned her rights under the contract to Hopkins. The Blairs paid Hopkins and recorded. Peterson sued Hopkins to quiet title when the lessee of Peterson's one-half mineral rights claimed Peterson had assigned them to Hopkins by mistake. Hopkins was granted summary judgment because the assignment conveyed all of Peterson's right, title, and interest in the property, together with the contract for deed. The judgment was reversed, and judgment was granted Peterson. The assignment stated that it was subject to the contract for deed, thus creating an ambiguity. Taken as a whole, it appeared that the assignment was of the contract for deed and was not itself a deed of the entire surface and mineral interests to Hopkins. This was supported by the conduct of the parties, for Peterson leased her reserved interest for the 22 years following the assignment until lessee raised the alleged mistake, and at no time up to his death in the 17th year of the 22 years did Hopkins claim all the mineral rights or demand Peterson's one-half interest. Peterson v. Hopkins, 210 M 429, 684 P2d 1061, 41 St. Rep. 1140 (1984).

Ambiguous Assignment — Explanatory Evidence Admissible: A contract for deed reserved one-half the mineral rights in seller. Seller's subsequent assignment was ambiguous where it assigned all of seller's right, title, and interest in the property, together with the contract for deed, yet also stated that it was subject to the contract for deed. Therefore, the evidence was admissible to explain the ambiguity and the intent of seller and assignee of seller's rights under the contract for deed. Peterson v. Hopkins, 210 M 429, 684 P2d 1061, 41 St. Rep. 1140 (1984).

Commission Agreement Found Unambiguous — Use of Extrinsic Evidence to Prove Lack of Ambiguity Upheld: Where the defendant seller of real estate made a commission agreement with the plaintiff providing for payment of the commission out of the receipts from the contract for deed, the District Court did not err in holding that money received by the defendant under a modification of the contract for deed could not be used to calculate the amount of commission owed to the plaintiff. The terms of the commission contract were not ambiguous and show that it was the intent of the parties to count only that money received under the original agreement. The District Court properly looked to the terms of the contract for deed only to determine whether an ambiguity existed in the commission agreement, and having determined there was none, properly excluded other evidence of the parties' intent in making the commission agreement. Martin v. Community Gas & Oil Co., 205 M 394, 668 P2d 243, 40 St. Rep. 1385 (1983).

Ambiguity in Reservation — Course of Conduct: Plaintiffs initiated an action to determine their rights under a reservation in an assignment of an oil and gas lease. The 1926 lease assigned reserved the right to take and use gas "for the purpose of extracting, making, or manufacturing casing-head gasoline or by-products or carbon black". The course of conduct and expert testimony both showed that the language was meant to be nonrestrictive. Souders v. Mont. Power Co., 203 M 483, 662 P2d 289, 40 St. Rep. 583 (1983).

Ambiguous "Cost-Plus" and Ceiling Price Language in Building Contract — Parol Evidence Properly Admitted: Plaintiff agreed to build a house for defendants. The contract entered into contained "cost-plus" language as well as ceiling price language. Costs were more than anticipated.

Defendants ordered plaintiff to stop working on the house. Defendants paid the ceiling price referred to in the contract, which left plaintiff with no profit. Plaintiff filed a mechanics' lien (now construction lien) on the property. A trial was held, with the judge finding for defendants. Plaintiff contended it was error to admit parol evidence to modify the contract. The Supreme Court found that the admission of parol evidence was proper due to the ambiguity of the contract. The question was then a factual one for the District Court. There was substantial evidence to support the finding of the ceiling price. Matos v. Rohrer, 203 M 162, 661 P2d 443, 40 St. Rep. 366 (1983), distinguished in Lewistown Miller Constr. Co., Inc. v. Martin, 2011 MT 325, 363 Mont. 208, 271 P.3d 48.

Termination of Lease — Removal of Holdover Tenant — Agricultural Exception to Landlord-Tenant: Defendant sold plaintiff her property. The instrument contained a lease back to defendant of the buildings and 6 acres. Plaintiff gave notice that the lease was to terminate. Defendant refused to vacate. Plaintiff brought an action under the unlawful detainer statutes which provide for an award of treble damages. Defendant contended the dispute was governed by the Montana Residential Landlord and Tenant Act of 1977. Plaintiff contended the lease was within the "agricultural" exclusion contained in 70-24-104(8). The lease provisions gave no indication of the nature of the buildings or of the intended use of the 6 acres. The trial court allowed the introduction of photographs and oral testimony regarding the lease, which established that the use of the land was for maintenance of defendant's livestock. The trial court properly allowed parol evidence to resolve an ambiguity in the lease. The Supreme Court determined that the legislative intent of 70-24-104 was for a comprehensive coverage of all agricultural operations, whether they are large-scale operations for profit or small-scale operations secondary to the use of the residence. The unlawful detainer provisions were properly applied. Dussault v. Hjelm, 192 M 282, 627 P2d 1237, 38 St. Rep. 738 (1981).

Conveyances in Mineral Deed: No ambiguity existed between clause conveying one-half of the minerals in 1,040 acres and the conveyance of 520 mineral acres, so that mineral deed could not be varied by parol evidence. Superior Oil Co. v. Vanderhoof, 297 F. Supp. 1086 (D.C. Mont. 1969).

Court to Determine Intent: In action for specific performance arising over interpretation of contract for conveyance of land reserving mineral interest, where cross-complaint of defendants alleged that the contract was ambiguous and uncertain and prayed for a declaratory judgment to adjudicate the rights of the parties, it was the duty of the trial court to determine the intent of the parties, and the exclusion of parol evidence of intent was error. Stokes v. Tutvet, 134 M 250, 328 P2d 1096 (1958).

When Language Needs Interpretation: If the language of a contract is clear it needs no interpretation, and the intention of the parties in entering into it must be ascertained from the writing alone. New Home Sewing Mach. Co. v. Songer, 91 M 127, 7 P2d 238 (1931).

Commission Sales Agreement: Where an agreement to furnish automobiles to be sold on commission did not furnish its own interpretation, parol evidence was properly admitted to determine the intention of the parties. Brockway v. Blair, 53 M 531, 165 P 455 (1917).

FRAUD

Summary Judgment on Fraud Claim Improper Given Genuine Issue of Material Fact: In order to purchase a condominium in downtown Bozeman, the plaintiff arranged bank financing. She requested a traditional 30-year loan and the bank provided her a truth in lending statement and a good faith estimate for a 30-year mortgage. At closing, and unbeknownst to her or her realtor, she signed documents for a loan with an 18-month finance term and a balloon payment instead. She claimed to have learned of the change in term only a couple of weeks before the balloon payment was due and, because the property was zoned as commercial, was unable to obtain long-term financing and was forced to sell it. She sued the bank for fraud for changing the term of the loan without informing her. The District Court granted the bank summary judgment, ruling that the plaintiff had not stated facts to support each of the nine elements of fraud. On appeal, the Supreme Court reversed summary judgment, based on its conclusion that the facts as presented by the plaintiff established a genuine issue of material fact, and remanded the matter to the District Court. McCulley v. Amer. Land Title Co., 2013 MT 89, 369 Mont. 433, 300 P.3d 679.

Representations in Negotiations:

The Graveleys argued that during negotiations for a loan, the Farm Credit Bank assured them that there was enough equity in the two properties that they were seeking to buy to secure the loan and that they did not have to worry that the home ranch would be subject to foreclosure if the loan failed. In a foreclosure action, the bank sought a summary judgment that would also allow it to foreclose on the home ranch for any deficiency judgment existing after the sale of the secured property for which the loan had been made. The Supreme Court held that the lower court had correctly denied the motion on the basis that the Graveleys' defense of equitable estoppel raised questions of fact. State ex rel. Farm Credit Bank of Spokane v. District Court, 267 M 1, 881 P2d 594, 51 St. Rep. 709 (1994).

In an action by the seller against the buyer for the purchase price of a hotel, the buyer should be permitted to present evidence that: (1) he was given false information by the seller's agent in response to inquiries made upon buyer's inspection of the property; and (2) that he was prevented by the seller from further inspection of the premises. Jenkins v. Hillard, 199 M 1, 647 P2d 354, 39 St. Rep. 1156 (1982).

Where a contract is sought to be avoided on the ground that the party bound was induced to enter into it by his opponent's fraudulent representations, the latter is not in a position to invoke the rule that a contract in writing may not be varied by parol testimony to prevent the former from testifying to such representations made during preliminary negotiations. Advance-Rumely Thresher Co. v. Wenholz, 80 M 82, 258 P 1085 (1927).

Court Review of Claim of Fraud Inducing Arbitration Clause Not Fraud Inducing Entry Into Contract Allowed Under Federal Arbitration Act: The appellant alleged that fraud had induced him to enter into an option agreement and margin contract with the respondents. The appellant further stated that he had not read the arbitration clause or the clause that exposed him to unlimited losses. The Supreme Court ruled that since the appellant only alleged fraud in the inducement and did not specifically allege that he had been induced to agree to the arbitration clause, the entire matter, including fraud in the inducement, was subject to arbitration under the Uniform Arbitration Act (Title 27, ch. 5). Larsen v. Opie, 237 M 108, 771 P2d 977, 46 St. Rep. 660 (1989).

Parol Evidence Inadmissible to Show Sham or Fraud: Plaintiff and defendant were in the business of developing oil and gas property. Defendant executed a promissory note in favor of plaintiff and gave plaintiff a "letter agreement" supplementing and clarifying the note. In plaintiff's action on the note, defendant attempted to introduce evidence of a contrary oral agreement that the note was a sham intended to induce third parties to give plaintiff investment funds and that it was never intended that the note be paid. The parol evidence rule prevented introduction of the evidence. In addition, defendant was not entitled to relief under the rule that delivery of an instrument for a special purpose is a defense against one not a holder of the instrument in due course. The sham claim in this case does not constitute a special purpose. Perez-Lizano v. Ayers, 215 M 95, 695 P2d 467, 42 St. Rep. 208 (1985).

Parol Evidence Rule — Constructive Fraud as Within the Exception: Defendant represented plaintiff in a civil action in federal court. The parties agreed that the case was originally handled on a 50% contingency fee basis. The case lasted almost 10 years. Plaintiff signed a formal authorization for defendant to settle. At the time of settlement, plaintiff contended the parties agreed to replace their 50% of net fee agreement with a percentage distribution of the gross settlement amount. At some point in time, the parties signed an agreement in defendant's handwriting providing for a 75%-25% split of the settlement. The agreement contained a clause stating the agreed sums had been paid in full. Plaintiff contended defendant had retained half the settlement. Defendant contended that the trial court erred in permitting plaintiff to testify concerning the agreement. On appeal, the Supreme Court held that the fraud exception to the parol evidence rule addresses both actual and constructive fraud. The court stated that constructive fraud often exists where the parties to a transaction have a special confidential or fiduciary relation which affords the power and means to one to take undue advantage of or exercise undue influence over the other. The attorney-client relationship is a fiduciary one. Evidence presented along with plaintiff's testimony established constructive fraud on defendant's part. The court held that plaintiff's claim of conduct against defendant, which constituted at least constructive fraud, fell within the ambit of the fraud exception of the parol evidence rule. Eaton v. Morse, 212 M 233, 687 P2d 1004, 41 St. Rep. 1708 (1984).

Independent Investigation Clause Not to Preclude Justifiable Reliance on Representations: Defendants owned property in Flathead County. Water for the property came from a neighbor's well for which they paid him $8 per month. No written agreement existed concerning the water supply. Defendants listed the property for sale with Tri-City Real Estate. Inserted in the listing contract in the printed space following "water" were the words "community $8/mo." Plaintiffs were interested in the land and looked at it. They asked both defendants and the realtor about the water supply and were told it came from a community well. Plaintiffs wanted written verification of the interest in the water system. The realtor told them he would obtain a copy of the register of the well for them. Plaintiffs continued asking for the register but never received it. Plaintiffs signed a contract for deed to buy the property which had been prepared by the realtor's attorney. The contract contained an "independent investigation" clause, which stated that plaintiffs had investigated the property and entered the contract based upon that investigation and that there were no other agreements or representations concerning the property. The neighbor stopped supplying water, and plaintiffs were forced to dig their own well. They sought recovery from defendants. It was held that defendants were responsible for the negligence of their agents in the sale as related to the community water interest. The Supreme Court held that the "independent investigation" clause did not preclude a holding that the plaintiffs justifiably relied on the representations of the realtor. Parkhill v. Fuselier, 194 M 415, 632 P2d 1132, 38 St. Rep. 1424 (1981), distinguished in Garrison v. Averill, 282 M 508, 938 P2d 702, 54 St. Rep. 454 (1997).

Fraud — Circumstances Leading to Contract: Letters from defendant to plaintiff relating to circumstances leading up to the execution of a promissory note for the purchase of property on a contract are admissible to establish fraud. It is an exception to the parol evidence rule. Flemmer v. Ming, 190 M 403, 621 P2d 1038, 37 St. Rep. 1916 (1980).

Fraud Exceptions: Defendant, who gave a bill of sale to plaintiff for 80 cows, was allowed to testify over a parol evidence objection that his own bill of sale was a sham and a means for providing plaintiff increased borrowing power under Higby v. Hooper, 124 M 331, 221 P2d 1043 (1950), this testimony is not admissible under the fraud exception. Kinjerski v. Lamey, 185 M 111, 604 P2d 782 (1979).

Parol Evidence to Show Fraud or Resolve Ambiguity: Parol evidence is admissible to resolve ambiguities and to determine whether the buyers were fraudulently induced into entering a written contract where seller made express warranties that application for SID had been made when he knew that an application had not been made. Dodds v. Gibson Prod. Co., 181 M 373, 593 P2d 1022 (1979).

Renewal Note: In an action by the payees against the makers for the balance due on a renewal note, where there was fraud and partial failure of consideration and one of the makers testified that he did not know how to figure interest, the makers were not precluded from showing that the contract was different from what the writing showed it to be. Jensen v. Franklin, 135 M 341, 340 P2d 832 (1959).

Illiteracy of Party: Generally in the absence of fraud or mistake where the terms of the contract have been reduced to writing by the parties it must be considered as containing all the terms of the agreement and parol evidence cannot be resorted to, to alter the written contract and usually plaintiff's inability to read does not alter the rule. Ikovich v. Silver Bow Motor Car Co., 117 M 268, 157 P2d 785 (1945).

Conditional Contract: In the absence of fraud, an unconditional written contract of purchase of building material presumably embraced the whole agreement of the parties, and therefore evidence of an oral understanding to the effect that it should not become binding until the architect in charge had approved the materials was inadmissible. Wheeler v. James, 70 M 37, 223 P 900 (1924).

Inducement for Agreement: Where plaintiff alleged mistake and fraud, and the evidence disclosed that the inducement held out to plaintiff to sign an agreement was based on fraudulent representations of defendants that a lease need not be mentioned in a contract of sale of a business and the lease, the evidence was admissible to show the purchase of the lease and defendant's fraudulent conduct, over objection that it varied the contract. Sathre v. Rolfe, 31 M 85, 77 P 431 (1904).

MISCELLANEOUS

Surrogacy Contract — Express Written Contract Limited to Clear and Unambiguous Terms — Contract Did Not Preclude Subsequent Establishment of Parental Interest Under Montana Law Not Based on Fact of Surrogacy. Sayler v. Yan Sun, 2023 MT 175, 413 Mont. 303, 536 P.3d 399.

Genuine Issue of Material Fact Whether Dam Operation Damaged Lakeshore Properties — Summary Judgment Improper — Class Action Vacated: Flathead Lake landowners brought a class action suit against defendant operators of Kerr Dam for operating outside the scope of their easements in a manner that continuously eroded and damaged plaintiffs' lakeshore properties. The District Court rejected plaintiffs' argument that the dam operator was not allowed to affect plaintiffs' properties above an elevation of 2,893 feet, concluding instead that defendants' easements covered entire parcels. The court concluded that erosion, including wave action erosion, was within the scope of the easements and held that any duty defendants had to not cause unreasonable damage to plaintiffs' properties applied only to damage unrelated to use of the easement. Therefore, summary judgment was granted to defendants, and plaintiffs appealed. The Supreme Court first agreed that the District Court's contour line theory was correct. The "2,893 feet" clause did not establish the vertical limit argued by plaintiffs because although the dam operators' right to flood, subirrigate, drain, or otherwise affect the shoreline was not unlimited, it was not restricted to a maximum elevation of 2,893 feet at each parcel, but rather extended to whatever part of each parcel was affected when the lake was held at 2,893 feet above mean sea level as measured at the dam. The court also agreed that the right to cause some erosion was necessary to the enjoyment of the right to perpetually flood, subirrigate, and drain and was thus included by implication in the easements. However, further factual development and trial were necessary to address the question of whether the erosion was reasonable, necessary, and within the scope of the easements, which could not be resolved by summary judgment. Additionally, the question of whether defendants breached their obligation to not cause unreasonable damage to the shoreline properties and to not unreasonably interfere with plaintiffs' enjoyment also required further factual development and possibly trial. Therefore, the order certifying the case as a class action was vacated and the case was remanded for further consideration. Mattson v. Mont. Power Co., 2009 MT 286, 352 M 212, 215 P3d 675 (2009).

On remand, the District Court decertified the class as to one defendant and denied the plaintiffs' motion for certification as to another defendant on the basis that the question of whether the erosion caused unreasonable damage to or unreasonably interfered with the plaintiffs' properties required an individual, property-by-property analysis that was improper for class certification. On appeal, the Supreme Court reversed, concluding that class certification to both defendants was proper because the reasonableness of the erosion presents a common question that is incapable of being resolved on a property-by-property basis since an aggregate of the benefits and burdens imposed on all of the shoreline properties must be considered together to determine reasonableness. Mattson v. Mont. Power Co., 2012 MT 318, 368 Mont. 1, 291 P.3d 1209.

Conscionability Analysis of Contractual Liquidated Damages Clause — Liquidated Damages Clause Presumed Enforceable: To provide direction to contracting parties and resolve the disparities in case law regarding liquidated damages, the Supreme Court adopted a rule to analyze liquidated damages clauses from the perspective of whether or not the clause is unconscionable as indicated by the nature of the bargaining process between the parties. Unconscionability involves a two-pronged determination regarding whether: (1) the clause fits the doctrine of contract of adhesion such that the weaker party had no meaningful choice regarding acceptance of the contract provisions; and (2) the contractual terms are unreasonably favorable to the drafter, which is usually the party with superior bargaining power. Whether the clause is unreasonably favorable to the drafter in turn involves an inquiry into whether the clause is within the reasonable expectations of or unduly oppressive to the weaker party. Liquidated damages clauses are presumed enforceable, and the party seeking to avoid the clause has the burden of proving unconscionability. Unless there are underlying disputed issues of fact, the question of unconscionability is purely a matter of law for the court to decide. Arrowhead School District No. 75 v. Klyap, 2003 MT 294, 318 M 103, 79 P3d 250 (2003), overruling Daugherty Cattle Co. v. Gen. Constr. Co., 254 M 479, 839 P2d 562 (1992), to the extent that it prevented one party from introducing relevant evidence by granting summary judgment based on contract language alone, overruling Story v. Bozeman, 259 M 207, 856 P2d 202 (1993), to the extent that it placed the burden on the nonbreaching party to prove the enforceability of a liquidated damages clause, and followed in Am. Music Co. v. Higbee, 2004 MT 349, 324 M 348, 103 P3d 518 (2004), and in Highway Specialties, Inc. v. Mont. Dept. of Transportation, 2009 MT 253, 351 M 527, 215 P3d 667 (2009).

Presumption That Services Provided by Relative Rendered Gratuitously — Compensation for Personal Care Services Provided by Decedent's Daughters Properly Denied: Following their father's death, three daughters presented a claim against the estate for personal care services that they provided to their father. Their claims were disallowed, and the daughters appealed. The Supreme Court affirmed. Generally, when services are provided to one person by another and the services are knowingly and voluntarily accepted, the law presumes that the services were provided in expectation of payment. However, a generally acknowledged exception applies when a relative seeks payment for services, and the presumption in those cases is that the services were rendered gratuitously unless there was an express agreement for payment or unless such an agreement can be inferred. In this case, the decedent determined prior to death how he wished his assets to be distributed and, despite several opportunities to do so, made no provision for compensation for the personal services that his daughters provided. The daughters were unable to rebut the general presumption of gratuity, and the Supreme Court declined to disturb the

District Court's denial of their claims for services. In re Estate of Orr, 2002 MT 325, 313 M 179, 60 P3d 962 (2002). See also San Antonio v. Spencer, 82 M 9, 264 P 944 (1928), Ziegler v. Kramer, 175 M 236, 573 P2d 644 (1978), Donnes v. Orlando, 221 M 356, 720 P2d 233 (1986), and Neumann v. Rogstad, 232 M 24, 757 P2d 761 (1988).

Application of Parol Evidence Rule to Stranger to Contract — Stranger to Contract Exception Clarified: Habets bought a 7-mile stretch of buried pipeline from Cenex and, upon attempting to recover the pipeline from the ground pursuant to the contract of sale, was refused access to part of the pipeline by the Swansons, who claimed that they had previously purchased a section of the same pipeline from Cenex. Habets brought an action against the Swansons for access to the pipeline, and the Swansons sought to introduce extrinsic parol evidence to show that under their contract with Cenex, which did not show the purchase of the segment of the pipeline in question, they had in fact purchased the segment of the pipeline in question. The District Court excluded the extrinsic parol evidence because of the parol evidence rule, and the Supreme Court affirmed the exclusion of that evidence. The Supreme Court examined the "stranger exception" to the parol evidence rule, which seemed to indicate that extrinsic parol evidence could be introduced by a person not a party to the contract to vary the terms of the contract. The Supreme Court distinguished its previous opinions in Read v. Lewis & Clark County, 55 M 412, 178 P 177 (1919), Greening v. Gazette Printing Co., 108 M 158, 88 P2d 862 (1939), and Fillinger v. NW. Agency, Inc., of Great Falls, 283 M 71, 938 P2d 1347 (1997), raised by the Swansons in support of that exception. The Supreme Court held that the parol evidence rule applies to exclude evidence extrinsic to an unambiguous contract in any situation involving either parties or strangers to the contract when rights and duties created by the contract are the dispositive issue. Habets v. Swanson, 2000 MT 367, 303 M 410, 16 P3d 1035, 57 St. Rep. 1567 (2000).

Coexistence of Instructions on Parol Evidence and Waiver: An instruction prohibiting consideration of parol evidence on what the contract language required for performance may coexist with an instruction and evidence on waiver. Pipe Indus. Ins. Fund Trust v. Consol. Pipe Trades Trust, 233 M 162, 760 P2d 711, 45 St. Rep. 1392 (1988).

Extrinsic Evidence Unnecessary When Devise Clear: The language of a devise bequeathed property, if any, left in a partnership at the time of testator's demise. The District Court found the partnership to be a conduit through which the partners conducted their tenancy-in-common business and reported income for tax purposes; however, absent any partnership interest in real property, the court determined no property should pass and properly granted summary judgment. Because the testator's intention could be ascertained from the plain language of the devise alone, it was not necessary or proper for the court to receive extrinsic evidence in making its determination. In re Estate of Greenfield, 232 M 357, 757 P2d 1297, 45 St. Rep. 1112 (1988).

Extrinsic Evidence of Ownership of Joint Bank Account Inadmissible When Third-Party Rights Involved: Evidence of the intent of the parties with respect to ownership of funds in a joint bank account is admissible only in a dispute between those parties and not when the dispute involves the rights of a third party. Univ. of Mont. v. Coe, 217 M 234, 704 P2d 1029, 42 St. Rep. 1160 (1985), distinguished in Seman v. Lewis, 252 M 508, 830 P2d 1294, 49 St. Rep. 206 (1992), in which extrinsic evidence regarding intent was held admissible because it was submitted to supplement rather than contradict the uncertain terms of the signature card.

28-2-906. When written contract takes effect.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

Case Notes

No Modification of Original Construction Agreement: In a construction contract dispute, the general contractor submitted a Subcontract Agreement (Agreement) to the subcontractor 2 weeks after the subcontractor had begun work. The Agreement expanded the scope of the work the subcontractor had agreed to perform without additional compensation. The general contractor argued the Agreement modified any contract with the subcontractor because the subcontractor: (1) orally agreed to the Agreement; (2) submitted a payment application in compliance with the Agreement; and (3) admitted to having signed the Agreement. The Supreme Court concluded no modification occurred. The parties had not fully executed the alleged oral agreement; therefore, it could not operate as a modification. Compliance with the payment process did not rise to the requisite level of assent to modification. Pursuant to 28-2-906, a written contract must be delivered before it becomes effective. Since the subcontractor never returned the Agreement to the general contractor, no modification occurred. AAA Constr. of Missoula, LLC v. Choice Land Corp., 2011 MT 262, 362 Mont. 264, 264 P.3d 709.

Incomplete Instrument: Delivery of an incompleted instrument is ineffective; hence where at the time a lessee signed a receipt for a copy of a lease the instrument was incomplete in that one of the lessors had not signed it, the Court properly found that it was ineffective for failure of delivery, the fact that later in the day the missing signature was appended not changing the result in the absence of evidence that the instrument was delivered thereafter. Nelson v. Davenport, 86 M 1, 281 P 537 (1929).

Lease: A lease, like any other written contract, does not become effective until it is delivered, the mere signing of it not binding the parties; the object of the delivery of such an instrument is to indicate an intent on the part of the grantor to give effect to the instrument, and whether delivery is complete is largely a question of intention. Nelson v. Davenport, 86 M 1, 281 P 537 (1929).

28-2-907. Applicability of rules concerning transfers in general.

Law Review Articles

Application of Equitable Conversion to Contracts for the Sale of Land, Stimson, 4 Mont. L. Rev. 88 (1943).

Part 15
Enforcement of Contracts

Part Case Notes

Party Not Entitled to Arbitration After Termination of Contract: The Whites entered into a construction contract with Longley for the construction of their home. After failing to perform under the terms of the contract, Longley persuaded the Whites to buy him out of the contract for $30,000 and to let him continue to build the home without a contract. Subsequently, Longley failed to build a house that could be occupied or salvaged. Prior to the start of trial, Longley filed a motion to compel arbitration under the terms of the original contract. The Supreme Court held that Longley had taken $30,000 to terminate the parties' ongoing obligations under the contract and therefore there was no legal or factual basis upon which Longley could compel the Whites to arbitrate any dispute. White v. Longley, 2010 MT 254, 358 Mont. 268, 244 P.3d 753.

District Court Enforcement of Settlement Agreement in Pending Case: When a case is pending before a District Court, either party is entitled to make a motion to enforce a settlement agreement as long as the existence and terms of the agreement are not in dispute. Hinderman v. Krivor, 2010 MT 230, 358 Mont. 111, 244 P.3d 306.

Challenge to Contract or to Arbitration Clause — When Arbitration Appropriate: Plaintiffs defaulted on a loan with defendant, and nonjudicial foreclosure proceedings were begun. The loan contract contained an arbitration clause, but plaintiffs challenged the validity of the contract as a whole, not the validity of the arbitration clause. On defendant's motion, the District Court ordered arbitration, and plaintiffs appealed. The Supreme Court held that under federal law, when a complaint specifically challenges a contract arbitration clause, the doctrine of severability set out in Prima Paint Corp. v. Flood & Conklin Mfg. Co., 388 US 395 (1967), in conjunction with the Federal Arbitration Act, allows a court to hear the challenge. However, when, as here, a complaint challenges a contract as a whole, Prima Paint and Buckeye Check Cashing, Inc. v. Cardegna, 546 US 440 (2006), require a court to grant a motion to compel arbitration if the contract contains an arbitration provision. Thus, despite plaintiffs' contention that the contract itself was void ab initio, the District Court was affirmed. Martz v. Beneficial Mont., Inc., 2006 MT 94, 332 M 93, 135 P3d 790 (2006). However, see Thompson v. Lithia Chrysler Jeep Dodge of Great Falls, 2008 MT 175, 343 M 392, 185 P3d 332 (2008), in which a narrow exception to the Martz rule established that when a party challenges a contract containing an arbitration clause on the ground that the parties never entered a contract, the court, not arbitration, is the appropriate forum to decide whether a contract existed, prior to compelling arbitration.

Federal Law Regarding Nonliability for Borrower's Payment of Fees to Lender Upon Loan Rescission Inapplicable to Mortgage Broker Fees: Plaintiff helped defendant secure a loan, which defendant subsequently rescinded within the applicable 3-day period pursuant to the federal Truth in Lending Act. Plaintiff sent defendant a bill for its brokerage fee and out-of-pocket expenses incurred in securing the loan commitment, as provided in the brokerage contract and an attendant promissory note. Defendant refused to pay the bill, and plaintiff brought an action to enforce the contract and promissory note, and the District Court enforced the note and ordered defendant to pay the bill. Defendant appealed on grounds that 16 U.S.C. 1635(b) of the Truth in Lending Act and 12 CFR 226.23, Regulation Z, clearly provide that when a consumer rescinds a transaction, the consumer is not liable for any amount, including any finance charge. The Supreme Court affirmed the District Court ruling. Although the federal law protects defendant from paying any fees to the lender, it does not address arrangements between a borrower and a mortgage broker, and in fact, portions of Regulation Z at 12 CFR 226.4(a) expressly exclude appraisal and service fees from the definition of a finance charge. Therefore, even though defendant effectively rescinded that mortgage with the lender, the rescission did not affect or alter defendant's obligation to the mortgage broker pursuant to the brokerage contract and promissory note. Mortgage Source, Inc. v. Strong, 2003 MT 205, 317 M 37, 75 P3d 304 (2003).

Attempted Sale of Parcel in Violation of Contract — Plantiff Allowed to Block Sale: Defendants contracted to purchase several parcels of property from plaintiff. When defendants ended up in default, defendants decided to sell one of the parcels to pay off part of the contract balance. Plaintiff attempted to block the sale, and the District Court confirmed plaintiff's ability to do so under the terms of the contract. Defendants appealed, but the Supreme Court affirmed. A provision of the contract allowed the subsequent sale of the parcels by defendants, but only after the principal balance was paid. Because defendants were in default when the attempted sale was made, sale of the tract was not permitted by the terms of the contract. The District Court did not err in holding that plaintiff had a contractual right to block the sale. Weter v. Archambault, 2002 MT 336, 313 M 284, 61 P3d 771 (2002).

State Remedy and State Court Enforcement of Contract Wages Required by Federal Davis-Bacon Act: The District Court had subject matter jurisdiction of state contract law claims against a contractor and subcontractors by workers hired to build housing on Malmstrom Air Force base under a contract between the contractor and the Air Force. The workers claimed that they were not paid the prevailing wages required by the federal Davis-Bacon Act. The defendants claimed that there was no private right of action and that the workers had not exhausted their federal administrative remedies. The evidence showed that the workers extensively used the administrative remedies, taking all proper steps to attempt to administratively resolve the dispute. The workers were not seeking to enforce the Davis-Bacon Act labor standards; they sought to enforce a contract that includes wages required by the Act, a subtle but important distinction. The Act does not preempt the workers' right to a state enforcement action, using state remedies, under the facts of this case. That right is in keeping with Montana's longstanding policy and constitutional guarantee in Art. II, sec. 16, Mont. Const., of citizens' access to Montana courts when they are aggrieved. As third-party beneficiaries of the contract, the workers have the right to sue in state court to enforce the contract under state law. Favel v. Am. Renovation & Constr. Co., 2002 MT 266, 312 M 285, 59 P3d 412 (2002).

Vehicle Service Contract — Enforcement as Third-Party Beneficiary: When Harman bought an automobile from a dealer, he also bought an extended service contract that was to be administered by MIA. MIA declared itself bankrupt shortly after Harman's purchase. Century, a wholly owned subsidiary of CIGNA, sold an insurance policy to the car dealer to cover repair costs not covered by the agreement between the dealer and MIA. When MIA declared bankruptcy, AAC, another subsidiary of CIGNA, was used to adjust service contracts sold by MIA. Later, Harman made a claim against the service contract when the front axle of his vehicle was damaged. AAC refused the claim, saying that the repair was not covered by the contract. Harman brought a breach of contract action against AAC, but the District Court found that because AAC was not a party to the contract between MIA and Harman, Harman could not sue AAC. Citing Restatement (Second) of Contracts 302 (1981), the Supreme Court held that Harman was the third-party beneficiary of an agreement between AAC and Century for AAC to adjust the claims covered by Century's insurance contract with the dealer. Because Harman was an intended beneficiary, he had a right to seek damages for breach of contract by AAC for its failure to perform its administrative responsibilities in accordance with Harman's rights under the contract. Harman v. MIA Serv. Contracts, 260 M 67, 858 P2d 19, 50 St. Rep. 954 (1993).

Obligation to Make Payments Under Mining Agreement When Escrow Not Established: In a mining agreement with an option to purchase, the covenant to establish escrow was a material part of the contract and a condition precedent to the plaintiff's obligation to make payments. Although the plaintiff knew escrow had not been established, he did not waive the requirement, and the defendant defaulted first when he refused to establish escrow. Therefore, the defendant could not enforce the making of payments. Rogers v. Relyea, 184 M 1, 601 P2d 37 (1979).

Part Law Review Articles

Corporate By-Law Depriving Stockholders of Right to Vote Cumulatively Unenforceable as a Contract, Wilson, 22 Mont. L. Rev. 185 (1961).

Venue of Actions on Contracts, McNamer, 16 Mont. L. Rev. 68 (1955).

28-2-1501. When successive actions on same contract permitted.

Case Notes

Successive Action for Each Missed Payment Under Contract — No Claims Preclusion: The parties entered into a contract whereby the defendant would operate a ski lift on behalf of a housing development in Big Sky for an annual fee. In 2008, the defendant filed a breach of contract claim against the plaintiff and sought payment for operating the ski lift from 2001 to 2002. In 2009, the plaintiff filed an action alleging that the defendant had engaged in wrongful collection efforts, and the defendant counterclaimed for operating costs for three more ski seasons. The plaintiff argued that the defendant's new claims were barred under claims preclusion because the issues in the earlier suit were the same. The District Court granted the defendant summary judgment. On appeal, the Supreme Court affirmed, ruling that each missed payment was for a different time period and therefore the issues were not the same. Lone Moose Meadows, LLC v. Boyne USA, Inc., 2017 MT 142, 387 Mont. 507, 396 P.3d 128.

Lease for Term of Years: Tenants after bringing action against landlords for breach of contract at end of 1957-1958 season could treat each year of the ranch lease contract as a divisible part of the contract where it contained several divisible parts and ran for 4 successive years; each year of the farm operation and each year of the livestock operation was a separate phase to be separately performed and settled. Green v. Wolff, 140 M 413, 372 P2d 427 (1962).

Alimony Installments: There is nothing in this section or in any other section of the Codes to prevent the bringing of successive suits for recovery of delinquent alimony installments fixed by an agreement between the parties in different departments of the same court. State ex rel. Towne v. District Court, 114 M 1, 132 P2d 161 (1942).

Part 16
Modification of Contracts

Part Case Notes

Reliance on Numerous Extensions of Loan to Receive Another — No Excuse for Nonpayment of Debt — Foreclosure — No Error: The defendant argued that the plaintiff bank waived its right to the mature debt of a loan at the end of a seventh extension period by continuing to give extensions, and the defendant did not pay off the loan because he assumed he would receive another extension. However, the plaintiff waived its rights only for a defined period within the extension agreements, not its right to full, eventual payment. Because the defendant was not promised another extension period and the evidence indicated that the plaintiff informed the defendant the loan would not be extended again, there was no issue of material fact to excuse the defendant's nonpayment of the debt, and the District Court did not err in granting the plaintiff summary judgment to foreclose. Furthermore, the plaintiff was not obligated by the covenant of good faith and fair dealing to extend the loan repayment an eighth time. HSBC Bank USA, N.A. v. Anderson, 2017 MT 257, 389 Mont. 106, 406 P.3d 416.

No Implied Waiver Contract Provision Subject to Waiver or Modification: In an action involving several complex business transactions, the District Court allowed the plaintiffs to present evidence regarding contract formation and waiver to the jury. On appeal, the defendant bank argued that the no waiver provision of the contract applied. The Supreme Court disagreed, holding that antiwaiver clauses are like any other clause in a contract, subject to waiver or modification by performance. Masters Group Int'l, Inc. v. Comerica Bank, 2015 MT 192, 380 Mont. 1, 352 P.3d 1101.

Bridle Path Easement — Express Easement by Reservation Versus Implied Easement — Extrinsic Evidence Regarding Parties' Intent Inadmissible: Purchasers in a subdivision had language in their deeds creating an express easement for a bridle path in the subdivision. The bridle path was never built, and over the years, the easement was obstructed by improvements on the lots of several subdivision residents. Eventually, the subdivision association attempted to extinguish the easement at a meeting of the board of directors. Some residents asked the District Court to establish the validity of the easement and to restrain obstruction of the easement, and their request was granted by partial summary judgment. On appeal, the Supreme Court noted the difference between an implied easement, which is a creature of equity dependent on the intent of the parties, and an express easement by reservation, which is a creature of the documents of conveyance and the record. An express easement by reservation arises when the purchaser's deed refers to the plat where the easement is clearly depicted and labeled. In this case, the intent of the parties to create a bridle path easement was manifested through the language in the deeds and the plat, so under 28-2-905, extrinsic evidence regarding the intent of the parties was inadmissible. Further, the subdivision association was given oversight of the easement, but not ownership of it, and so lacked authority to extinguish the easement. The lower court's finding that a valid bridle path easement existed was affirmed. Pearson v. Virginia City Ranches Ass'n, 2000 MT 12, 298 M 52, 993 P2d 688, 57 St. Rep. 65 (2000), following Missoula v. Mix, 123 M 365, 214 P2d 212 (1950), Bache v. Owens, 267 M 279, 883 P2d 817 (1994), Halverson v. Turner, 268 M 168, 885 P2d 1285 (1994), and Tungsten Holdings, Inc. v. Parker, 282 M 387, 938 P2d 641, 54 St. Rep. 399 (1997), and distinguishing White v. Landerdahl, 191 M 554, 625 P2d 1145, 38 St. Rep. 412 (1981).

Executed Oral Agreement — Meeting of Minds Required: The parties entered into an agreement for the lease of a truck. The lease agreement contained a noncancellation provision and provided alternative remedies to the lessor in the event of a default. Lessee returned the truck with current payments to lessor prior to the termination date of the lease. Lessor had to make repairs to the truck. Lessee contended the return was a fully executed oral contract to terminate the lease. Lessor contended that termination was dependent on the condition of the truck. There was substantial evidence to support the finding that there was no meeting of the minds and therefore no agreement to terminate the lease. Diede v. Davis, 203 M 205, 661 P2d 838, 40 St. Rep. 394 (1983).

Enforceability of Nonmodification Clause: Parties filed a joint petition for dissolution of marriage in 1979. With their petition they filed a separation and property settlement agreement that included a provision requiring the husband to pay the wife $375 a month until she died or remarried. The agreement contained a nonmodifiability clause. The court found the agreement was not unconscionable and incorporated it into the decree. In 1982, the wife petitioned the District Court to order the husband to appear and show cause why he had not complied with the agreement. The husband cross-petitioned for an order terminating his maintenance obligation. The District Court granted the husband's petition. On appeal, the Supreme Court reversed and remanded, finding that under 40-4-201(6) the nonmodifiability clause was valid and enforceable regarding maintenance. Bolstad v. Bolstad, 203 M 131, 660 P2d 95, 40 St. Rep. 344 (1983).

Implied Easements — When Found — Effect of Contract: The plaintiffs sold a parcel of land to the defendants after a series of negotiations. No easement was specified through that parcel to the plaintiff's adjoining parcel, and no other access existed to that second parcel. The Supreme Court found no implied easement, noting that the trial court would have been rewriting the contract had it found an implied easement. The trial court cited eight offers and counteroffers regarding an easement in this land sale and noted that there was a final decision between the parties that there would be no easement across the defendants' land. A court may not create as a matter of law an implied easement when the facts indicate the parties did not intend that an easement be created. Implied easements rest upon the intent of the parties gathered from the evidence. The record contained insufficient evidence to support an implied easement but contained substantial evidence to support the trial court's findings, conclusions, and judgment. White v. Landerdahl, 191 M 554, 625 P2d 1145, 38 St. Rep. 412 (1981), distinguished in Pearson v. Virginia City Ranches Ass'n, 2000 MT 12, 298 M 52, 993 P2d 688, 57 St. Rep. 65 (2000), with regard to the applicability of an implied easement, which is a creature of equity dependent on the intent of the parties, versus an expressed easement by reservation, which is a creature of the documents of conveyance and the record.

28-2-1601. Alteration of oral contract by parties.

Case Notes

Employee Handbook — Adoption by Employer After Employee Began Work — Consideration Found in Continuation of Employment — Part of "Bargained" Contract — Gates Distinguished — Remand Unnecessary: After Langager went to work for Crazy Creek Products (CCP), CCP distributed an employee handbook that Langager felt changed the terms of her oral contract regarding earning and using paid vacation days by requiring that she be present to work immediately before and after a paid vacation. At a meeting of CCP employees that was held after distribution of the handbook, CCP supervisors asked if there were any comments from employees concerning the handbook. After Langager went on a 2-week vacation but was refused pay for her vacation weeks because she quit her job and was not at work the shift following her vacation, she filed an action to recover her wages earned while she was on vacation. The Supreme Court held that because Langager remained an employee at CCP after the handbook was distributed, there was sufficient consideration for the change in her contract represented by the handbook and that because employees were asked for their input concerning the handbook, the change in the employment contract represented by the handbook had been "bargained" for.

In so holding, the Supreme Court distinguished Gates v. Life of Mont. Ins. Co., 196 M 178, 638 P2d 1063 (1982), in which an employee handbook was adopted many years after some employees commenced employment, was not bargained for, and constituted a unilateral amendment of an employment contract. The Supreme Court also held that since there was general evidence throughout the District Court record that the terms of the handbook were bargained for and that new consideration was given for the change, it was unnecessary, in response to CCP's argument that the District Court substituted its judgment for that of the Board of Personnel Appeals in violation of 2-4-704, to remand the case to the District Court. In re Wage Claim of Langager v. Crazy Creek Products, Inc., 1998 MT 44, 287 M 445, 954 P2d 1169, 55 St. Rep. 169 (1998).

Prior Oral Agreement Extinguished by Doctrine of Merger: The plaintiff, Eiselein, argued that the lower court had erred in granting the bank's motion for summary judgment. The lower court ruled that even if the bank had made an oral promise to lend Eiselein $150,000, that agreement was extinguished by a subsequent written agreement under which the bank lent the plaintiff only $35,000. The Supreme Court affirmed the lower court's decision on the basis that even if there had been a prior oral agreement, the subsequent writing between the parties would extinguish the oral agreement pursuant to the doctrine of merger. Eiselein v. Mont. Bank of Roundup, 250 M 71, 818 P2d 365, 48 St. Rep. 826 (1991).

Alteration of Oral Contract — Rescission — Damages: Plaintiffs had an oral agreement with defendants to pay one-half of defendants' purchase price under defendants' written contract for deed for purchase of certain real property with the understanding that plaintiffs' names would be added to the title as copurchasers. Without plaintiffs' consent, defendants made written assignment of their interests under the written contract to a third party, retaining a life estate to themselves. Plaintiffs refused to make further payments and sued for damages and to quiet title in themselves. The District Court denied plaintiffs' claims and in effect found plaintiffs to be the breaching party. The Supreme Court found plaintiffs were entitled to rescission and reversed the District Court decision. Defendants' assignment while retaining a life estate constituted a material alteration of the oral agreement to which plaintiffs had not consented. Defendants' breach entitled plaintiffs to recover money they had paid on the contract with interest. Forsythe v. Elkins, 216 M 108, 700 P2d 596, 42 St. Rep. 680 (1985).

Employee Handbook — Not Modification of Employment Contract: Gates was discharged from her employment by Life of Montana, which did not follow its employee handbook in discharging her. The court found that the handbook was not distributed until 2 years after Gates was hired. It constituted a unilateral statement of company policies and procedures. Its terms were not bargained for, and there was no meeting of the minds. The employee handbook was not part of Gates' employment contract at the time she was hired, nor could it have been a modification to her contract because there was no new and independent consideration for its terms. Gates v. Life of Mont., 196 M 178, 638 P2d 1063, 39 St. Rep. 16 (1982), distinguished in In re Wage Claim of Langager v. Crazy Creek Products, Inc., 1998 MT 44, 287 M 445, 954 P2d 1169, 55 St. Rep. 169 (1998).

28-2-1602. How written contract may be altered by parties.

Case Notes

Oral Modification Effective 289
Oral Modification Ineffective 291
Parol Evidence Admissible 293
Parol Evidence Inadmissible 294
General 295

ORAL MODIFICATION EFFECTIVE

Substantial Evidence to Support Award of Damages: In an action by the plaintiff contractor to foreclose a construction lien against the defendant homeowners, the District Court awarded contract damages to the plaintiff for $8,317 in contractor's fees, work completed, and materials used. The defendants appealed, arguing the District Court awarded damages to the plaintiff in error. On appeal, the Supreme Court affirmed, finding that the parties had formed an enforceable contract with sufficient consideration between them, even though the contract consisted of a written construction estimate from the plaintiff that did not include some important terms. The Supreme Court found there was sufficient evidence that the plaintiff was entitled to its contractor fee for driveway work, based on an oral modification to the agreement and the defendants' payment of contractor fees for other work, and found there was also sufficient evidence that the plaintiff was entitled to additional money related to labor and materials supplied for masonry and stonework. Vintage Constr., Inc., v. Feighner, 2017 MT 109, 387 Mont. 354, 394 P.3d 179.

No Duty to Recover Funds Under Contract — No Breach of Contract or Covenant of Good Faith and Fair Dealing — Statute of Limitations for Equitable Relief Expired: The plaintiff contracted with Bancard Services, Inc. (Bancard), one of the defendants, for Bancard to provide processing services to the plaintiff's ATMs located throughout Montana. Bancard subcontracted with a third-party payment processor to assist in processing transactions, and an agent of the third party made a data entry error that transferred $285,000 of the plaintiff's funds to an out-of-state individual, Leland Ruzicka, and B&B Lounge (collectively Ruzicka), also defendants in the case. Bancard was able to recover all but $35,000 of the plaintiff's funds. Eventually, the plaintiff sued both Bancard and Ruzicka for the outstanding $35,000. The plaintiff also filed several contractual related claims against Bancard. The District Court granted summary judgment to the defendants because Bancard did not have an obligation to recover the funds under the parties' contract and because the statute of limitations had expired on the unjust enrichment claims against Ruzicka. Grizzly Sec. Armored Express, Inc. v. Bancard Serv., LLC, 2016 MT 287, 385 Mont. 307, 384 P.3d 68.

Acquiescence in Contract Modification Precluding Assertion of Damages From Breach of Original Contract — Proof of Waiver: A party that acquiesces to the modification of a contract may be estopped from asserting damages arising from breach of the original contract. Waiver of contract provisions may be proved by express declarations or by a course of acts and conduct that induce the belief that the intention or purpose was to waive. In the present case, the District Court did not err in finding that the parties agreed to a modification in the terms of a road building contract and that the contractor was not in breach of the original contract by building the road to the specifications of the modification. DeNiro v. Gasvoda, 1999 MT 129, 294 M 478, 982 P2d 1002, 56 St. Rep. 521 (1999), following Hellickson v. Barrett Mobile Home Transp., Inc., 161 M 455, 507 P2d 523 (1973), Mathis v. Daines, 196 M 252, 639 P2d 503, 39 St. Rep. 73 (1982), and Lemley v. Allen, 203 M 37, 659 P2d 262, 40 St. Rep. 279 (1983). See also Lewistown Miller Constr. Co., Inc. v. Martin, 2011 MT 325, 363 Mont. 208, 271 P.3d 48.

Lease — Effective Date of Oral Modification: Lessor and lessee orally agreed to modify written lease to expand the space leased and raise the rent from $150 to $220 a month. The oral agreement was executed and in force when lessee started using the additional space and began paying the additional rent. Lemley v. Allen, 203 M 37, 659 P2d 262, 40 St. Rep. 279 (1983), followed in Eagle Watch Inv., Inc. v. Smith, 278 M 187, 924 P2d 257, 53 St. Rep. 757 (1996), and DeNiro v. Gasvoda, 1999 MT 129, 294 M 478, 982 P2d 1002, 56 St. Rep. 521 (1999).

Modification of Lease: A written lease may be modified by executed verbal agreements such as increases in the rental payment and expansion of the leased premises. Kosena v. Eck, 195 M 12, 635 P2d 1287, 38 St. Rep. 1736 (1981), followed in Eagle Watch Inv., Inc. v. Smith, 278 M 187, 924 P2d 257, 53 St. Rep. 757 (1996).

Waiver of Contract Requirement:

Buyer and seller of real estate could orally alter agreement to sell and purchase, thus waiving condition in the instrument that it would be void if contract for deed was not executed within 10 days. Reilly v. Maw, 146 M 145, 405 P2d 440 (1965).

Where a building contract required that all changes in building plans by the owner were to be in writing and owner later made oral changes in the plans, the requirement of writing was deemed waived by the court. Gramm v. Ins. Unlimited, 141 M 456, 378 P2d 662 (1963).

A requirement of written notice may be waived by parol, and a waiver of notice may be express or may be inferred from the conduct of the parties. Flint v. Mincoff, 137 M 549, 353 P2d 340 (1960).

Oral Termination: A written lease for term of years may be terminated by an oral agreement provided the conduct of the parties is consistent with such an agreement. Rodgers v. Saunders, 144 M 424, 396 P2d 817 (1964).

Acceleration Agreement: Plaintiff, subcontractor, a bridge construction specialist, under road construction project, was entitled to part of acceleration payment under prime contract pursuant to agreement, where written contract was orally modified to provide for acceleration of certain items of work by plaintiff and for payment of additional sums to him; there was consideration for the modification, and such work was performed by plaintiff. Dalakow v. Geery, 132 M 457, 318 P2d 253 (1957), distinguished in Total Indus. Plant Serv., Inc. v. Turner Indus. Group, LLC, 2013 MT 5, 368 Mont. 189, 294 P.3d 363.

When Oral Agreement Fully Executed:

The date when an oral agreement takes effect as altering a written contract within the meaning of this section is the date when it is executed. Griffiths v. Thrasher, 95 M 210, 26 P2d 995 (1955).

Where the maturity of promissory notes had been extended 2 years by an executed oral agreement, to wit, by payment of $1,000 in consideration of such extension, immediately upon payment of the consideration the agreement became fully executed and effective to modify the written contract of the parties under this section. Griffiths v. Thrasher, 95 M 210, 26 P2d 995 (1933).

Extension — Consent: Where the lessor of oil and gas lands, before default by the lessee, orally agreed to an extension of the time within which the latter was required to make payment under the contract, and the lessee remained in possession of and exercised dominion over the property thereafter with the consent of the lessor, the written contract became modified by an executed oral agreement. Griffith v. Cedar Creek Oil & Gas Co., 91 M 553, 8 P2d 1071 (1932).

Complete, Not Partial, Execution of Oral Agreement Necessary:

A contract to sell land is an "executory contract" until the conveyance is made. Bauer v. Monroe, 117 M 306, 158 P2d 485 (1945).

An "executed contract" is one where nothing remains to be done by either party, while an "executory contract" is one in which a party binds himself to do or not to do a particular thing in the future. Bauer v. Monroe, 117 M 306, 158 P2d 485 (1945).

An oral agreement altering a written agreement is not an "executed oral agreement" within statute authorizing modification of a written contract by an executed oral agreement unless its terms have been fully performed, and performance on one side is not sufficient. Ikovich v. Silver Bow Motor Co., 117 M 268, 157 P2d 785 (1945).

To bring about a modification or alteration of a written contract by an executed oral agreement under this section or to make parol evidence of such modification admissible there must have been a complete, not partial, execution of the obligations of both parties. Cont. Oil Co. v. Bell, 94 M 123, 21 P2d 65 (1933).

Extension of Due Date by Executed Oral Agreement — Authority of Agent to Agree to Extension Need Not Be in Writing: Where the due dates of chattel mortgage notes were extended 2 years by oral agreement between the maker and the agent of the payee, which agreement was at once fully executed by payment of a consideration for the extension, it was not necessary that the authority of the agent to act should have been in writing; the oral agreement having been fully executed, it was valid though not in writing (this section) and therefore the authority of the agent was likewise not to be required to be in writing. Griffiths v. Thrasher, 95 M 210, 26 P2d 995 (1933).

Abrogation — Subsequent Agreement: The parties to an agreement may abrogate it by a subsequent one, and therefore may in a deed agree that it shall run to the purchaser "and wife" though in a bond for the deed it was provided that it should run to the purchaser alone. Humble v. St. John, 72 M 519, 234 P 475 (1925).

ORAL MODIFICATION INEFFECTIVE

No Modification of Original Construction Agreement: In a construction contract dispute, the general contractor submitted a Subcontract Agreement (Agreement) to the subcontractor 2 weeks after the subcontractor had begun work. The Agreement expanded the scope of the work the subcontractor had agreed to perform without additional compensation. The general contractor argued the Agreement modified any contract with the subcontractor because the subcontractor: (1) orally agreed to the Agreement; (2) submitted a payment application in compliance with the Agreement; and (3) admitted to having signed the Agreement. The Supreme Court concluded no modification occurred. The parties had not fully executed the alleged oral agreement; therefore, it could not operate as a modification. Compliance with the payment process did not rise to the requisite level of assent to modification. Pursuant to 28-2-906, a written contract must be delivered before it becomes effective. Since the subcontractor never returned the Agreement to the general contractor, no modification occurred. AAA Constr. of Missoula, LLC v. Choice Land Corp., 2011 MT 262, 362 Mont. 264, 264 P.3d 709.

Landowner Subdivision Rights Precluded by Restrictive Covenants — No Oral Contract Without Consideration — Statute of Frauds Applied: Plaintiffs subdivided about 80 acres into a 40-acre water ski lake and five residential lots. Restrictive covenants provided that no more than six landowners would be allowed to use the lake, that five landowners would be owners of lots in the subdivision, and that one landowner would be the owner of a single family dwelling built on property immediately west of the lake. Plaintiffs initially intended to build on the west side of the lake and become the sixth landowner but changed their minds, sold the west side property, and decided to build on the south side instead. Four of the five landowners filed an affidavit that when they purchased their lots, they understood that plaintiffs would be the sixth landowner and that they had orally approved the relocation of plaintiffs' residence to the south shore. After plaintiffs' home was built on the south side, they sought a declaratory judgment that they were the sixth landowner under the restrictive covenants and thus had the right to use the lake. One dissenting landowner opposed the declaratory judgment and moved for summary judgment on grounds that the restrictive covenants prohibited plaintiffs from use of the lake. The District Court agreed and granted summary judgment. On appeal, the Supreme Court agreed that there was no evidence of consideration given to the landowners for modification of the covenants and that as a result, the modification benefited plaintiffs only. The right to use the lake ran with the land and was therefore a real property interest, and under the statute of frauds, any transfer of the right from one parcel to another had to be in writing or altered by an executed oral agreement. However, without consideration, there could be no oral contract, and without an oral contract, there could be no executed oral contract. Plaintiffs' argument that because they relied on oral agreements, equitable estoppel should prohibit defendants from denying plaintiffs' use of the lake also failed because equitable estoppel does not apply under the statute of frauds except when the statute would operate to perpetuate a fraud. The District Court was affirmed. Hanson v. Water Ski Mania Estates, 2005 MT 47, 326 M 154, 108 P3d 481 (2005).

Contract With Dispute Resolution Clause Not Superseded by Unexecuted Oral Agreement: Nelcon made an agreement with the state for highway construction work, and Nelcon subcontracted the clearing of trees to Westfork, agreeing that Westfork could have the timber that was removed from the property. After discovering that the timber belonged to Champion and had been removed, Westfork wrote Nelcon, requiring additional payment for the missing trees. Nelcon provided notice to the state that Nelcon needed additional compensation for the missing trees and was paid approximately $20,000, which Nelcon paid to Westfork. Westfork brought an action against Nelcon for additional compensation, and the District Court granted a directed verdict for Nelcon. Citing Kraft v. Hodson, 254 M 262, 836 P2d 1234 (1992), the Supreme Court held that there was no executed oral modification of the original contract. The Supreme Court also held that the language of the original contract was clear in its meaning, binding Westfork to the same rights against Nelcon that Nelcon had against the state. Westfork Constr. Co. v. Nelcon, Inc., 265 M 398, 877 P2d 481, 51 St. Rep. 553 (1994), followed, with regard to lack of court authority to insert or delete contract provisions in an unambiguous contract, in Topco, Inc. v. St., 275 M 352, 912 P2d 805, 53 St. Rep. 175 (1996), and distinguished in Lewistown Miller Constr. Co., Inc. v. Martin, 2011 MT 325, 363 Mont. 208, 271 P.3d 48.

Reliance on Statute of Frauds Not Perpetuation of Fraud Against Broker: Kraft, a broker, alleged that the seller, Hodson, had orally modified their listing agreement in a manner allowing Kraft to negotiate with the ultimate buyer of the property, thereby entitling Kraft to a commission. The Supreme Court held that any modification to the contract had to be in writing or else the statute of frauds would be rendered a nullity. Kraft v. Hodson, 254 M 262, 836 P2d 1234, 49 St. Rep. 792 (1992), followed in WRB-West Associates, Inc. v. Madison Addition Inv. Ltd. Partnership, 270 M 498, 893 P2d 340, 52 St. Rep. 329 (1995).

Breach of Verbal Agreement — Proof of Performance and Damages Required: Defendants claimed that their bank breached its verbal agreement to reamortize loan payments, which led to defendants' inability to repay the loan and eventual foreclosure. In order for defendants to prevail, they had to prove that they would have been in a position to perform their part of such an agreement and that they were damaged by the bank's refusal to reamortize their loan. However, evidence showed that reamortization would have resulted in payments higher rather than lower than the original loan payments, which defendants were unable to repay. Absent evidence of the ability to make further payments if allowed to reamortize, defendants sustained no damage by the bank's refusal to do so. Fed. Land Bank of Spokane v. Snider, 247 M 508, 808 P2d 475, 48 St. Rep. 285 (1991).

Oral Profit-Sharing Agreement Not Executed: Winkel filed a complaint arising out of an employment contract. Vranish argued that Winkel was not entitled to any profit-sharing bonus because the original written employment contract did not provide for a profit-sharing bonus. A contract in writing may be altered by a contract or by an executed oral agreement and not otherwise. An oral agreement altering a written agreement is not an executed oral agreement within this section unless its terms have been fully performed; performance on one side is not sufficient. The testimony reveals that the oral agreement concerning the profit-sharing bonus was never performed; thus the oral agreement was not executed. Winkel v. Family Health Care, 205 M 40, 668 P2d 208, 40 St. Rep. 1083 (1983), distinguished in Lewistown Miller Constr. Co., Inc. v. Martin, 2011 MT 325, 363 Mont. 208, 271 P.3d 48.

Alteration by Subsequent Oral Executed Agreement: Terms of written contract may be waived or modified by independent oral agreements between the parties that are subsequently executed. However, where electrical contractor submitted claim for extra material and services performed without written request of owner and owner refused to pay, owner could not be said to have waived any terms of original contract since no evidence was produced to indicate that he relinquished his right to object. Mathis v. Daines, 196 M 252, 639 P2d 503, 39 St. Rep. 73 (1982), followed in DeNiro v. Gasvoda, 1999 MT 129, 294 M 478, 982 P2d 1002, 56 St. Rep. 521 (1999). See also Lewistown Miller Constr. Co., Inc. v. Martin, 2011 MT 325, 363 Mont. 208, 271 P.3d 48.

Oral Modification of Contract for Deed: Under this section, a written contract for deed could not be properly modified by an oral agreement to offset against payments due under the contract certain rents due buyer from sellers. Hares v. Nelson, 195 M 463, 637 P2d 19, 38 St. Rep. 2036 (1981).

Effect of Oral Agreement on Written Agreement — Contract for Deed: In this case concerning a contract for deed, one issue on appeal was the effect of an oral agreement on written instruments that followed. The Supreme Court held that it was clear that the written instruments superseded the oral agreement. Stoddard v. Grokin, 191 M 495, 625 P2d 529, 38 St. Rep. 326 (1981), followed in Nimmick v. Hart, 248 M 1, 808 P2d 481, 48 St. Rep. 293 (1991).

Oral Modification of Written Property Settlement — Effect on Debts: An alleged oral modification of a written property settlement agreement could not have the effect of altering a written agreement to repay a loan made to spouses prior to divorce. Thus payment by one obligor (purportedly in the form of a loan to the obligee) of part of the balance was considered as a discharge of the other obligor's obligation to pay that portion. Davidson v. Lewis, 177 M 55, 579 P2d 762 (1978).

Modification of Listing Agreement and Failure to Provide Copy: A seller's alleged verbal consent to a broker's unsubscribed and unexecuted modification of a listing agreement was not a factual issue precluding summary judgment in light of the statutory and decisional law which is uniformly suspicious of such modifications. As a matter of law, the broker's failure to provide the seller with a copy of the listing agreement also supported the granting of summary judgment. Carnell v. Watson, 176 M 344, 578 P2d 308 (1978). See also WRB-West Associates, Inc. v. Madison Addition Inv. Ltd. Partnership, 270 M 498, 893 P2d 340, 52 St. Rep. 329 (1995).

Partial Execution: Alleged oral agreement to pay director commission for procuring purchaser for corporation's realty and personalty was not an "executed oral agreement" within this section since there was no performance by corporation and director's performance was consistent with performance of his duties as an officer-director and not necessarily pursuant to contract. Hart v. Billings Pub. Stockyards, 157 M 345, 486 P2d 120 (1971).

Contract for Deed: Where a formal written contract for deed had been entered into, an alleged oral agreement of the vendor to give the purchaser a deed if he would, among other things, give the vendor a home, was an "executory contract" and was ineffectual to alter the written contract. Bauer v. Monroe, 117 M 306, 158 P2d 485 (1945).

Unexecuted Oral Agreement:

"A contract in writing may be altered by a contract in writing or by an executed oral agreement, and not otherwise" (this section), and since the contract pleaded rested in parol and appears to have been unexecuted, it is impotent and constituted no defense. Olsen v. Zappone, 83 M 573, 273 P 635 (1929); Swan v. Le Clair, 77 M 422, 251 P 155 (1926).

An unexecuted oral agreement, the effect of which was to alter the terms of a promissory note by extending the time of payment and changing the amount due, constituted no defense under this section to the enforcement of the note, and evidence tending to prove the agreement was improperly admitted. Lish v. Martin, 55 M 582, 179 P 826 (1919). See also Morrow v. Bank of America, N.A., 2014 MT 117, 375 Mont. 38, 324 P.3d 1167.

A note and chattel mortgage given to secure it are not affected by an unexecuted oral agreement in respect to the time and manner of payment. Kinsman v. Stanhope, 50 M 41, 144 P 1083 (1914).

Sublease of Mining Claim: A subsequent oral agreement between the parties to a written sublease of a mining claim, that in case the sublessors should buy the property the lease would be extended, was void, being a mere executory agreement without consideration. Armington v. Stelle, 27 M 13, 69 P 115 (1902).

PAROL EVIDENCE ADMISSIBLE

Parol Evidence of Circumstances Under Which Bid Prepared Proper in Interpreting Uncertain Contract Provisions: Bid estimates on a road building project contained vague and ambiguous project requirements, and testimony at trial regarding the height of the finished road was conflicting. Thus, the District Court, in interpreting provisions of the contract that appeared ambiguous or uncertain, properly considered parol evidence of the circumstances under which the bid was prepared. The court found more credible the contractor's testimony that there was not agreement that a subroad would be constructed of pit run gravel 6 inches above field grade, and that determination was affirmed on appeal. DeNiro v. Gasvoda, 1999 MT 129, 294 M 478, 982 P2d 1002, 56 St. Rep. 521 (1999).

Construction Contract — Breach of Contract: Haines Pipeline Construction, Inc., contracted to build a pipeline for Montana Power Company (MPC). Performance was secured by an irrevocable letter of credit. The project ran into regulatory problems, and a settlement agreement was signed between the parties. The parties entered a second contract for miscellaneous repair work on the completed portion of the pipeline, including repair of buried pipeline. Haines extended the letter of credit at the request of MPC, and MPC subsequently drew upon the letter of credit. Haines sued to recover damages against MPC for breach of the construction contract. The District Court found that MPC had accepted Haines' work, that MPC had no authority to draw upon the letter of credit, and that presentment of the letter of credit constituted a breach of the construction contract. On appeal, the Supreme Court held that the District Court did not err in admitting parol evidence of the alteration or modification of the contract by performance and oral agreement of the parties and that the District Court's finding was supported by substantial evidence and was not clearly erroneous. Haines Pipeline Constr., Inc. v. Mont. Power Co., 251 M 422, 830 P2d 1230, 48 St. Rep. 1102 (1991).

Estoppel: Evidence of telephone conversations tending to show acquiescence to agreement to repurchase shares of stock pursuant to corporate officer's previously executed stock repurchase agreement was admissible to show that seller had waived benefit of or become estopped to assert his rights under some or all provisions in his favor in the agreement where conversations were not introduced to vary terms of the contract but to demonstrate that the tender and acceptance had in fact been made. State ex rel. Howeth v. D. A. Davidson & Co., 163 M 355, 517 P2d 722 (1973), overruled, with regard to elements of collateral estoppel, in Dagel v. Great Falls, 250 M 224, 819 P2d 186, 48 St. Rep. 919 (1991).

Parol Evidence of an Executed Oral Agreement:

A written contract may be altered or modified by an executed oral agreement as provided by this section, and parol evidence of alteration or modification may be heard. Jenson v. Olson, 144 M 224, 395 P2d 465 (1964).

Since under this section a written agreement may be modified by an executed oral one where parties had executed a portion of their engagement and then committed the remainder to writing, parol evidence of the part which had been executed was admissible. Webber v. Killorn, 66 M 130, 212 P 852 (1923).

Exception to Establish Fraud: In an action by the payees against the makers for the balance due on a renewal note, where there was fraud and partial failure of consideration and one of the makers testified that he did not know how to figure interest, the makers were not precluded from showing that the contract was different from what the writing showed it to be. Jensen v. Franklin, 135 M 341, 340 P2d 832 (1959).

PAROL EVIDENCE INADMISSIBLE

Modification of Nonexistent Contract Impossible — Minutes of Preconstruction Meeting Inadmissible Extrinsic Evidence Absent Ambiguity in Subsequent Contract: Keeney Construction (Keeney) subcontracted to perform certain construction work for James Talcott Construction Co., Inc. (Talcott). The subcontract stated that time was of the essence, but contained no specific date of completion, Rather, Keeney was to complete the work as directed by Talcott and on Talcott's completion schedule. Keeney asserted that the parties intended a 1996 completion date, but the project was not finished until 1997. Keeney sued for damages for delay and extra work, contending that extrinsic evidence in the form of minutes from a preconstruction meeting, held 2 days before the contract was finalized, would verify the parties' intent and represented an executed oral agreement that modified the written contract. The Supreme Court found no ambiguity in the written contract to warrant further examination of the intent of the parties. Because the intent of the contract was clear, the extrinsic evidence was inadmissible to support the contention that a specific completion date was intended. Keeney could not assert a claim for damages based on Talcott's direction of the timing of the completion of the project when the contract authorized Talcott to do so. Further, because an oral agreement cannot modify a contract that does not yet exist, the meeting and conversations held prior to the contract signing could not be interpreted as a modification of the subsequent written contract. Keeney Constr. v. James Talcott Constr. Co., Inc., 2002 MT 69, 309 M 226, 45 P3d 19 (2002).

Oral Testimony Inadmissible: Trial Court could have excluded evidence relating to a joint venture, 135 M 188, 338 P2d 1037 (1959).

Parol Evidence Inadmissible to Vary Written Contract:

Parol evidence which tended to vary or alter the terms of a written chattel mortgage will be disregarded, where the chattel mortgage was plain and unambiguous and needed no construction. First Nat'l Bank of Plains v. Green Mtn. Soil Conserv. Dist., 130 M 1, 293 P2d 289 (1956).

The statutory rule that a contract in writing may be altered by a contract in writing or by an executed oral agreement and not otherwise is not a rule of evidence but a rule of substantive law. Bauer v. Monroe, 117 M 306, 158 P2d 485 (1945).

Parol testimony of an oral unexecuted agreement by the tenant holding under a written lease that he would surrender the lease and vacate the premises as soon as the landlord could procure a new tenant was inadmissible under this section. Quong v. McEvoy, 70 M 99, 224 P 266 (1924).

Admission of parol evidence to vary and contradict the terms of a written contract is error. Prichett v. Jenkins, 52 M 81, 155 P 974 (1916).

Waiver of Written Option: Where there was a written contract of lease with option to purchase, a waiver of such option could not be shown by oral testimony that lessee prior to time for exercising option made statements that he did not intend to purchase the property if he could get certain other property he was interested in. Fiers v. Jacobson, 123 M 242, 211 P2d 968 (1949).

Extension of Time for Payment: Where escrow agreement in connection with sale of land required $700 to be paid by a certain date, oral evidence could not be received to show that there had been an extension of time. Herman v. Herman, 123 M 39, 207 P2d 1155 (1949).

Rescission by Mutual Consent Not Such "Alteration" as Contemplated by This Section: Where evidence did not indicate an "alteration" of written contract for clearing of land after partial performance, except by rescission, the contention that evidence that parties mutually agreed to rescind written contract was inadmissible on ground that under this section contract in writing may be altered by a contract in writing or by an executed oral agreement and not otherwise, while a novel argument, cannot prevail, since in Montana, under 28-2-1711, rescission of a contract may be had by mutual consent. Barnard-Curtiss Co. v. Maehl, 117 F2d 7 (9th Cir. 1941).

Executed Oral Agreement to Be Pleaded: Where plaintiff in an action on a written contract relies upon an alteration thereof by a subsequent executed oral agreement, he must plead it; in the absence of such a pleading, testimony of the alteration is inadmissible. Hunt v. S Y Cattle Co., 75 M 594, 244 P 480 (1926).

GENERAL

No Implied Waiver Contract Provision Subject to Waiver or Modification: In an action involving several complex business transactions, the District Court allowed the plaintiffs to present evidence regarding contract formation and waiver to the jury. On appeal, the defendant bank argued that the no waiver provision of the contract applied. The Supreme Court disagreed, holding that antiwaiver clauses are like any other clause in a contract, subject to waiver or modification by performance. Masters Group Int'l, Inc. v. Comerica Bank, 2015 MT 192, 380 Mont. 1, 352 P.3d 1101.

Statement of Present Intent to Perform or Not Perform Not Considered Contract — Lease Not Altered by Gratuitous Promise: Defendants had a 99-year lease on a ranch owned by Earl. The lease provided that in case of need, it was subject to recall on demand by Earl. When Earl had to be placed in a nursing home without the assets to bear her expenses and needed to liquidate the property in order to qualify for federal benefits, defendants were notified that the lease was being terminated. Defendants objected, citing a letter from Earl purporting to gift to them all interest in the ranch. However, to be a gift, a transfer of property must be irrevocable, complete, without adequate or full consideration, and unmistakably intended to divest the donor of title, dominion, and control over the property. The District Court concluded that sufficient need existed to terminate the lease and denied defendants' motion to resolve any effect that the letter had on the original lease. The Supreme Court affirmed, finding that the letter was a mere statement by Earl of present intent to perform or not perform an act in the future and that such a gratuitous promise did not constitute a valid written modification of the original lease. Earl v. Beager, 2001 MT 44, 304 M 258, 20 P3d 788 (2001).

Acceptance of One Asphalt Test Sample Insufficient Proof of Waiver of Right to Apply Contract Specifications: Respondent submitted a bid on a highway construction project and contracted with the state to provide polymer modified asphalt cement (PMAC) according to specifications in the state contract, including satisfaction of the ring-and-ball softening point test. The contract required that asphalt samples be taken at the project site, with each sample representing an asphalt lot. Those samples began to fail the ring-and-ball softening point test almost immediately, so according to the contract terms, reductions were made in payments to respondent to make up for the shorter life expectancy and inferior quality of the asphalt. Respondent disputed the payment reductions on the basis that the state had improperly heated the project test samples to a pouring temperature of 330 degrees F rather than 340 degrees F used during the mix design testing, causing the project samples to fail the test. Citing Kelly v. Lovejoy, 172 M 516, 565 P2d 321 (1977), the District Court held that the state had waived the temperature requirements when it accepted the mix design sample at 340 degrees F and had therefore erroneously assessed price reductions for the samples tested at 330 degrees F. The Supreme Court noted that for the state to waive the right to enforce the contract, the acquiescence must be voluntary and intentional. By accepting one PMAC at 340 degrees F, unlike in Kelly, the state did not voluntarily and intentionally relinquish its right to enforce the contract specifications. Relinquishment may be proved either by express declaration or by a course of acts and conduct so as to induce the belief that the state's intention and purpose were to waive its rights. Evidence failed to show that the one-time acceptance was an intentional relinquishment of the right to enforce the contract specifications, nor was the one-time acceptance a course of conduct sufficient to induce the belief that the state's intention and purpose were to waive the temperature requirement mandated by the ring-and-ball softening point test. The District Court's finding of waiver was incorrect as a matter of law, constituting reversible error. Respondent's claims for breach of contract, fraud, and negligent misrepresentation and a motion for summary judgment were properly denied. Idaho Asphalt Supply v. St., 1999 MT 291, 297 M 66, 991 P2d 434, 56 St. Rep. 1168 (1999).

Question of Whether Contract Was Orally Modified Sufficient to Preclude Summary Judgment: For an oral contract to effectively alter the terms of a written contract, the oral agreement must be fully executed on both sides of the agreement. Whether Bernhard and his attorney agreed to permit Doble to continue logging Bernhard's property until all harvestable timber was removed, thereby agreeing to effectively extend the terms of the logging contract, was a question of material fact that precluded an award of summary judgment in Bernhard's favor. Doble v. Bernhard, 1998 MT 124, 289 M 80, 959 P2d 488, 55 St. Rep. 489 (1998).

Court Error in Modifying Clearing and Grubbing Contract: The District Court erred in: (1) substituting the subcontract price for the contract price in enforcing a highway clearing and grubbing contract that was assigned to the subcontractor; (2) awarding damages at the subcontract price rather than the contract price; (3) admitting testimony concerning custom and usage when the contract explicitly excluded its consideration in determining the area for which Topco was to be paid for clearing and grubbing; (4) determining the acreage measurement using horizontal distance rather than slope distance; and (5) failing to award the subcontractor compensation for acres cleared but not paid for. Topco, Inc. v. St., 275 M 352, 912 P2d 805, 53 St. Rep. 175 (1996).

Rights Under Written Contract Not Obliterated by Implied Obligation — Nonrenewal of Term Contract: Farris was hired under a term contract that lasted 1 year. The contract provided for nonrenewal with adequate notice. After signing term contracts for 3 consecutive years, Farris was notified that employment would be discontinued. Farris sought to invoke the implied covenant of good faith and fair dealing, contending that the employer's oral negotiations implied permanent employment and objective manifestations of job security. However, consideration of the oral negotiations was barred by the parol evidence rule of 28-2-904, under which oral stipulations are superseded by a written contract. Consideration of representations of permanent employment made after the contract was signed was barred by this section, which allows only written or executed oral agreement to affect the validity of a written contract. The Supreme Court cited Carma Developers v. Marathon Dev. Calif., Inc., 826 P2d 710 (Calif. 1992), for the proposition that no obligation can be implied that would result in the obliteration of a right expressly given under a written contract. In interpreting a contract, an implication should not be made when the contrary is indicated in clear and express words. Farris v. Hutchinson, 254 M 334, 838 P2d 374, 49 St. Rep. 717 (1992), distinguishing at-will dismissal under a written contract in Stark v. Circle K Corp., 230 M 468, 751 P2d 162 (1988), and Prout v. Sears, Roebuck & Co., 236 M 152, 772 P2d 288 (1989), and followed in Talley v. Flathead Valley Community College, 259 M 479, 857 P2d 701, 50 St. Rep. 889 (1993).

Elements Necessary to Show Waiver of Contractual Right of Nonwaiver: In determining if nonwaiver provisions of a contract should not be applied, not only must the evidence show a course of conduct by which one party waived the contractual obligations of the other party, but additionally the evidence should show that the same party also waived any right to rely on the nonwaiver provisions of his contract. Because waiver is a known and voluntary relinquishment of a known right, those elements of waiver at least have to appear from the evidence before it can be held that the contractual right of nonwaiver has been waived. Trustees of the Wash.-Idaho-Mont. Carpenters-Employers Retirement Trust Fund v. Galleria Partnership, 239 M 250, 780 P2d 608, 46 St. Rep. 1661 (1989).

Oral Waiver of Contract Requirements — Substantial Evidence to Support Jury Verdict: When the defendants failed to make four monthly payments on a contract for deed for the sale of a motel, the sellers sued to recover possession of the motel. The defendants counterclaimed for the payments they had made on the motel and for punitive damages on the grounds of "fraudulent malicious acts", contending that the sellers had orally waived the four monthly payments and ignored the notice provisions of the contract. The jury awarded a verdict of over $67,000 in favor of the defendants as actual damages and no punitive damages. The sellers appealed, alleging that the lower court erred by incorrectly stating the law in its jury instructions. The Supreme Court affirmed and held that the defendant's testimony regarding the sellers' alleged express waiver of the four payments is sufficient proof of the fact and sufficient evidence to support the jury verdict. Thiel v. Johnson, 219 M 271, 711 P2d 829, 42 St. Rep. 2010 (1985), followed in Holm-Sutherland Co., Inc. v. Shelby, 1999 MT 150, 295 M 65, 982 P2d 1053, 56 St. Rep. 595 (1999).

Addenda Complete and Final Agreement of Parties: Written addenda to construction contract, which stated the addenda and attached agreement and exhibits constituted the entire agreement between the parties, represented the complete and final agreement of the parties. The language to this effect in the addenda was unambiguous; the contract taken as a whole in its wording and phraseology is not reasonably subject to two different interpretations. Martin Dev. Co. v. Keeney Constr. Co, 216 M 212, 703 P2d 143, 42 St. Rep. 752 (1985). On a later appeal, the parties were bound by the facts and law established in this prior case. Relitigation of issues was barred by collateral estoppel, and claims of legal malpractice were barred by the statute of limitations. Peschel v. Jones, 232 M 516, 760 P2d 51, 45 St. Rep. 1244 (1988).

Alleged Oral Modification of Written Real Estate Contract Not Sufficient to Prevent Summary Judgment: Real estate agent sued to recover remainder of his broker's commission on sale of ranch which fell through. District Court granted agent summary judgment, and the Supreme Court affirmed. The Supreme Court found there were no material issues of fact in dispute, and an allegation that the agent orally waived the remainder of the fee in return for the opportunity to relist the property was insufficient to prevent summary judgment because the alleged waiver was not in writing. Taylor v. Weingart, 214 M 282, 693 P2d 1231, 41 St. Rep. 2474 (1984).

Offer Followed by Suggested Changes, Passage of Time, and Acceptance: Following oral modification of written lease to allow lessee to use additional space for additional rent, lessor sent lessee a new lease that incorporated the modification and was essentially the same as the current lease. Lessee's attorney suggested changes not accepted by lessor. Lessor did not revoke his offer of the new lease, and a few months later lessee told lessor on the phone that her attorney's changes were not important to her and she would sign and deliver the lease, which she did the next month. The attorney's suggested changes were not a rejection, the time between the suggestions and the delivery of the signed lease by lessee was not unreasonable under the circumstances and did not work a revocation of the offer of the new lease, and the new lease was executed when lessee signed and delivered it. Lemley v. Allen, 203 M 37, 659 P2d 262, 40 St. Rep. 279 (1983).

Waiver of Provision in Collective Bargaining Agreement Not Properly Before Court: A declaratory judgment action was brought to construe a collective bargaining agreement. The plaintiff filed a motion for summary judgment. The defendant opposed the motion and filed an affidavit in support of its opposition. The plaintiff argued that the affidavit submitted by defendant was inadmissible as a violation of the parol evidence rule. The trial court concluded that no material factual issue existed but denied the motion because of waiver by the plaintiff. The waiver issue was addressed in the affidavit but not in any of the other pleadings. The Supreme Court held that the waiver issue was not properly before the trial court and ordered the trial court to reconsider its denial of the motion for summary judgment. The Supreme Court also said that the defendant could amend its answer to affirmatively plead waiver. Butte Teachers' Union v. Bd. of Trustees, 201 M 482, 655 P2d 146, 39 St. Rep. 2248 (1982).

Contract for Sale — Change to Option Contract: Plaintiff and realtor authorized to sell lots for corporation executed a 1975 contract under which plaintiff deposited $500, would pay $5,000 upon payment to plaintiff at a future uncertain time of a bonus in that amount, and would pay the balance of the purchase price within 90 days of the $5,000 payment and be given title. The contract was later modified to provide that if the bonus was not paid by January 1, 1980, plaintiff could either purchase the lot by paying the balance of the purchase price beyond the deposit within 90 days or choose not to purchase and to receive back his deposit. The modification changed both parties' rights and obligations, and such changes constituted consideration for the modification. The benefits and obligations of the parties under the modification were sufficient to constitute a mutually binding contract. Naylor v. Hall, 201 M 59, 651 P2d 1010, 39 St. Rep. 1953 (1982).

Essentials of Contract Required: A contract may be modified by a subsequent agreement that complies with the requirements of a contract. Naylor v. Hall, 201 M 59, 651 P2d 1010, 39 St. Rep. 1953 (1982).

Articles of Partnership — Subsequent Contract: Articles of partnership provided for a partner's retirement and the disposition of his interest in the partnership. However, the plaintiff partner contracted to sell her interest to the partnership for an amount greater than that provided for in the articles. Since a later written contract may alter a former contract if both parties so agree, the articles of partnership do not control. Bridaham v. Moore, 199 M 161, 648 P2d 731, 39 St. Rep. 1233 (1982).

Contingent Fee Contract: A contingent fee contract providing that in event suit was instituted attorney would be entitled to 40% of any sums recovered is binding in absence of written contract or executed oral contract varying the original contract. Gross v. Holzworth, 151 M 179, 440 P2d 765 (1968).

Application of Section: This section applied to all written contracts and not only to those which are required to be in writing by the Statute of Frauds. Fiers v. Jacobson, 123 M 242, 211 P2d 968 (1949).

New Contract on Same Subject as Extinguishing Old: Where the parties to a contract make a new and independent agreement concerning the same matter as the original and the terms of the new contract are so inconsistent with those of the former that they cannot stand together, the new agreement may be construed to discharge the preceding one. Kester v. Nelson, 92 M 69, 10 P2d 379 (1932).

When Escrow May Modify Contract for a Deed: While a deed to land is an "agreement" which when delivered may modify a contract for the deed, a deed deposited in escrow is but an escrow, does not pass title, and can modify the contract only on a clear showing that the opposing party knew of the recitals in the deed and acceded thereto and that the deed and contract were parts of the same transaction. Hollensteiner v. Anderson, 78 M 122, 252 P 796 (1927).

Presumption on Appeal: A contract which must have been in writing in order to be effective will be presumed on appeal to have been in writing, nothing to the contrary appearing in the record. Hurley v. Great Falls Baseball Ass'n, 59 M 21, 195 P 559 (1921).

Attorney General's Opinions

Termination of Payments in Lieu of Participation in Group Health Plan for Nonunion County Employee: The Board of County Commissioners may terminate payments in lieu of participation in a group health plan for a nonunion county employee only if termination is consistent with the county's employment agreement with the employee. 51 A.G. Op. 11 (2005).

When Collective Bargaining Agreement That Includes Payments in Lieu of Group Health Plan Participation May Be Altered: When a collective bargaining agreement includes a provision for payments to county employees in lieu of participation in a group health plan, that provision may not be altered by the Board of County Commissioners without the written agreement of the collective bargaining unit. 51 A.G. Op. 11 (2005). See also 43 A.G. Op. 79 (1990).

Law Review Articles

Modification of Written Contracts, Brown, 10 Mont. L. Rev. 63 (1949).

28-2-1611. When written contract may be revised by court.

Case Notes

Mutual Mistake 298
Mistake by One Party 300
Fraud 301
General 302

MUTUAL MISTAKE

Extrinsic Evidence Permissible Based on Parties' Intent — Intent Defeated by Mistakes in Vital Facts: The District Court did not err by considering extrinsic evidence to interpret and reform the parties' contract. Generally, when the terms of an agreement are reduced to writing by the parties, the writing is considered as containing all those terms and there can be no evidence of the terms of the agreement other than the contents of the writing. However, an exception to this rule permits extrinsic evidence to be admitted when a mistake or other imperfection of the writing is put at issue. The District Court correctly concluded that the recorded agreement did not reflect the parties' intent. The mistakes in the agreement constituted "vital facts" that defeated the parties' contractual intentions. It was therefore appropriate for the District Court to consider extrinsic evidence and to reform the contract to reflect the parties' true intent. In re Platt, 2018 MT 43, 390 Mont. 338, 413 P.3d 818.

Extrinsic Evidence Properly Admitted to Prove Original Contract Intent — Reformation of Warranty Deed Based on Mutual Mistake Proper: Extrinsic evidence provided by plaintiffs to prove the parties' original intent in entering a buy-sell agreement proved that, by virtue of a mutual mistake, the deed did not contain agreed-upon restrictions. The evidence was squarely within the exception to the parol evidence rule, and the District Court did not err in admitting the parol evidence or in reforming the deed to include the restrictions and enforcing the restrictions against defendants. Thibodeau v. Bechtold, 2008 MT 412, 347 M 277, 198 P3d 785 (2008), following Interstate Prod. Credit Ass'n v. DeSaye, 250 M 320, 820 P2d 1285 (1991).

Standard of Proof Applicable to Reformation of Contract: A party urging reformation of a contract must overcome the presumption that the writing contains the final agreement of the parties and expresses their real purpose and intent. The correct standard of proof for reformation is clear, convincing, and satisfactory proof. Story v. Bozeman, 259 M 207, 856 P2d 202, 50 St. Rep. 761 (1993), distinguishing Reilly v. Maw, 146 M 145, 405 P2d 440 (1965).

Purchase Money Mortgages — Reformation: The bank prepared a mortgage from the buyer to the sellers and a deed of trust from the buyer to the bank as a service to and at the request of the buyer and the sellers. The bank inadvertently inserted the term "no exceptions" into the mortgage through a typographical error. Upon default of the buyer, the sellers filed an action for declaratory ruling that their purchase money mortgage was prior in time and right to the bank's deed of trust. The trial court reformed the sellers' mortgage to delete the term "no exceptions" and held that the bank's deed of trust was prior in time and right to the mortgage. The Supreme Court affirmed. The bank's mistake, while negligent, did not amount to neglect of a legal duty that would preclude reformation. The mistake was mutual because the mortgage as written did not reflect the mutual intentions of the parties which, the evidence indicated, were for the bank to receive a first mortgage and the sellers to receive a second mortgage. Pulse v. N. Am. Land Title Co. of Mont., 218 M 275, 707 P2d 1105, 42 St. Rep. 1578 (1985).

Deed Reserving Mineral Interest to County — No Mutual Mistake: A 1944 deed reserved a mineral interest to the county. The deed did not on its face indicate mutual mistake; the parties agreed in 1977 that the 1944 deed reserved a royalty, and not one of the interested parties claimed mutual mistake. Plaintiff did not overcome the presumption that the 1944 deed contained the final agreement of the parties. McSweyn v. Musselshell County, 193 M 525, 632 P2d 1095, 38 St. Rep. 1260 (1981).

Mistake as to Ownership: Where a deed reserved to the grantors the right to all the minerals, subject only to the right of grantee to receive half the royalties, the fact that grantors owned the mineral rights on only half the tract conveyed did not furnish ground for reformation in the absence of a showing of mutual mistake as to the extent of the grantor's ownership of minerals. Crawford v. Griffith, 137 M 140, 351 P2d 223 (1960).

When Reformation Lies for Mutual Mistake: Where both parties to a mortgage intended that it should cover all the lands of a livestock company, mortgagor, but stenographer of the mortgagee's attorney who prepared the document, in copying the description of the lands inadvertently omitted a tract of 440 acres of the total of 2,600 and the mistake was not discovered until shortly before commencement of the action to reform the mortgage and enforce it as reformed, the evidence was sufficient to warrant reformation. Clack v. Clack, 98 M 552, 41 P2d 32 (1935).

Equity Court: Where the parties to a contract agree upon its terms and conditions and through mutual mistake the writing signed by them fails to express their agreement, a court of equity will reform it. Clack v. Clack, 98 M 552, 41 P2d 32 (1935).

Proof Required for Mutual Mistake: To warrant reformation of a written instrument for mistake, it must appear that the parties agreed upon a certain contract, that they executed it, that the contract executed was not the one agreed upon, that the variance occurred by mistake, in what the mistake consisted, and that it was mutual. Thielbar Realties, Inc. v. Nat'l Union Fire Ins. Co., 91 M 525, 9 P2d 469 (1932).

Mistake to Be Common and Reciprocal: The mutual mistake for which a written instrument may be reformed must be reciprocal and common to both parties, each alike laboring under the same misconception. Theilbar Realties, Inc. v. Nat'l Union Fire Ins. Co., 91 M 525, 9 P2d 469 (1932).

Promissory Note: The rule declared by this section that a written contract which through mutual mistake does not truly express the intention of the parties may be reformed applies to a promissory note executed by the officers of a corporation for a company debt but which by such mistake made it their own obligation instead of their principal's. Bitter Root Creamery Co. v. Muntzer, 90 M 77, 300 P 251 (1931).

Fire Insurance Policy: Where reformation of a fire insurance policy was sought on the ground of a mutual mistake on the part of the insured and the agent of the insurer relative to the answer to the question in the application whether the building insured stood upon ground not owned by the insured, the evidence showing that plaintiff was unable to read the English language and that he advised the agent that he did not own the land but was assured that the policy "was all right", there was a sufficient showing that the mistake was mutual, within this meaning of this section. Krpan v. Cent. Fed. Fire Ins. Co., 87 M 345, 287 P 217 (1930).

Reliance on Another Document: Under this section, authorizing the reformation of a contract when through mutual mistake it does not truly express the intention of the parties, the court in a mortgage foreclosure suit properly excluded one of a number of lots described by number, where it was apparent that the mortgagor did not intend to include it and the attorney of the mortgagee who drew it, in following the descriptions given in another mortgage, inadvertently added the number of the lot excluded, the circumstances having been such as to excuse the negligence of the mortgagor in failing to read the mortgage before signing it. First St. Bank v. Mussigbrod, 83 M 68, 271 P 695 (1928).

Burden of Proof: The party who seeks to revise or reform a written instrument on the ground of a mutual mistake of the parties has the burden of establishing such mistake by clear, convincing, and satisfactory evidence if he would overcome the presumption that the writing contains their final agreement and expresses their real purpose and intent. August v. Burns, 79 M 198, 255 P 737 (1927).

Evidence to Be Presented: Before equity will intervene to correct an alleged mutual mistake in a written instrument the evidence of the mistake must be clear, convincing, and satisfactory. Humble v. St. John, 72 M 519, 234 P 475 (1925).

MISTAKE BY ONE PARTY

Competitive Bidding — Contract Formed by Execution of Written Instrument, Not by Award of Project — No Requirement That State Be Notified of Bidding Error Prior to Award of Project: After E.H. Oftedal and Sons, Inc. (Oftedal), submitted a bid on a highway project, but before the actual contract was signed, Oftedal notified the state that $789,000 in errors had been discovered. Oftedal requested that the bid be withdrawn or that the contract amount be adjusted upward, but the requests were denied. Oftedal appealed, but the District Court held that Oftedal did not give timely notice of the mistakes prior to the acceptance of the bid, so equitable relief was unavailable under this section. The Supreme Court disagreed and reversed. As a matter of law, no contract for performance of the highway project was formed by the award of the project, prior to execution of the written contract, so there could be no requirement that the state have knowledge of Oftedal's unilateral mistake prior to the award of the project. No notice of the mistake was necessary at that time to obtain equitable relief under this section. E.H. Oftedal & Sons, Inc. v. St., 2002 MT 1, 308 M 50, 40 P3d 349 (2002), distinguishing Baker v. St., 218 M 235, 707 P2d 20 (1985).

Equitable Relief Available to Correct Inadvertent Bidding Errors in Revising Highway Construction Project: Contractor E.H. Oftedal and Sons, Inc. (Oftedal), submitted a bid on a Montana highway project. Because Oftedal's was the lowest bid, the state awarded the contract to Oftedal, but upon later investigation, Oftedal determined that the bid contained several errors amounting to $789,000, and requested that the bid be withdrawn. The request was denied, so Oftedal requested an upward revision of the bid to reflect the mistakes. Even if the contract amount was revised upward to reflect the errors, Oftedal's bid would still have been lowest. Although the state recognized that Oftedal had made an unintended mistake, the request for upward revision was also denied, in part because the Federal Highway Administration would not allow any federal money to be used to cover any state cost over Oftedal's original bid. To avoid losing its substantial bid bond, Oftedal signed the contract under protest for the original amount and petitioned the District Court for equitable relief under this section through an upward revision of the contract sum. The District Court denied relief and granted summary judgment to the state. Oftedal appealed to the Supreme Court, seeking an upward revision to reflect the amount of the error and an order for specific performance of the revised contract. The Supreme Court found that equitable relief was appropriate because of mistake, and remanded to the

District Court with instructions to reform the contract to reflect the true intentions of the parties. The mistakes in this case were inadvertent, and even though some negligence might have been inherent in the mistakes, they could not be said to preclude equitable relief when viewed in light of the parties' agreed assessment of the nature of the errors. Negligence of the party creating the mistake is not necessarily a bar to judicial reformation of a contract. Under 28-2-1612, for the purpose of revising a contract, a court must presume that all parties intended to make an equitable and conscientious agreement, and it could not be presumed that either party intended Oftedal to incur the hardship of supplying $789,000 of work and material to the state without compensation. E.H. Oftedal & Sons, Inc. v. St., 2002 MT 1, 308 M 50, 40 P3d 349 (2002).

Unambiguous Contract Description — Applicability of Parol Evidence Rule — Unilateral Mistake: Since a 1971 written agreement was not ambiguous with respect to the land it affected, the parol evidence rule prevented admission of evidence of a 1967 oral agreement to show intent of the parties as to what land was involved. Admission of the oral agreement would only have provided evidence of unilateral mistake, which is not grounds for reforming a written contract. Haggerty v. Gallatin County, 221 M 109, 717 P2d 550, 43 St. Rep. 674 (1986).

Essentials for Reformation: Where plaintiff knew that defendant was acting under a mistake with regard to a writing, he was not entitled to revision on the ground of mistake. Schillinger v. Huber, 133 M 80, 320 P2d 346 (1958), followed in Story v. Bozeman, 259 M 207, 856 P2d 202, 50 St. Rep. 761 (1993), and Goodman Realty, Inc. v. Monson, 267 M 228, 883 P2d 121, 51 St. Rep. 1074 (1994).

Effect of Negligence on Reformation: Every mistake for which an instrument may be reformed involves the idea of negligence in greater or less degree, and if the negligence in failing to read the instrument is excusable under the circumstances, as where the person charged with negligence was of foreign extraction unable to read English well, and no rights of innocent third persons are involved, reformation may be had. Bitter Root Creamery Co. v. Muntzer, 90 M 77, 300 P 251 (1931).

Extent of Remedy: This section provides for the reformation of instruments on the ground of the mutual mistake of the parties. Section 28-3-304 declares that when through mistake a written contract fails to express the real intention of the parties, such intention is to be regarded and the erroneous part of the writing disregarded. Although a voluntary conveyance is unilateral and therefore lacks in mutuality, a court of equity under its inherent power and 28-3-304 may grant reformation of a deed evidencing such a conveyance even though the mistake was not mutual. Laundreville v. Mero, 86 M 43, 281 P 749 (1929).

Excusable Negligence: The mere fact that a party seeking a reformation of an instrument on the ground of mistake may himself have been negligent is not a ground for refusing relief; if the negligence is excusable, as where plaintiff is an old man and not accustomed to transact business and defendant a much younger man of extensive business experience, relief will be granted when, in view of all the circumstances, to deny it would permit plaintiff to suffer a gross wrong at the hands of defendant. Ayers v. Buswell, 73 M 518, 238 P 591 (1925).

Reformation Not to Lie for Unilateral Mistake: Where a mistake in an instrument was unilateral, i.e., made only by one party to it, and not mutual or one which the other party by it knew or suspected, reformation did not lie. Comerford v. USF&G Co., 59 M 243, 196 P 984 (1921).

Allegation of Mistake: In an action to reform a contract the complaint should allege some mistake in the making of the contract or some mistake or inadvertence in reducing its terms to writing. Gaffney Mercantile Co. v. Hopkins, 21 M 13, 52 P 561 (1898).

FRAUD

Sufficiency of Pleadings and Proof: The defendant sold real estate to plaintiff on a contract for deed, and the District Court reformed the contract, finding fraud by defendant in orally misrepresenting that there were three good wells on the property, that ownership of a cabin on the property would transfer with the property, and that he would survey or provide papers concerning the boundary of the property. The Supreme Court reversed, finding no basis for fraud in that: (1) the water in the wells had never been tested and proven unfit for use, and the lack of pumps on two wells was obvious from visual inspection at the time the contract was entered; (2) plaintiff had, on a verified complaint, in fact acknowledged defendant's continuing ownership of the cabin, contrary to her testimony and the District Court's finding; and (3) plaintiff never alleged that a survey was to be performed, contrary to the District Court's findings, and plaintiff could have easily ascertained the boundaries by looking at an existing survey and talking with a neighbor. Krone v. McCann, 197 M 380, 642 P2d 584, 39 St. Rep. 500 (1982). See also Fossen v. Fossen, 2013 MT 299, 372 Mont. 175, 311 P.3d 743.

Independent Investigation Clause Not to Preclude Justifiable Reliance on Representations: Defendants owned property in Flathead County. Water for the property came from a neighbor's well for which they paid him $8 per month. No written agreement existed concerning the water supply. Defendants listed the property for sale with Tri-City Real Estate. Inserted in the listing contract in the printed space following "water" were the words "community $8/mo." Plaintiffs were interested in the land and looked at it. They asked both defendants and the realtor about the water supply and were told it came from a community well. Plaintiffs wanted written verification of the interest in the water system. The realtor told them he would obtain a copy of the register of the well for them. Plaintiffs continued asking for the register but never received it. Plaintiffs signed a contract for deed to buy the property which had been prepared by the realtor's attorney. The contract contained an "independent investigation" clause, which stated that plaintiffs had investigated the property and entered the contract based upon that investigation and that there were no other agreements or representations concerning the property. The neighbor stopped supplying water, and plaintiffs were forced to dig their own well. They sought recovery from defendants. It was held that defendants were responsible for the negligence of their agents in the sale as related to the community water interest. The Supreme Court held that the "independent investigation" clause did not preclude a holding that the plaintiffs justifiably relied on the representations of the realtor. Parkhill v. Fuselier, 194 M 415, 632 P2d 1132, 38 St. Rep. 1424 (1981), distinguished in Garrison v. Averill, 282 M 508, 938 P2d 702, 54 St. Rep. 454 (1997).

Assignment of Royalty Interest: Where a landowner induced by the fraud of the person with whom he was contracting assigned a 1/32 royalty interest instead of an undivided 1/32 interest in and to minerals under and upon his lands, the assignment will be reformed, amended, and corrected by the courts to correctly embody the agreement of the parties. Carroll v. Funk, 222 F2d 508 (9th Cir. 1955).

Not Exclusive Remedy: Neither the remedy afforded by 28-2-1711, giving a party to a contract the right to rescind on the ground of fraud, among others, nor that granted by this section, under which he may have the contract reformed on the same ground, is exclusive, each being independent of the other; hence the defrauded party may elect to pursue either remedy. Campana v. Dobry, 69 M 240, 221 P 540 (1923).

GENERAL

Reformation of Insurance Policy Not Permitted — Clear and Explicit Language Used — Lack of Due Diligence in Discovering Error Not Justifying Reformation: An insurer attempted to reform an insurance policy on the ground that the policy should not cover property near a structure that was specifically exempted from the policy. However, the policy specifically included property within 1,000 feet of other insured property, including property around the exempted structure. The District Court applied 33-15-302 and determined that it was prohibited from reforming insurance policies. On appeal, the Supreme Court also declined to reform the contract, as the language was clear and explicit, due diligence would have uncovered the error, and the insurer failed to establish that its insurance policy expressed something other than what the parties mutually intended. Lincoln County Port Authority v. Allianz Global Risks US Ins. Co., 2013 MT 365, 373 Mont. 60, 315 P.3d 934.

Request for New Beneficiary Not Appropriate Use of Reformation — Summary Judgment Properly Granted to Stepson: Reformation does not permit the court to create an entirely new contract. In this case, the petitioner asked the court to name her as an entirely new beneficiary, which would be a substantial addition resulting in a new contract. This request went beyond what is permitted by way of reformation. Section 28-3-304 governs the interpretation of contracts, not their reformation, and was properly applied here; however, the standard for disregarding a writing contained in 28-3-304 was not met because the evidence showed the decedent intended to list his estate as his contingent beneficiary, so the District Court properly granted summary judgment to the decedent's stepson. In re Estate of Irvine, 2013 MT 271, 372 Mont. 49, 309 P.3d 986.

Public Contracts Subject to Fundamental Contract Analysis — Public Bidding and Contract Modification Statutes Not Inherently Inconsistent: Public contracts are not necessarily exempt from fundamental contract analysis because competitive bidding statutes were established for the benefit of the public rather than to establish the rights of bidders. Nothing in the competitive bidding statutes places public contracts out of reach of remedies at law or the equitable relief provided under this section if a party is otherwise qualified for relief under the terms of the statute. Further, public bidding statutes and contract modification statutes are not inherently inconsistent, so this section may be applied to public contracts. E.H. Oftedal & Sons, Inc. v. St., 2002 MT 1, 308 M 50, 40 P3d 349 (2002).

Modification of Property Settlement Resulting in Conflicting Provisions — Interpretation Giving Effect, Not Voidness, Preferred: The original property settlement agreement provided that husband and wife would divide equally the proceeds from the sale of their house. An escrow agreement, signed by all parties, later assigned the balances on a percentage basis, 72% to wife and 28% to husband, and further provided that wife would receive a total of $30,000 from the net proceeds of the sale. However, the percentage amount did not approximate the total amount. Husband contended that because the conflicting portions could not be taken together so as to give effect to every part of the contract and the intention of the parties, the modification should be voided and the original equal division contained in the dissolution should rule. The District Court inquired as to the instrument's intent and its legal consequences, favoring effect over voidness. The court properly confined its inquiry to the language of the instrument and held that the 72/28 provision ruled. The interpretation was reasonable and within the scope of the court's inquiry. In re Marriage of Bourque, 241 M 38, 785 P2d 699, 47 St. Rep. 64 (1990).

Effect of Unanticipated Condition on Contractor's Obligation: Even though a contract incorporates by reference federal, state, or local laws, a contractor is not required to alter construction plans to comply with health standards when the condition to be alleviated is abnormal, unanticipated, or substantially different from those in the contract plans and drawings. Ace Plumbing & Heating, Inc. v. School District, 204 M 81, 662 P2d 1327, 40 St. Rep. 678 (1983).

Merger of Conveyance Agreement Description Into Later Deed: There was a discrepancy between the descriptions of real property contained in an agreement to convey property and a later deed that purported to convey the same property. Where transferees were aware of the discrepancy for 12 years and did nothing to correct it, the agreement was merged into the deed and there were no grounds for reformation of the deed. Tillotsen v. Frazer, 199 M 342, 649 P2d 744, 39 St. Rep. 1442 (1982).

Certainty of Option Contract — Specific Performance of Reformed Contract: Where the plaintiff and defendant entered into an option contract giving the plaintiff an option to purchase certain real estate but the parties failed to specify the interest which would be retained by the defendant in certain improvements and failed to specify the dates upon which the downpayment and annual payments would be made and the date upon which interest would accrue, the contract was nonetheless sufficiently definite to allow its enforcement by specific performance. At trial, the court took testimony of the parties and reformed the contract so as to make it sufficiently definite as to the defendant's retained interest to allow specific performance. The fact that certain dates were not specified is not fatal to the contract, as it need not be absolutely certain in every detail, and where a time of performance is not specified, a reasonable time will be implied. Keaster v. Bozik, 191 M 293, 623 P2d 1376, 38 St. Rep. 194 (1981).

Regret Not Grounds for Avoiding Obligation: Courts must interpret contracts as they are made by the parties, not make new ones for them, no matter how unreasonable terms may appear after they have been consummated. Merely because the plaintiffs in an oil and gas lease may have reason to regret their bargain affords them no ground to avoid the obligation assumed. Fey v. A. A. Oil Corp., 129 M 300, 285 P2d 578 (1955).

Defect in Complaint Cured by Answer: Where defendant by his answer and cross-complaint alleged that he was a purchaser of the land in good faith for value and without notice of any adverse interest held by plaintiffs and this was denied in reply and answer of plaintiff, defendants supplied the issue of good faith and cannot complain of the absence of an allegation in the complaint that defendant was not a purchaser in good faith. Strack v. Fed. Land Bank of Spokane, 124 M 19, 218 P2d 1052 (1950).

Intention of Parties: Proof that failure of contract to express true intention of the parties was the result of fraud, mutual mistake, or a mistake of one party which the other at the time knew or suspected is necessary to warrant reformation of a written contract. Brubaker v. D'Orazi, 120 M 22, 179 P2d 538 (1947).

When Acquiescence in Contract Destroys Right of Reformation: Under the rule that acquiescence in a contract after learning that it does not represent the actual agreement destroys the right of reformation, where purchasers of land included in an irrigation district entered into the contract of purchase under alleged false representations by the vendor that the lands were not subject to liens for payment of bonds issued by the district and paid assessments for 10 years without protest, they will be held to have acquiesced in the contract, barring the right of reformation. Krueger v. Morris, 110 M 559, 107 P2d 142 (1940).

Judgment Lien Acquired After Execution of Mortgage No Bar to Reformation: The lien of a judgment is a general one and must yield to all prior equitable titles in others; hence such a lien acquired between the date of the execution of a mortgage and the bringing of an action to reform the instrument and foreclose it as reformed does not stand in the way of granting such relief. Clack v. Clack, 98 M 552, 41 P2d 32 (1935).

Oral Preceding Agreement: If a party claims that a written contract does not correctly state the true terms of the agreement, he must have it reformed and recover on it as reformed, if at all; but he cannot recover on an oral preceding agreement differing from that which was reduced to writing. Biering v. Ringling, 78 M 145, 252 P 872 (1927).

No Culpable Negligence: Reformation of an instrument will not be decreed on the ground of mistake unless the real intent of the parties is satisfactorily shown and the party seeking the relief was free from culpable negligence. Comerford v. USF&G Co., 59 M 243, 196 P 984 (1921), explained in Ayers v. Buswell, 73 M 518, 238 P 591 (1925).

Court Not to Insert Provisions: The purpose of the equity of reformation is not to make a new agreement but to establish and perpetuate the true one, and courts cannot insert a provision which was omitted with the consent of the party asking reformation, although such consent was given in reliance on an oral promise of the other party that the omission should not make any difference. Comerford v. USF&G Co., 59 M 243, 196 P 984 (1921).

28-2-1612. Presumption that parties intended equitable agreement.

Case Notes

Extrinsic Evidence Permissible Based on Parties' Intent — Intent Defeated by Mistakes in Vital Facts: The District Court did not err by considering extrinsic evidence to interpret and reform the parties' contract. Generally, when the terms of an agreement are reduced to writing by the parties, the writing is considered as containing all those terms and there can be no evidence of the terms of the agreement other than the contents of the writing. However, an exception to this rule permits extrinsic evidence to be admitted when a mistake or other imperfection of the writing is put at issue. The District Court correctly concluded that the recorded agreement did not reflect the parties' intent. The mistakes in the agreement constituted "vital facts" that defeated the parties' contractual intentions. It was therefore appropriate for the District Court to consider extrinsic evidence and to reform the contract to reflect the parties' true intent. In re Platt, 2018 MT 43, 390 Mont. 338, 413 P.3d 818.

Equitable Relief Available to Correct Inadvertent Bidding Errors in Revising Highway Construction Project: Contractor E.H. Oftedal and Sons, Inc. (Oftedal), submitted a bid on a Montana highway project. Because Oftedal's was the lowest bid, the state awarded the contract to Oftedal, but upon later investigation, Oftedal determined that the bid contained several errors amounting to $789,000, and requested that the bid be withdrawn. The request was denied, so Oftedal requested an upward revision of the bid to reflect the mistakes. Even if the contract amount was revised upward to reflect the errors, Oftedal's bid would still have been lowest. Although the state recognized that Oftedal had made an unintended mistake, the request for upward revision was also denied, in part because the Federal Highway Administration would not allow any federal money to be used to cover any state cost over Oftedal's original bid. To avoid losing its substantial bid bond, Oftedal signed the contract under protest for the original amount and petitioned the District Court for equitable relief under 28-2-1611 through an upward revision of the contract sum. The District Court denied relief and granted summary judgment to the state. Oftedal appealed to the Supreme Court, seeking an upward revision to reflect the amount of the error and an order for specific performance of the revised contract. The Supreme Court found that equitable relief was appropriate because of mistake, and remanded to the District Court with instructions to reform the contract to reflect the true intentions of the parties. The mistakes in this case were inadvertent, and even though some negligence might have been inherent in the mistakes, they could not be said to preclude equitable relief when viewed in light of the parties' agreed assessment of the nature of the errors. Negligence of the party creating the mistake is not necessarily a bar to judicial reformation of a contract. Under this section, for the purpose of revising a contract, a court must presume that all parties intended to make an equitable and conscientious agreement, and it could not be presumed that either party intended Oftedal to incur the hardship of supplying $789,000 of work and material to the state without compensation. E.H. Oftedal & Sons, Inc. v. St., 2002 MT 1, 308 M 50, 40 P3d 349 (2002).

U.C.C. Unconscionability Provision — Application to Leases: The Montana Uniform Commercial Code provision relating to unconscionable sales contracts (30-2-302) can, at least by analogy, be applied to lease transactions and should guide the Supreme Court in determining whether a lease is unconscionable. All-States Leasing Co. v. Top Hat Lounge, 198 M 1, 649 P2d 1250, 39 St. Rep. 425 (1982).

Unconscionability — Leases Between Businessmen: Courts have readily applied the doctrine of unconscionability of contracts as between consumers and businessmen but are reluctant to rewrite the terms of a contract between businessmen themselves. When, as in instant case, all provisions of a lease are agreed to by businessmen on both sides, none of the surrounding circumstances suggest oppression of lessee's freedom to select another lessor, nothing on the record suggests disparity of bargaining power, and lessee selected both the equipment leased and the supplier of the equipment to the lessor and notified lessor of lessee's desire to make the lease, the lease cannot be considered unconscionable. All-States Leasing Co. v. Top Hat Lounge, 198 M 1, 649 P2d 1250, 39 St. Rep. 425 (1982).

Unconscionability — Success of Unsupported Claim: The mere unsupported claim that equipment lease under which appellants were sued was unconscionable and that a more oppressive lease was hard to imagine could not succeed on appeal from summary judgment for delinquent payments under lease. All-States Leasing Co. v. Top Hat Lounge, 198 M 1, 649 P2d 1250, 39 St. Rep. 425 (1982).

Contract for Deed — Forfeiture — Notice to Persons With Interest: A contract for deed was executed between Morin, the seller, and Roberts, the buyer. Later, Roberts entered into a second contract selling the property to Iverson. The second contract provided that Iverson would assume Roberts' obligation to Morin, and upon completion of Iverson's obligation to Roberts, Roberts would assign his interest in the Morin contract to Iverson. Iverson defaulted on the Morin contract, and Morin sent a notice of default to Iverson but not to Roberts. When Roberts learned of the default he offered to cure. Morin refused the offer, seeking instead to enforce the forfeiture provision of the contract, thereby regaining the property, which had greatly increased in value. The court found that this situation is similar to the purchaser in an executory real estate contract who mortgages his interest. In that case the mortgagee is entitled to notice of forfeiture if the seller knows of the mortgage and the mortgagee has the right to tender payment to the seller necessary to protect his security. Roberts v. Morin, 198 M 233, 645 P2d 423, 39 St. Rep. 892 (1982).

Mineral Rights: Grantors seeking reformation of deeds by which they retained portions of landowners' mineral royalties were not entitled to relief where evidence did not show that deeds contained no provision reserving all mineral and leasing rights in grantors. Voyta v. Clonts, 134 M 156, 328 P2d 655 (1958).

Law Review Articles

Presumptions Concerning Contracts, Clarke, 37 Mont. L. Rev. 101, 111 (1976).

28-2-1613. Scope of court's inquiry.

Case Notes

Equitable Relief Available to Correct Inadvertent Bidding Errors in Revising Highway Construction Project: Contractor E.H. Oftedal and Sons, Inc. (Oftedal), submitted a bid on a Montana highway project. Because Oftedal's was the lowest bid, the state awarded the contract to Oftedal, but upon later investigation, Oftedal determined that the bid contained several errors amounting to $789,000, and requested that the bid be withdrawn. The request was denied, so Oftedal requested an upward revision of the bid to reflect the mistakes. Even if the contract amount was revised upward to reflect the errors, Oftedal's bid would still have been lowest. Although the state recognized that Oftedal had made an unintended mistake, the request for upward revision was also denied, in part because the Federal Highway Administration would not allow any federal money to be used to cover any state cost over Oftedal's original bid. To avoid losing its substantial bid bond, Oftedal signed the contract under protest for the original amount and petitioned the District Court for equitable relief under 28-2-1611 through an upward revision of the contract sum. The District Court denied relief and granted summary judgment to the state. Oftedal appealed to the Supreme Court, seeking an upward revision to reflect the amount of the error and an order for specific performance of the revised contract. The Supreme Court found that equitable relief was appropriate because of mistake, and remanded to the District Court with instructions to reform the contract to reflect the true intentions of the parties. The mistakes in this case were inadvertent, and even though some negligence might have been inherent in the mistakes, they could not be said to preclude equitable relief when viewed in light of the parties' agreed assessment of the nature of the errors. Negligence of the party creating the mistake is not necessarily a bar to judicial reformation of a contract. Under 28-2-1612, for the purpose of revising a contract, a court must presume that all parties intended to make an equitable and conscientious agreement, and it could not be presumed that either party intended Oftedal to incur the hardship of supplying $789,000 of work and material to the state without compensation. E.H. Oftedal & Sons, Inc. v. St., 2002 MT 1, 308 M 50, 40 P3d 349 (2002).

Modification of Property Settlement Resulting in Conflicting Provisions — Interpretation Giving Effect, Not Voidness, Preferred: The original property settlement agreement provided that husband and wife would divide equally the proceeds from the sale of their house. An escrow agreement, signed by all parties, later assigned the balances on a percentage basis, 72% to wife and 28% to husband, and further provided that wife would receive a total of $30,000 from the net proceeds of the sale. However, the percentage amount did not approximate the total amount. Husband contended that because the conflicting portions could not be taken together so as to give effect to every part of the contract and the intention of the parties, the modification should be voided and the original equal division contained in the dissolution should rule. The District Court inquired as to the instrument's intent and its legal consequences, favoring effect over voidness. The court properly confined its inquiry to the language of the instrument and held that the 72/28 provision ruled. The interpretation was reasonable and within the scope of the court's inquiry. In re Marriage of Bourque, 241 M 38, 785 P2d 699, 47 St. Rep. 64 (1990).

Power of Court to Reform a Contract: The court may make the contract express the real intent of the parties as it existed when the contract was entered into but it may not make an entirely new agreement. In this case, the District Court properly ordered an accounting, scheduled a new option to purchase date, and set up a new payment schedule as these adjustments were necessary to make specific performance possible. However the District Court erred by adding new rights and obligations requiring the plaintiff to execute a promissory note and real estate mortgage. Rogers v. Relyea, 184 M 1, 601 P2d 37 (1979).

Reformation of Terms Entered by Mistake: If the parties to a contract agree upon terms and conditions named by them, and through mistake the writing embodying the agreement signed by them, or either of them, fails to express the agreement as made, or includes therein terms and conditions not agreed upon, the result is that there is no contract between them. Under such circumstances a court of equity will reform the written evidence of the contract so as to make it express the terms of the agreement as actually fixed by the parties. Parchen v. Chessman, 49 M 326, 142 P 631 (1914).

Part 17
Extinction of Contracts — Rescission

Part Case Notes

Party Entitled to Seek Damages for Breach of Terminated Contract for Damages Incurred Prior to Termination: The Whites entered into a construction contract with Longley for the construction of their home. After failing to perform under the terms of the contract, Longley persuaded the Whites to buy him out of the contract for $30,000 and to let him continue to build the home without a contract. Subsequently, Longley failed to build a house that could be occupied. Longley argued that the trial court had incorrectly based part of the damages awarded to the Whites on the original contract, which had been terminated. The Supreme Court held that after the termination the Whites were still entitled to recover for any damages they had suffered prior to the termination and could rely on the terms of that contract in determining their damages. White v. Longley, 2010 MT 254, 358 Mont. 268, 244 P.3d 753.

Rescission of Waiver of Interest Document on Grounds of Fraud: Kindsfather's son purchased some land from Kindsfather pursuant to a contract for deed. When the son was unable to make the payments, the son executed a document waiving the back interest that was owing and Kindsfather signed the document. Kindsfather subsequently died, and the son sought a declaratory ruling that the waiver of interest document was valid and that upon receipt of the unpaid balance of the contract, the bank would release the warranty deed held in escrow for the son. Kindsfather's personal representative opposed the judgment, and the District Court found the document to be invalid and ordered the son to make all payments due to the estate. On appeal, the Supreme Court affirmed the District Court's decision to rescind the document because it was obtained by fraud. The Supreme Court examined each of the nine elements of actual fraud and determined that a prima facie case of actual fraud was established. In re Estate of Kindsfather, 2005 MT 51, 326 M 192, 108 P3d 487 (2005), following Davis v. Church of Jesus Christ of Latter Day Saints, 258 M 286, 852 P2d 640 (1993).

Federal Law Regarding Nonliability for Borrower's Payment of Fees to Lender Upon Loan Rescission Inapplicable to Mortgage Broker Fees: Plaintiff helped defendant secure a loan, which defendant subsequently rescinded within the applicable 3-day period pursuant to the federal

Truth in Lending Act. Plaintiff sent defendant a bill for its brokerage fee and out-of-pocket expenses incurred in securing the loan commitment, as provided in the brokerage contract and an attendant promissory note. Defendant refused to pay the bill, and plaintiff brought an action to enforce the contract and promissory note, and the District Court enforced the note and ordered defendant to pay the bill. Defendant appealed on grounds that 16 U.S.C. 1635(b) of the Truth in Lending Act and 12 CFR 226.23, Regulation Z, clearly provide that when a consumer rescinds a transaction, the consumer is not liable for any amount, including any finance charge. The Supreme Court affirmed the District Court ruling. Although the federal law protects defendant from paying any fees to the lender, it does not address arrangements between a borrower and a mortgage broker, and in fact, portions of Regulation Z at 12 CFR 226.4(a) expressly exclude appraisal and service fees from the definition of a finance charge. Therefore, even though defendant effectively rescinded that mortgage with the lender, the rescission did not affect or alter defendant's obligation to the mortgage broker pursuant to the brokerage contract and promissory note. Mortgage Source, Inc. v. Strong, 2003 MT 205, 317 M 37, 75 P3d 304 (2003).

Unenforceability of Buy-Sell Agreement on Grounds of Impossibility or Impracticality of Performance — Requiring Performance of Contract With Potential for Environmental Degradation Unconstitutional: Cape-France Enterprises (Cape-France) entered a buy-sell agreement with Peed (now deceased) and Moore to purchase some property near Bozeman for a subdivision. Before the subdivision could be completed, water needed to be procured for the site. According to the agreement, as buyers, Peed and Moore were responsible to bring water to the property, but because city water was not available, a well needed to be drilled. However, the presence of a pollution plume was discovered near the land. After the subdivision process was commenced, the Department of Environmental Quality notified Cape-France that: (1) the plume may have advanced under the property; (2) a subdivision would not be approved unless a well was drilled and tested; (3) a well could be drilled, but if testing showed pollution in the water, treatment would be extensive; and (4) if drilling or pumping of the water caused expansion of the pollution, then Cape-France, as owner of the property, would be held liable for cleanup costs. On cross-motions for summary judgment, the District Court held that the buy-sell agreement could be rescinded on the basis of mutual mistake of fact and impossibility or impracticality of performance and that specific performance would not be granted. The Supreme Court affirmed. A court may determine that an act is impossible in legal contemplation when it is not practicable, when the act can be done only at an excessive, unreasonable, and unbargained-for cost. The doctrine of impossibility or impracticability is applied when, aside from the object of a contract being unlawful, the public policy underlying the strict performance of the contract is outweighed by the senselessness of requiring performance. The doctrine is not limited to cases of literal impossibility but may also be applied in cases that present a potential for substantial and unbargained-for damages. In this case, requiring Cape-France to go forward with the performance of the contract when there was a very real possibility of substantial environmental degradation and resultant financial liability for cleanup was not in the public interest or in the interests of the contracting parties and was not in accord with the guarantee of a clean and healthful environment in Art. II, sec. 3, Mont. Const., or the mandate to maintain and improve a clean and healthful environment for present and future generations in Art. IX, sec. 1, Mont. Const. Thus, rescission of the contract was proper. Cape-France Enterprises v. Estate of Peed, 2001 MT 139, 305 M 513, 29 P3d 1011 (2001). See also Smith v. Zepp, 173 M 358, 567 P2d 923 (1977), and Mont. Envtl. Information Center v. Dept. of Environmental Quality, 1999 MT 248, 296 M 207, 988 P2d 1236 (1999).

Failure to Timely Enforce Contract Provision Insufficient of Itself to Constitute Waiver — Proof of Waiver — Reasonable Diligence Required of Rescinding Party: Mere failure to take steps to enforce a legal right under a contract in a timely manner is not, by itself, sufficient to constitute proof of waiver. Rather, a party claiming waiver must prove that the language or conduct by the other party showed unequivocally that the party voluntarily and intentionally relinquished the right to receive the full benefit of the contract. (See Pipe Indus. Ins. Fund Trust v. Consol. Pipe Trades Trust, 233 M 162, 760 P2d 711, 45 St. Rep. 1392 (1988).) Even though a party may be entitled to rescind a contract because of failure of consideration, the rescinding party must take action within a reasonable time upon discovering the facts that enable the rescission. Here, the District Court erred in concluding, without first determining whether the provisions of 28-2-1713 were complied with, that purchasers under a contract could rescind for failure of consideration. Norwood v. Serv. Distrib., Inc., 2000 MT 4, 297 M 473, 994 P2d 25, 57 St. Rep. 8 (2000), following Liddle v. Petty, 249 M 442, 816 P2d 1066, 48 St. Rep. 779 (1991).

Materiality of Claim of Failure of Consideration to Contract Required Before Rescission Available as Remedy — Partial Failure of Consideration — Meltdown of Ice Cream Distributorship

Agreement: Under Johnson v. Meiers, 118 M 258, 164 P2d 1012 (1946), a breach that goes to only part of the consideration, that is incidental and subordinate to the main purpose of the contract, and that may be compensated in damages does not warrant rescission. The injured party is still bound to perform that party's part of the contract, and the only remedy for the breach consists of the damages suffered from the breach. By contrast, under Van Hook v. Baum, 245 M 407, 800 P2d 151, 47 St. Rep. 1883 (1990), a party may rescind if, through the fault of the other party, consideration fails in whole or in part. In clarifying the disparate holdings, the Supreme Court noted that the term "failure of consideration", as either a claim or an affirmative defense, does not relate to the absence of consideration or whether there is good consideration for the formation of a valid, enforceable contract, but rather the term pertains to the failure of one party's performance, which then suspends or excuses the performance of the other party pursuant to the terms of a valid contract. Failure of consideration is generally synonymous with a material breach of performance of a contract, rather than whether a contract was enforceable because of the absence of the essential element of consideration. Thus, a claim or affirmative defense of failure of consideration that gives rise to the equitable remedy of rescission requires a showing by the claiming party that the other party's failure to perform was, in fact, material to the contract, and whether consideration was sufficient or good is immaterial. To reconcile this holding with 28-2-1711, the court went on to hold that failure of part of a promised performance may warrant rescission, but only if the claiming party proves that the deficient part of the other party's performance was material to the contract. If the failure to perform was not material, rescission is not an available remedy, performance cannot be excused, and the claiming party "may only be entitled to money damages for breach". Here, the District Court erred when it did not determine whether Norwood's failure to assign an ice cream distributor agreement to Service Distributing, Inc. (SDI), was material to the transaction as a whole. Absent that finding, SDI could not as a matter of law rescind the contract and be excused from further performance of its obligation to Norwood, so the case was remanded to determine whether a material breach occurred. Norwood v. Serv. Distrib., Inc., 2000 MT 4, 297 M 473, 994 P2d 25, 57 St. Rep. 8 (2000). See also Flaig v. Gramm, 1999 MT 181, 295 M 297, 983 P2d 396, 56 St. Rep. 710 (1999).

Breach Insufficient to Warrant Rescission: In a contract for sale of real estate, use of words such as "deposit", "depositing", and "held on deposit" prohibited the sellers from spending the earnest money paid by the buyer pending the closing of the sale; however, the sellers' failure to keep earnest money on deposit until the closing did not constitute a material breach of contract. The buyer was entitled to seek contract damages but not rescission. Cady v. Burton, 257 M 529, 851 P2d 1047, 50 St. Rep. 395 (1993), followed in Flaig v. Gramm, 1999 MT 181, 295 M 297, 983 P2d 396, 56 St. Rep. 710 (1999).

Payment Withheld in Anticipation of Breach: When employee sent letter to employer stating terms substantially different from original oral contract, employer withheld employee's pay. Court held that the employer's action was reasonable and in good faith and did not breach the contract. The employer had reasonable grounds to believe the employee would breach the contract and thus give the employer a claim for damages; therefore, the employer was entitled to withhold performance until he received assurance of the employee's intent to fulfill the contract. This is the rule stated in section 251 of the Restatement (Second) of Contracts (1979). Julian v. Mont. St. Univ., 229 M 362, 747 P2d 196, 44 St. Rep. 2046 (1987).

Breach Inadequate to Warrant Rescission — Damages as Remedy: A breach that goes to only part of the consideration, is incidental and subordinate to the main purpose of the contract, and may be compensated in damages does not warrant a rescission of the contract. The injured party is still bound to perform his part of the agreement, and his only remedy for the breach consists of the damages he has suffered therefrom. Halcro v. Moon, 226 M 121, 733 P2d 1305, 44 St. Rep. 504 (1987), citing Johnson v. Meiers, 118 M 258, 164 P2d 1012 (1946), and followed in Garcia v. Schell, 239 M 475, 781 P2d 274, 46 St. Rep. 1844 (1989), and Flaig v. Gramm, 1999 MT 181, 295 M 297, 983 P2d 396, 56 St. Rep. 710 (1999).

Damages Awarded on Theories of Breach of Contract and Rescission: Appellant argued that the District Court award of damages on both theories of breach of contract and rescission was improper, contending that the remedies were mutually exclusive. The Supreme Court noted that restitution under a theory of rescission can, under some circumstances, be a remedy for breach of contract; however, it was clear from the complaint and judgment in this case that the recovery was in damages for breach of contract and as such was properly computed. Hostetter v. Donlan, 221 M 380, 719 P2d 1243, 43 St. Rep. 909 (1986).

Mutual Cancellation: Plaintiff brought an action as personal representative to set aside a deed recorded in defendant's name. Defendant's father entered into a contract for deed with defendant in 1961. Defendant contended he paid off the contract in 1975. In 1965, defendant filed bankruptcy and did not list the land under contract as an asset or the note as a claim against the bankruptcy estate. Defendant's father made payments on the land to the land bank as late as 1977. In 1977, defendant and his wife filed for divorce, and the property was not listed as a marital asset. Defendant's father leased the property in 1978 and 1980, and defendant was not a party to either lease. Defendant recorded a deed to the property in his name in 1981. Defendant's father died in 1981, and plaintiff as personal representative brought the action to set aside the deed. The trial court refused an instruction on mutual cancellation. Plaintiff alleged in its complaint that the contract for deed had been terminated and introduced testimony that the bankruptcy had been the mutual consent terminating the contract. It was error to refuse the instruction as the doctrine of mutual cancellation is well recognized in Montana. NW. Union Trust Co. v. Worm, 204 M 184, 663 P2d 325, 40 St. Rep. 758 (1983).

Failure to Pay Draft Justification for Cancellation of Oil and Gas Lease: Oil and gas leases are to be liberally construed in favor of the lessor, and forfeiture is favored in such leases. Thus, failure of lessee to timely pay a draft executed at the same time as the lease was sufficient justification for cancellation of the lease. Clawson v. Berklund, 188 M 48, 610 P2d 1168 (1980).

Breach of Restrictive Covenant — Effect on Default: When lots within a legal subdivision are sold pursuant to a contract for deed, the sellers' breach of a restrictive covenant, occurring prior to the contracted due date and relating to a 30-foot setback requirement on sellers' adjacent lot, does not excuse the buyer from his duty to make payment by the due date and his right to recover damages is precluded by his failure to make such payment. Reinke v. Biegel, 185 M 31, 604 P2d 308 (1979).

28-2-1701. How contract extinguished.

Case Notes

Distributorship Contract — No Termination Date — When Terminable: In deciding an issue never before decided by the court, the Supreme Court, in action by distributor for breach of wine distributorship contract by wine broker who terminated the contract, which had no termination provision, adopted the "modern majority rule" that when a distributorship contract has no termination provision, it is terminable at will only after a reasonable amount of time and upon reasonable notice. The court held that the rule applied where, as in the case at hand, the distributor had made a substantial investment in establishing or furthering the distributorship. The court deferred to the trier of fact on the issue of what a reasonable amount of time is, stating that absent an abuse of discretion the Supreme Court would not interfere. In the present case, the court upheld the lower court's decision that 24 months was a reasonable amount of time. Bronken's Good Time Co. v. J. W. Brown & Associates, 203 M 427, 661 P2d 861, 40 St. Rep. 549 (1983), followed in Moats Trucking Co., Inc. v. Gallatin Dairies, Inc., 231 M 474, 753 P2d 883, 45 St. Rep. 772 (1988).

Rescission of Lease and Option for Failure of Consideration Upheld: In an action for breach of a lease of certain commercial property, the District Court did not err in denying the defendants' claim for damages based upon wrongful rescission and termination of the contract, which also contained an option to purchase. Upon reading the contract, it is clear that a $17,000 check, which was dishonored for nonsufficient funds, was an essential part of the consideration to be received by the plaintiff upon the defendants' exercise of the option. Rescission was promptly accomplished, and when exercised, the contract, including all of the provisions for default in installment payments, was extinguished. Ragen v. Weston, 191 M 546, 625 P2d 557, 38 St. Rep. 456 (1981).

Termination of Joint Venture: A contract for a joint venture may be terminated by the members but only by the mutual consent of all the members or by a proceeding for rescission. Murphy v. Redland, 178 M 296, 583 P2d 1049 (1978).

Mutual Consent of Parties — Question of Facts: The court did not err in determining that agency-manager contracts were terminated on a specific date since termination by mutual consent is a question of fact for the court and there was substantial evidence to support the court's determination. Standard Ins. Co. v. Sturdevant, 173 M 23, 566 P2d 52 (1977).

Termination of Agreement for Cause: Defendant's going out of the building materials business in good faith for business reasons did not constitute "cause" as the term was used in the termination provision of a franchise agreement with plaintiff because there was no condition forcing termination and sale of assets. J & S Home Realty, Inc. v. Anaconda Co., 172 M 236, 563 P2d 566 (1977).

Mutual Consent of Parties: This section provides that a contract may be extinguished in like manner with any other obligation and also in the manner prescribed by this chapter. Thus by mutual consent the parties to a contract may terminate the contract and all obligations thereunder. Edwards v. Muri, 73 M 339, 237 P 209 (1925).

28-2-1702. Extinction of written contract by destruction or cancellation.

Case Notes

Promissory Note Canceled: The promissory note was canceled as a matter of law when the holder of the note intentionally removed the signature of the party to be charged. Northwest Plating Co. v. Hoffman, 234 M 360, 763 P2d 44, 45 St. Rep. 1971 (1988).

28-2-1703. Extinction of executory obligations of contract by destruction, cancellation, or alteration.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Promissory Note Canceled: The promissory note was canceled as a matter of law when the holder of the note intentionally removed the signature of the party to be charged. Northwest Plating Co. v. Hoffman, 234 M 360, 763 P2d 44, 45 St. Rep. 1971 (1988).

Unilateral Material Alteration of Contract: After issuance of title insurance policy, insured signed and returned to insurers an agreement that "the second parties [the title companies] shall not be liable for any claim or claims brought directly by first party [insured] as a result of the presence of either of the two ditches on his lands, which ditches were the subject of the above referred to lawsuit", which was a suit relating to ditch rights and easements that had been settled. The insurers had failed to disclose the existence of the ditch rights and easements. Before signing the agreement, the companies inserted "see insert below" and inserted "except that the payment hereunder by [the title companies] shall be deemed to be in full compensation for any reduction in the value of the insured property of [the insured] caused by the existence of the two ditches". In insured's suit against the companies for failure to defend suits against him by the owner of ditch rights and easements, the companies could not use the altered agreement to avoid paying damages caused by their failure to discover and disclose the ditch rights and easements. It was a material alteration which insured had not agreed to. Lipinski v. Title Ins. Co., 202 M 1, 655 P2d 970, 39 St. Rep. 2283 (1982).

Modification of Listing Agreement and Failure to Provide Copy: A seller's alleged verbal consent to a broker's unsubscribed and unexecuted modification of a listing agreement was not a factual issue precluding summary judgment in light of the statutory and decisional law which is uniformly suspicious of such modifications. As a matter of law, the broker's failure to provide the seller with a copy of the listing agreement also supported the granting of summary judgment. Carnell v. Watson, 176 M 344, 578 P2d 308 (1978). See also WRB-West Associates, Inc. v. Madison Addition Inv. Ltd. Partnership, 270 M 498, 893 P2d 340, 52 St. Rep. 329 (1995).

Alteration of Contract: Where State and condemnee had agreed prior to contract to allow condemnee access to newly constructed highway from one particular spot, but State altered written contract giving condemnee no access at all, it was improper to delete all nonaccess clauses in a reformation of the contract and condemnee should have been allowed only the one access route which the parties had agreed to previously. Crissey v. St. Highway Comm'n, 147 M 374, 413 P2d 308 (1966).

Date of Promissory Note: In a suit on a promissory note an allegation of the answer that the date of the note "has been fraudulently changed by the plaintiff' is a mere conclusion and insufficient to tender issue as to an intentional, material alteration by the plaintiff precluding recovery under this section; where the note was written by the plaintiff's agent at the beginning of a new year, it is not error to permit such agent to testify that he wrote "1904" instead of "1905". McDonald v. Klenze, 52 M 142, 157 P 175 (1916).

Effect of Alteration: The legal effect of the alteration of a written contract is to extinguish all the executory obligations of the contract in favor of the party responsible for it, as against the party who does not consent, and the former cannot maintain an action on the contract in either its original or altered form; while the nonconsenting party loses no right, and is not required to rescind or repudiate the contract as it actually was made, he may ignore the change and hold the party at fault to the contract as originally made. Smith v. Barnes, 51 M 202, 149 P 963 (1915).

28-2-1711. When party may rescind.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Mistake 311
Fraud 313
Failure of Consideration 315
Mutual Agreement 319
General 320

MISTAKE

Defaulting Buyer Under Unambiguous Written Contract Cannot Rely Upon Expectations Not Covered by Contract to Avoid Contract — Disposition of Downpayment Amounts Paid and Due — County Not Liable for Negligent Misrepresentation as to Recordability of Deeds and Seller's Title Insurer Not Liable for Loss in Marketability: Documents for the sale and purchase of two sections of land unambiguously showed, and it was undisputed, that the resale of 20-acre parcels by the buyer, the immediate acceptance by the county of 20-acre resale deeds of a type that would make subdivision review unnecessary, and the ability to resell without having to undergo subdivision review were not parts of the bargain. The parties knew that these things were contemplated, but the documents did not refer to them or make them a part of the contract. Before the contract was made, the county indicated that it would accept the 20-acre resale deeds. The deal fell through when the county changed its position after the contract was signed. The buyer failed to pay the whole downpayment, and the seller terminated the contract and kept the paid portion of the downpayment. Precontract discussions on the matter must be disregarded as parol evidence because the documents were unambiguous and did not refer to the matter. The buyer was not entitled to rescind the contract and have the paid portion of the downpayment returned based on mutual mistake or failure of consideration. There was no mutual mistake because the parties knew that it was not a certainty that the county would accept the deeds. There was no failure of consideration because the resale, county acceptance of the deeds, and avoidance of subdivision review were not part of the written contract. In addition, the need for a subdivision review would not make the land unmarketable; at most, its market value decreased and it would take longer to sell it. Furthermore, a party in default is not entitled to rescission. The seller was entitled to terminate the contract. The seller was also entitled to keep an amount of the paid portion of the downpayment equal to the amount by which the contract price for the land exceeded the market value of the land at the time of the breach. The seller was not entitled to keep the remainder of the paid portion of the downpayment or to a judgment for the unpaid portion of the downpayment because the contract did not provide for that remedy. The county was not liable in tort to the seller for negligent misrepresentation, and the buyer's title insurance company was not liable to the seller for the loss in the marketability of the land caused by the need for subdivision review. Yellowstone II Dev. Group, Inc. v. First Am. Title Ins. Co., 2001 MT 41, 304 M 223, 20 P3d 755 (2001), overruled in Mary J. Baker Revocable Trust v. Cenex Harvest St., Cooperatives, Inc., 2007 MT 159, 338 M 41, 164 P3d 851 (2007), to the extent that Yellowstone II held that the determination of whether a term in a contract is ambiguous is not a question involving parol evidence.

Mistaken Valuation of Stock Insufficient Grounds for Rescission of Contract: Following termination from employment with Bitterroot International Systems, Inc. (Bitterroot), Knutson sought to exercise his buyout rights under the shareholders' agreement. Bitterroot refused to pay and sought rescission on grounds of mistake of fact, arguing that both parties had mistakenly valued stock exchanged during the purchase of another business. The District Court could not rescind a validly formed contract simply because Bitterroot undervalued the stock. A mutual mistake as to value is not necessarily sufficient to rescind a contract (see 17A C.J.S. Contracts §149). The District Court did not err in dismissing the affirmative defense of mistake of fact because the law does not protect a business from its improvident valuation of stock. Knutson v. Bitterroot Int'l Sys., Inc., 2000 MT 203, 300 M 511, 5 P3d 554, 57 St. Rep. 800 (2000).

Ignorance of Defect Precluding Rescission: Houdashelts sold Lutes a business that had a sump system that was believed by Houdashelts to be legal and properly permitted. Lutes sought to rescind the contract because of constructive fraud, based on Houdashelts's failure to disclose the fact that the sump system did not have the proper permits. Houdashelts were excused from disclosure because of their own ignorance. Therefore, no constructive fraud existed and rescission was improper. Houdashelt v. Lutes, 282 M 435, 938 P2d 665, 54 St. Rep. 420 (1997).

Contract Based Upon Mutual Mistake as to Workers' Compensation Law on Subrogation Rights of Insurer: Brown entered into a settlement agreement with the State Fund for $52,329.17, less $18,666.67 characterized as the "subrogation due the State Fund". Brown then pursued a third-party claim and settled for less than the policy limits. After the Supreme Court's decision in Zacher v. Am. Ins. Co., 243 M 226, 794 P2d 335 (1990), holding that an insurer is not entitled to subrogation unless the claimant is fully compensated for the injury, Brown sued to recover the money withheld by the State Fund. The Supreme Court held that Brown was entitled to rescind the agreement because the parties had made a mutual mistake as to state law that pertains to subrogation rights. However, the Supreme Court refused to award Brown the money retained by the State Fund on the basis that the whole agreement was void and that the lower court would have to determine the amount of money that Brown was entitled to receive. Brown v. Richard A. Murphy, Inc., 261 M 275, 862 P2d 406, 50 St. Rep. 1330 (1993).

No Finding of Fraud or Mistake in Real Estate Transaction — No Right to Rescission: Riveras sought rescission of a real estate contract after testing the water on a ranch they intended to buy and finding the water to be contaminated. Webers contended, but Riveras denied, that they told the Riveras the water would not test out but that the Weber family had been drinking it for years without problems. The District Court, having had the opportunity to observe and judge the credibility and demeanor of the witnesses, resolved the factual dispute in favor of Webers. Being in a superior position to make that finding and absent clear error in the decision, denial of the right to rescind was proper. Weber v. Rivera, 255 M 195, 841 P2d 534, 49 St. Rep. 969 (1992).

Mutual Mistake — Act of Negligent Third Person Not Required: As a matter of law, mutual mistake does not have to be the result of the negligent act of a third person. Wyman v. DuBray Land Realty, 231 M 294, 752 P2d 196, 45 St. Rep. 621 (1988).

Mutual Mistake Regarding Zoning Ordinance — Rescission Proper: When both parties believed, at the time a contract for deed was executed, that a business was in compliance with a zoning ordinance but the business was later found not to comply, it constituted a mutual mistake of fact under 28-2-409 and rescission was therefore proper under 28-2-1711. Carey v. Wallner, 223 M 260, 725 P2d 557, 43 St. Rep. 1706 (1986), affirmed, 229 M 57, 744 P2d 881, 44 St. Rep. 1778 (1987), and followed in Mitchell v. Boyer, 237 M 434, 774 P2d 384, 46 St. Rep. 928 (1989).

Damages Awarded on Theories of Breach of Contract and Rescission: Appellant argued that the District Court award of damages on both theories of breach of contract and rescission was improper, contending that the remedies were mutually exclusive. The Supreme Court noted that restitution under a theory of rescission can, under some circumstances, be a remedy for breach of contract; however, it was clear from the complaint and judgment in this case that the recovery was in damages for breach of contract and as such was properly computed. Hostetter v. Donlan, 221 M 380, 719 P2d 1243, 43 St. Rep. 909 (1986).

Mutual Mistake Must Defeat Object of Contract: Plaintiffs and defendant entered an agreement whereby defendant would lease condominiums from the plaintiffs and would sell plaintiffs her home. The lease of one of the condominiums contained an option for defendant to purchase the unit by forgiving plaintiffs their obligation under the promissory note on the home. Plaintiffs discovered that the floors in the home sloped north at a rate of 5½ inches over 30 feet. Plaintiffs sought to rescind the contract, and defendant sought specific performance. Plaintiffs contended mutual mistake in the making of the contract. The District Court found that the object of the contract was to furnish plaintiffs with a home to live in. This purpose was not frustrated by the unlevel condition, as defendant's family had lived in the house for 10 years. In order for mutual mistake to warrant rescission of a contract, the mistake must be so substantial and fundamental as to defeat the object of the parties in making the contract. Here, the mistake did not affect the object of the parties and rescission did not lie. Woodahl v. Matthews, 196 M 445, 639 P2d 1165, 39 St. Rep. 238 (1982), followed in Wyman v. DuBray Land Realty, 231 M 294, 752 P2d 196, 45 St. Rep. 621 (1988), and in Van Hook v. Baum, 245 M 407, 800 P2d 151, 47 St. Rep. 1883 (1990). See also Halcro v. Moon, 226 M 121, 733 P2d 1305, 44 St. Rep. 504 (1987).

Mutual Mistake — Basis for Rescission: Defendants purchased an irregular tract of land and commenced construction of a commercial building. They were contacted by plaintiff concerning purchase of the building. They consulted an attorney and discussed condominiumizing the building. He suggested as a tax matter that defendant should hold the property long enough to qualify for long-term capital gain treatment. An option to purchase with contract for deed was entered. The deeds and contract were not completed, as a survey was needed for a legal description of the property. The contract contained a provision that defendants provide and pave parking lots north and south of the building. The survey was completed and showed that the building encroached on state and county rights-of-way to the north and south. Plaintiffs then sought to rescind the contract and recover their money. The Supreme Court held that the providing of parking lots was material to the contract and that mutual mistake of fact as to the parking lots was an adequate basis for rescinding the contract. They also held that any findings not made could be implied to support the trial court's decision. Berry v. Romain, 194 M 400, 632 P2d 1127, 38 St. Rep. 1434 (1981).

Misunderstanding of Tax Consequences: A misunderstanding by the plaintiff of tax consequences attendant to a sale agreement is not ground for rescission as a mistake of law when the other party is not aware of or under the same misapprehension. Quinn v. Briggs, 172 M 468, 565 P2d 297 (1977).

Mutual Mistake: Where the buyer and the seller, an administrator, were of the opinion that the realty in question belonged to the latter's decedent, the court mistakenly ordering and approving the sale, and the buyer had made part payment and executed a note for the balance due, there was such a mutual mistake and a failure of consideration as justified a rescission of the contract under this section. Rinio v. Kester, 99 M 1, 41 P2d 405 (1935).

FRAUD

No Misrepresentation Regarding Property Encumbrances — Actual and Constructive Notice to Plaintiffs: It was not an error for the District Court to enforce a settlement agreement despite plaintiffs' allegation of misrepresentation by the defendants regarding property encumbrances. The claims of misrepresentation failed since the plaintiffs had actual notice of the mortgages in the purchase agreement on one parcel and in the warranty deed on another parcel. Alternatively, there was no misrepresentation since the mortgages were recorded, which gave the plaintiffs constructive notice. Hinderman v. Krivor, 2010 MT 230, 358 Mont. 111, 244 P.3d 306.

No Finding of Fraud or Mistake in Real Estate Transaction — No Right to Rescission: Riveras sought rescission of a real estate contract after testing the water on a ranch they intended to buy and finding the water to be contaminated. Webers contended, but Riveras denied, that they told the Riveras the water would not test out but that the Weber family had been drinking it for years without problems. The District Court, having had the opportunity to observe and judge the credibility and demeanor of the witnesses, resolved the factual dispute in favor of Webers. Being in a superior position to make that finding and absent clear error in the decision, denial of the right to rescind was proper. Weber v. Rivera, 255 M 195, 841 P2d 534, 49 St. Rep. 969 (1992), followed in Eissinger v. Mullin Trucking, Inc., 263 M 38, 865 P2d 300, 50 St. Rep. 1695 (1993).

Rescission Barred by Laches: The Supreme Court held that plaintiffs' inability to completely restore defendants to their original condition would not alone foreclose rescission as a remedy. Plaintiffs had notice of circumstances that should have put them on inquiry of possible fraud at the time of sale in 1977 and in 1978 when the net income did not reflect earlier representations. Nevertheless, plaintiffs continued to make payments and operate the business without complaint until 1981. The court held that these facts constituted laches, or a failure to use reasonable diligence to rescind promptly on the part of the plaintiffs. Since the time period between notice of possible fraud and filing of a complaint exceeded the 2-year Statute of Limitations for fraud, the District Court erred in permitting the jury to consider rescission as a remedy for the plaintiffs. McGregor v. Cushman/Mommer, 220 M 98, 714 P2d 536, 43 St. Rep. 206 (1986).

Bank's Fiduciary Duty to Customers It Gives Financial Advice — Real Estate Sales: Wife, whose husband had recently died, signed a contract for a deed to her ranch with Dittman, who signed as "trustee". There were two other purchasers, who did not sign: a person to whom, according to the evidence, wife would not have knowingly sold and the marketing officer of the bank used by the wife and husband for some 24 years. Wife was unfamiliar with real estate and financial affairs and relied upon the advice of various bank officers with regard to the sale of the ranch. This put the bank in a prima facie fiduciary relationship as to the wife. The relationship and its attendant duties extended to the advising officers in their dealings with the wife in regard to sale of the ranch. The marketing officer thus had a duty to fully inform the wife and protect her interests. This duty he breached, and the breach amounted to constructive fraud, where evidence showed that: (1) the contract price and terms were disadvantageous to the wife; (2) the true purchasers were not disclosed to her either by the contract or the marketing officer; (3) the purchasers intended to and began to subdivide and sell the ranch, though the marketing officer knew wife apparently did not wish this, having refused an earlier offer to purchase with right to subdivide; (4) the marketing officer had extensive financial interests involving loans to him from his bank, and an audit of the bank recommended that in view of this his lending authority should be eliminated or curtailed; and (5) the lower court was unimpressed with the way in which wife's attorney in the negotiations represented her interests. The lower court properly ordered the contract for deed rescinded. Deist v. Wachholz, 208 M 207, 678 P2d 188, 41 St. Rep. 286 (1984).

Constructive Fraud — Requirement of Breach of Duty: Plaintiffs and defendant entered an agreement whereby defendant would lease condominiums from the plaintiffs and would sell plaintiffs her home. The lease of one of the condominiums contained an option for defendant to purchase the unit by forgiving plaintiffs their obligation under the promissory note on the home. Plaintiffs discovered that the floors in the home slope north at a rate of 5½ inches over 30 feet. Plaintiffs sought to rescind the contract, and defendant sought specific performance. Plaintiffs contended that their consent to the contract was obtained through constructive fraud. Constructive fraud requires the breach of a duty. Defendant and several contractors who performed work on the house testified that they were unaware of the condition of the floors. Plaintiffs inspected the house twice, and their professional appraiser was unaware of the condition during his appraisal. Since defendant was unaware of the defect, she was under no duty to disclose. Because defendant had no duty that she could breach, there was no constructive fraud. Woodahl v. Matthews, 196 M 445, 639 P2d 1165, 39 St. Rep. 238 (1982).

Statements of Property Value Not Grounds for Rescission — Trial Court's Decision on Fraud Issue: The defendants in this case owed the plaintiff a sum of money, and the plaintiff agreed to accept a piece of land as partial satisfaction. The plaintiff never inspected the property until the settlement agreement was executed. Later the plaintiff found he could not sell the parcel for nearly the amount of the debt. The plaintiff then sought rescission because of the defendants' alleged misrepresentations of the nature and value of the property. On review, the Supreme Court held that statements of property value are opinions and do not constitute a proper basis for rescission. It is solely the trial court's decision whether fraud was perpetrated on an innocent purchaser. The Supreme Court noted that the plaintiff's business acumen and the nature of his relationship with the defendants greatly weakened his claim. Dolson Co. v. Imperial Cattle Co., 191 M 357, 624 P2d 993, 38 St. Rep. 306 (1981).

Defrauded Purchaser in Default — No Waiver of Right to Rescind: A purchaser who has been defrauded by a seller in the course of making a contract for sale of real property does not waive his right to rescind the contract even if purchaser is in default as to payments on the property. It would be incongruous to hold that when the purchaser decided to rescind rather than to bring the payments up to date that purchaser waived his right to rescind; purchaser would then be left without a remedy. Moschelle v. Hulse, 190 M 532, 622 P2d 155, 37 St. Rep. 1506 (1980).

Fraud — Rescission by Purchaser in Default: A vendor's fraud vitiates a contract of sale from its inception, and a purchaser in default may seek rescission. Moschelle v. Hulse, 190 M 532, 622 P2d 155, 37 St. Rep. 1506 (1980).

Material Misrepresentations in Sale of Real Property — Damages Inadequate: Where seller misrepresents the condition of premises to be sold to the extent that over $27,000 in repairs would be needed to bring the premises up to the condition represented and where repairs would result in a prolonged period during which premises could not be used for business, the misrepresentation is material and damages, as opposed to rescission, would be inappropriate. Moschelle v. Hulse, 190 M 532, 622 P2d 155, 37 St. Rep. 1506 (1980).

False Representations: The sellers of a business falsely represented the profitability of the business and its standing with suppliers and wholesalers to prospective buyers. The buyers relied on and had a right to rely on the truth of the representations and were induced to purchase the business because of the false representations. Upon learning of the falsity of the representations that had induced them to purchase the business, the purchasers had the right to rescind the contract for deed for the purchase of the business. Lumby v. Doetch, 183 M 427, 600 P2d 200 (1979).

Reliance on Fraudulent Representations: Fraud is not established unless the plaintiff proves he relied on the truth of the representations made to him, and where the evidence showed that the plaintiffs relied upon their own investigations and those of a realtor hired by them and not the representations made by the defendant, there was no reliance and no cause of action for fraud. Waller v. Heid, 170 M 501, 554 P2d 1331 (1976).

Compliance With Contract: Rescission of contract alleging fraudulent misrepresentations as to taxes and insurance was properly denied where sellers had paid taxes and procured insurance according to the terms of the sale contract. Dunlap v. Nelson, 165 M 291, 529 P2d 1394 (1974).

Failure to Pass Title: The purchaser of an automobile was entitled to rescind chattel mortgages given for purchase of the car where it was misrepresented by the seller and the seller and the assignee of the chattel mortgages failed to pass title to the buyer. Sonnek v. Universal C.I.T.

Credit Corp., 140 M 503, 374 P2d 105 (1962), explained in Safeco Ins. Co. of Am. v. NW. Mut. Ins. Co., 142 M 155, 382 P2d 174 (1963).

Insufficient Pleadings: Where defendant in an action to recover the purchase price of personal property in his answer pleaded that the representation of plaintiff that he had title to the property was false but did not allege that plaintiff knew it to be false, that it was made in a manner not warranted by the information possessed by the seller, that it was made with intent to deceive, that the buyer believed it to be true or relied upon it, and that he was deceived by it and misled to his prejudice, the pleading was insufficient to warrant rescission of the contract on the ground of fraud. Courtney v. Gordon, 74 M 408, 241 P 233 (1925).

Election of Remedies: Neither the remedy afforded by this section, giving a party to a contract the right to rescind on the ground of fraud, among others, nor that granted by 28-2-1611, under which he may have the contract reformed on the same ground, is exclusive, each being independent of the other; hence the defrauded party may elect to pursue either remedy. Campana v. Dobry, 69 M 240, 221 P 540 (1923).

Valueless Security: The buyer of a promissory note secured by mortgages on real and personal property, subject to prior liens which were foreclosed by their holders, rendering the security valueless but through no fault of the seller of the note, had no cause of action for rescission (no fraud or deceit having been practiced upon him) under any of the provisions of this section. Simeon v. Klenze, 66 M 341, 213 P 440 (1923).

Fraud in Inducement: If false representations were held out to plaintiff as an inducement for the execution of notes in payment of a subscription for corporate stock upon which it acted, the obligation becomes a nullity and the subscriber may rescind. Equity Cooperative Ass'n v. Milling Co., 63 M 26, 206 P 349 (1922).

Land Contract — Remedies: Where a contract for the purchase of land was procured through false representations whereby the vendee has been deceived and defrauded, he has an election of remedies: he may stand upon the contract and sue for damages or rescind the contract but cannot pursue both. Smith v. Christie, 60 M 604, 201 P 1011 (1921).

Material Misrepresentations: A misrepresentation made by the owner of a ranch to its purchaser that a barn and a spring in close proximity thereto inclosed with a fence were a part of the property sold was material, and sufficient ground for rescission. Fontaine v. Lyng, 61 M 590, 202 P 1112 (1921), distinguished in Estabrook v. Sonstelie, 86 M 435, 284 P 147 (1930).

FAILURE OF CONSIDERATION

Defaulting Buyer Under Unambiguous Written Contract Cannot Rely Upon Expectations Not Covered by Contract to Avoid Contract — Disposition of Downpayment Amounts Paid and Due — County Not Liable for Negligent Misrepresentation as to Recordability of Deeds and Seller's Title Insurer Not Liable for Loss in Marketability: Documents for the sale and purchase of two sections of land unambiguously showed, and it was undisputed, that the resale of 20-acre parcels by the buyer, the immediate acceptance by the county of 20-acre resale deeds of a type that would make subdivision review unnecessary, and the ability to resell without having to undergo subdivision review were not parts of the bargain. The parties knew that these things were contemplated, but the documents did not refer to them or make them a part of the contract. Before the contract was made, the county indicated that it would accept the 20-acre resale deeds. The deal fell through when the county changed its position after the contract was signed. The buyer failed to pay the whole downpayment, and the seller terminated the contract and kept the paid portion of the downpayment. Precontract discussions on the matter must be disregarded as parol evidence because the documents were unambiguous and did not refer to the matter. The buyer was not entitled to rescind the contract and have the paid portion of the downpayment returned based on mutual mistake or failure of consideration. There was no mutual mistake because the parties knew that it was not a certainty that the county would accept the deeds. There was no failure of consideration because the resale, county acceptance of the deeds, and avoidance of subdivision review were not part of the written contract. In addition, the need for a subdivision review would not make the land unmarketable; at most, its market value decreased and it would take longer to sell it. Furthermore, a party in default is not entitled to rescission. The seller was entitled to terminate the contract. The seller was also entitled to keep an amount of the paid portion of the downpayment equal to the amount by which the contract price for the land exceeded the market value of the land at the time of the breach. The seller was not entitled to keep the remainder of the paid portion of the downpayment or to a judgment for the unpaid portion of the downpayment because the contract did not provide for that remedy. The county was not liable in tort to the seller for negligent misrepresentation, and the buyer's title insurance company was not liable to the seller for the loss in the marketability of the land caused by the need for subdivision review. Yellowstone II Dev. Group, Inc. v. First Am. Title Ins. Co., 2001 MT 41, 304 M 223, 20 P3d 755 (2001), overruled in Mary J. Baker Revocable Trust v. Cenex Harvest St., Cooperatives, Inc., 2007 MT 159, 338 M 41, 164 P3d 851 (2007), to the extent that Yellowstone II held that the determination of whether a term in a contract is ambiguous is not a question involving parol evidence.

Reciprocal Rights and Obligations Considered Sufficient Consideration to Sustain Shareholders' Agreement: Following his termination from employment with Bitterroot International Systems, Inc. (Bitterroot), Knutson sought to exercise his buyout rights under the shareholders' agreement. Bitterroot refused to pay on grounds of insufficient consideration, contending that the essential consideration for the shareholders' agreement was the exchange of stocks of equal value—an argument based on the premise that the stock exchange and the shareholders' agreement were one agreement. However, the shareholders' agreement was enforceable independent of the stock exchange between the parties, and the creation of reciprocal rights and obligations among the shareholders was sufficient consideration to sustain the shareholders' agreement; thus, the District Court did not err in concluding that the consideration was sufficient. Knutson v. Bitterroot Int'l Sys., Inc., 2000 MT 203, 300 M 511, 5 P3d 554, 57 St. Rep. 800 (2000).

Materiality of Claim of Failure of Consideration to Contract Required Before Rescission Available as Remedy — Partial Failure of Consideration — Meltdown of Ice Cream Distributorship Agreement: Under Johnson v. Meiers, 118 M 258, 164 P2d 1012 (1946), a breach that goes to only part of the consideration, that is incidental and subordinate to the main purpose of the contract, and that may be compensated in damages does not warrant rescission. The injured party is still bound to perform that party's part of the contract, and the only remedy for the breach consists of the damages suffered from the breach. By contrast, under Van Hook v. Baum, 245 M 407, 800 P2d 151, 47 St. Rep. 1883 (1990), a party may rescind if, through the fault of the other party, consideration fails in whole or in part. In clarifying the disparate holdings, the Supreme Court noted that the term "failure of consideration", as either a claim or an affirmative defense, does not relate to the absence of consideration or whether there is good consideration for the formation of a valid, enforceable contract, but rather the term pertains to the failure of one party's performance, which then suspends or excuses the performance of the other party pursuant to the terms of a valid contract. Failure of consideration is generally synonymous with a material breach of performance of a contract, rather than whether a contract was enforceable because of the absence of the essential element of consideration. Thus, a claim or affirmative defense of failure of consideration that gives rise to the equitable remedy of rescission requires a showing by the claiming party that the other party's failure to perform was, in fact, material to the contract, and whether consideration was sufficient or good is immaterial. To reconcile this holding with this section, the court went on to hold that failure of part of a promised performance may warrant rescission, but only if the claiming party proves that the deficient part of the other party's performance was material to the contract. If the failure to perform was not material, rescission is not an available remedy, performance cannot be excused, and the claiming party "may only be entitled to money damages for breach". Here, the District Court erred when it did not determine whether Norwood's failure to assign an ice cream distributor agreement to Service Distributing, Inc. (SDI), was material to the transaction as a whole. Absent that finding, SDI could not as a matter of law rescind the contract and be excused from further performance of its obligation to Norwood, so the case was remanded to determine whether a material breach occurred. Norwood v. Serv. Distrib., Inc., 2000 MT 4, 297 M 473, 994 P2d 25, 57 St. Rep. 8 (2000). See also Flaig v. Gramm, 1999 MT 181, 295 M 297, 983 P2d 396, 56 St. Rep. 710 (1999).

Immaterial Breach — Suspension of Performance Not Justified: Neighbors constructed a well on one's property. They shared the costs of construction and agreed that the plaintiffs would share in maintenance costs by installing and maintaining a yard light for the benefit of both lots. When the plaintiffs failed to maintain the light, the defendants shut off the plaintiffs' water. The District Court terminated the well agreement. The Supreme Court held that the lower court erred in terminating the agreement because failure to maintain the light was an immaterial breach. Flaig v. Gramm, 1999 MT 181, 295 M 297, 983 P2d 396, 56 St. Rep. 710 (1999).

Alleged Lack of Permit for Business — Legal Consideration: Lutes contended that the contract that he entered with Houdashelts for sale of an engine rebuilding business was void for failure of consideration because the sump system in the business did not have the proper permits and was therefore illegal. The District Court rejected the contention that the system was illegal. The Supreme Court held that the parties had each received good consideration in the simple sale of the business and that rescission was thus improper. Houdashelt v. Lutes, 282 M 435, 938 P2d 665, 54 St. Rep. 420 (1997).

Contract for Deed — No Right of Buyer to Suspend Performance for Failure of Consideration Not Attributable to Sellers: Petty made the downpayment on a contract for deed that called for conveyance of part of the property to Petty upon downpayment. Petty assumed the property was unzoned. The contract stated that Petty would use the property for a recreational vehicle park and that if after Petty's due diligence Petty could not obtain zoning approval within 30 months after the contract was signed, the purchase price would be reduced by $25,000. The bank that held a preexisting mortgage on the property told Petty it would not release the property until he brought current his payments to the sellers and the bank. Over 30 months passed from the time of the downpayment until the sellers filed suit, during which time Petty made no payments to the sellers or the bank and did not obtain zoning approval. Petty did not request a deed until 27 months after making the downpayment. Petty was not entitled to suspend performance for failure of delivery of the deed and transfer of the property because he was accountable, not the sellers. The award of damages to the sellers was affirmed. Liddle v. Petty, 249 M 442, 816 P2d 1066, 48 St. Rep. 779 (1991), followed in Norwood v. Serv. Distrib., Inc., 2000 MT 4, 297 M 473, 994 P2d 25, 57 St. Rep. 8 (2000).

Rescission Inapplicable Absent Total Voidness: Plaintiffs, whose home flooded, claimed they were entitled to rescission due to a partial or complete failure of consideration, based in part on slightly reduced property values subsequent to the flood. However, the applicable provision of this section requires that a party may rescind if consideration becomes entirely void. The lessened appraised values were made in apprehension that the property might flood again; therefore, the District Court ruling that there was not an adequate failure of consideration was properly based on evidence and law. Van Hook v. Baum, 254 M 407, 800 P2d 151, 47 St. Rep. 1883 (1990).

Breach of Implied Warranty of Habitability Not Based on Fault: The plaintiffs brought an action for specific performance when the defendants quit making house payments and demanded rescission of a contract for deed. The defendants argued for rescission, alleging that the plaintiffs had breached the implied warranty of habitability. The plaintiffs, a husband and wife, contended that the warranty did not apply to them because they were not "builder-vendors" as contemplated by Montana case law. The Supreme Court held that the warranty did apply because the plaintiffs had built and sold two other houses prior to the one sold the defendants and though the plaintiffs were only amateur builders, the theory behind the warranty is not to discern fault but to place liability on the one most able to prevent the harm. Pracht v. Rollins, 239 M 62, 779 P2d 57, 46 St. Rep. 1513 (1989).

Licensing Requirement as Partial Failure of Consideration in Sale of Business — Rescission Proper: When the seller warranted in a special provision of a contract for deed that no license was required to operate a business and that no restrictions or license would be required as a result of change of ownership and seller later defaulted under these terms when it was discovered that a license was required but denied, it constituted a partial failure of consideration under 28-2-801 because seller did not transfer a going business and buyer was unable to operate the kind of business intended at the time of purchase. Rescission was therefore proper under 28-2-1711. Carey v. Wallner, 223 M 260, 725 P2d 557, 43 St. Rep. 1706 (1986), affirmed, 229 M 57, 744 P2d 881, 44 St. Rep. 1778 (1987).

Inability to Record Deed — Basis for Rescission of Contract: Plaintiffs purchased land from the defendants. The description of the land in the deed to defendants and in the notice of real estate contract, both of which were filed with the county, were identical. When the plaintiffs tried to convey the land to a third party, using the same description, the county refused to record the deed, relying on a 1981 Attorney General's opinion which had been issued subsequent to the prior filings. The District Court granted summary judgment for the plaintiffs, and the Supreme Court affirmed. Because the plaintiffs could not get a recordable title without suing for rescission or suing the county to require recording, the defendants could not deliver a marketable title to the plaintiffs and plaintiffs were entitled to rescission. McCarthy v. Timberland Resources, Inc., 219 M 278, 712 P2d 1292, 42 St. Rep. 2016 (1985).

Alteration of Oral Contract — Rescission — Damages: Plaintiffs had an oral agreement with defendants to pay one-half of defendants' purchase price under defendants' written contract for deed for purchase of certain real property with the understanding that plaintiffs' names would be added to the title as copurchasers. Without plaintiffs' consent, defendants made written assignment of their interests under the written contract to a third party, retaining a life estate to themselves. Plaintiffs refused to make further payments and sued for damages and to quiet title in themselves. The District Court denied plaintiffs' claims and in effect found plaintiffs to be the breaching party. The Supreme Court found plaintiffs were entitled to rescission and reversed the District Court decision. Defendants' assignment while retaining a life estate constituted a material alteration of the oral agreement to which plaintiffs had not consented. Defendants' breach entitled plaintiffs to recover money they had paid on the contract with interest. Forsythe v. Elkins, 216 M 108, 700 P2d 596, 42 St. Rep. 680 (1985).

Action to Set Aside Quitclaim Deed — No Failure of Consideration Proved: The plaintiff, son of a deceased rancher, received 24½% of the surface rights to his father's ranch in accordance with the terms of an estate plan established for the benefit of the plaintiff and his brothers, the defendants. Upon leaving the ranch, plaintiff executed one quitclaim deed to his mineral interest in 1977 and one quitclaim deed to his surface interest in 1968 in exchange for a promise that the defendants would hold him harmless on a promissory note. The District Court did not err (in a subsequent challenge by the plaintiff to the validity of the quitclaim deeds) in declaring both deeds to be valid and denying the plaintiff any interest in the ranch. The facts and law do not support the plaintiff's contention that there was a failure of consideration for his signing the two quitclaim deeds. First, 28-2-1711 is not applicable, because under 70-1-502 consideration for the transfer of real property is not required. Second, the facts of the case show that the plaintiff was indemnified for signing the two deeds by the defendants' agreement to hold the plaintiff harmless on the promissory note. That is sufficient consideration. Turley v. Turley, 199 M 265, 649 P2d 434, 39 St. Rep. 1336 (1982).

Rescission of Lease and Option for Failure of Consideration Upheld: In an action for breach of a lease of certain commercial property, the District Court did not err in denying the defendants' claim for damages based upon wrongful rescission and termination of the contract, which also contained an option to purchase. Upon reading the contract, it is clear that a $17,000 check, which was dishonored for nonsufficient funds, was an essential part of the consideration to be received by the plaintiff upon the defendants' exercise of the option. Rescission was promptly accomplished, and when exercised, the contract, including all of the provisions for default in installment payments, was extinguished. Ragen v. Weston, 191 M 546, 625 P2d 557, 38 St. Rep. 456 (1981).

Rescission of Landfill Operation Contract — Operator Unlicensed: The county refuse board contracted with the appellant to operate a landfill. Because of his own fault and disregard, the appellant failed to comply with the statutory and contractual requirements to obtain a license to operate the landfill. As a result of this failure, the Department of Health Solid Waste Management Bureau began refusing to lift sanitary restrictions on proposed subdivisions in the area. The refusal in effect prevented the approval of those subdivisions for solid waste disposal and thereby exposed the County Commissioners to potential liability. When the County Commissioners chose to terminate the appellant's contract, there was a failure of consideration through the fault of the defendant, resulting in an alteration of the Commissioners' position to their prejudice. Consequently, the trial court acted properly in rescinding the contract. Ryan v. Bd. of County Comm'rs, 190 M 273, 620 P2d 1203, 37 St. Rep. 1965 (1980).

Substantial Failure of Consideration: Trial court's finding of substantial failure of consideration in mobile home sale was upheld and rescission by buyer allowed. Compton v. Alcorn, 171 M 230, 557 P2d 292 (1976).

Failure of Consideration for Any Cause: Under this section party may rescind contract when consideration for his obligation fails in whole or in part through fault of party as to whom he rescinds, or if such consideration, before it is rendered to him, fails in material respect from any cause. Brown v. First Fed. S & L Ass'n of Great Falls, 154 M 79, 460 P2d 97 (1969), overruled, to the extent that this case holds that no recovery can be allowed for an injury that results from an intervening act of a third party, in Estate of Strever v. Cline, 278 M 165, 924 P2d 666, 53 St. Rep. 576 (1996).

Failure to Register: Chattel mortgages given for the purchase of an automobile were without consideration where vendor failed to register transfer under 61-3-201 which was necessary to pass title to the buyer. Sonnek v. Universal C.I.T. Credit Corp., 140 M 503, 374 P2d 105 (1962), explained in Safeco Ins. Co. of Am. v. NW. Mut. Ins. Co., 142 M 155, 382 P2d 174 (1963).

Rescission of Partnership Agreement Barred by Laches: Rescission of a partnership agreement lies under this section where consideration fails, but where there was no such failure upon creation of the relationship but mere breaches in manner of operation after the relationship was established it may not be resorted to. Where defendant refused for several years to deliver to the partnership two pairs of foxes as part of the consideration to be furnished by him, plaintiff's complaint impliedly shows, on its face, laches, and plaintiff's choice to affirm the agreement instead of promptly rescinding it is hence subject to general demurrer. Lommasson v. Hall, 111 M 142, 106 P2d 1089 (1940).

Failure to Deliver Possession: Partial failure of consideration of a contract though ground for rescission does not support a plea of entire failure thereof; therefore evidence, in an action by a chattel mortgagor to enjoin the sale of sheep under a mortgage given to secure the rental of a tract of grazing land comprising 800 acres, that defendant lessors were unable to deliver possession of 320 acres thereof, held by another under a prior lease, was insufficient to support an allegation of entire failure of consideration for the contract of lease. Nelson v. Davenport, 86 M 1, 281 P 537 (1929).

Personal Property Sale: A buyer cannot rescind a sale of personal property on the ground of failure of consideration until he has been disturbed in his possession or otherwise suffered damages. Courtney v. Gordon, 74 M 408, 241 P 233 (1925).

Executory Contract Required: Subsection (4) of this section authorizing rescission if consideration for the contract fails in a material respect from any cause applies only to executory, not executed, contracts, i.e., where there has been a change in the situation causing the consideration to fail between the time of its making and its execution. Simeon v. Klenze, 66 M 341, 213 P 440 (1923).

MUTUAL AGREEMENT

Notice of Rescission Required: As part of a subdivision, the developers and the county reserved from the dedication a 1-foot strip of land adjacent to the exterior boundary. The reservation could be voided by the County Commission in the public interest for the purpose of ensuring good traffic circulation. A dispute arose between the developers and adjoining landowners over the use of subdivision streets. The County Commissioners, acting on the advice of the County Surveyor and a deputy county attorney, unilaterally rescinded the reservation agreement. Although the resolution rescinding the agreement was filed with the Clerk and Recorder, the developers claimed no actual knowledge and the resolution did not appear in the official county file concerning the subdivision. The Supreme Court, relying on Small v. Coca-Cola Bottling Co., 134 M 168, 328 P2d 124 (1958), held that although written notice is not required to rescind, both parties must assent to and be aware of the rescission in order for it to be effective. Notice had to be received by the developers for the rescission to be effective, and the jury should have been so instructed. Smith v. Moran, 215 M 31, 693 P2d 1246, 42 St. Rep. 152 (1985).

Oral Cancellation of Insurance Policy: The lower court properly found that defendant's policy had been canceled by mutual oral agreement, leaving plaintiff liable for the entire loss on its policy issued to the insured. Nat'l Indem. Co. v. St. Paul Fire & Marine Ins. Co., 176 M 137, 576 P2d 733 (1978).

Exclusive Listing Agreement: In the instant case there was no mutual assent as is required for the effective rescission of a contract. McDonald & Co. v. Fishtail Creek Ranch, 175 M 53, 572 P2d 195 (1977).

Oral Termination: A written lease for term of years may be terminated by an oral agreement provided the conduct of the parties is consistent with such an agreement. Rodgers v. Saunders, 144 M 424, 396 P2d 817 (1964).

Mutual Consent to Termination: The parties to an executory written agreement may terminate it at any time by mutual consent independently of any express agreement so provided, and it is immaterial whether the termination is characterized as abandonment, cancellation, mutual rescission, or waiver, and may be established by parol evidence. However, mutual cancellation of the contract must be clearly expressed and shown, and acts and conduct of the parties to be sufficient must be clear, convincing, and inconsistent with the existence of the contract. W. River Equip. Co. v. Holzworth Constr. Co., 134 M 582, 335 P2d 298 (1959). See also Jorgensen v. Trademark Woodworks, LLC, 2018 MT 291, 393 Mont. 381, 431 P.3d 29.

Characterization Immaterial: The parties to an executory written contract could by mutual consent terminate it independently of any express agreements so providing, and it is immaterial whether such termination is characterized as an abandonment, cancellation, mutual rescission, or waiver, and the effect of such termination was to relieve the parties from going forward under such written contract. Eggers v. Gen. Refrigeration Co., 123 M 205, 210 P2d 636 (1949); Kester v. Nelson, 92 M 69, 10 P2d 379 (1932).

Written Contract Rescinded by Oral Consent: Under this section rescission of a contract may be had by mutual consent and a written contract may be rescinded by mutual consent not expressed in writing. Barnard-Curtiss Co. v. Maehl, 117 F2d 7 (9th Cir. 1941).

Mutual Consent — Allegation in Answer Sufficient: The parties to an executory contract of sale of real property may terminate it by mutual consent independently of any provision in the contract permitting them to do so; hence, an allegation in defendant's answer to a complaint for the specific performance of the contract that plaintiff had informed him that if the abstract furnished was not satisfactory the deal would be called off and that he accepted the offer to terminate the contract, was sufficient to show a mutual rescission of the contract a good defense, and was proof against a general demurrer (demurrer abolished, former Rule 7(c), M.R.Civ.P., now superseded) and motion to strike. Ogg v. Herman, 71 M 10, 227 P 476 (1924).

GENERAL

Settlement Agreement Properly Approved — Sibling Trustee Present and Represented by Counsel — Mediation's Key Terms Understood Despite COVID-19 Illness — Undue Influence Inapplicable — Doctrine of Laches Elements Established. Lindemulder v. Lindemulder, 2022 MT 119, 409 Mont. 69, 512 P.3d. 260.

Waiver of Contract Rights — Late Payments Not Considered Breach Based on Prior Acceptance: The uninsured employers' fund (UEF) sought indemnity from an employer that did not have workers' compensation insurance using a monthly payment arrangement that was agreed to by the parties. The UEF accepted four late payments before turning the employer over to collections, at which point the employer sued UEF for breach of contract. The Supreme Court held that UEF waived its right to terminate the contract based on late payment when it accepted late payments without objection. Consequently, it was a breach of contract for the UEF to turn the employer over to collections and the employer was entitled to damages. Elk Mtn. Motor Sports, Inc. v. Dept. of Labor and Industry, 2012 MT 261, 367 Mont. 36, 289 P.3d 165.

Validity of Voluntary Easement Affirmed: The Permanns requested that Urick grant an easement across Urick's property for the Permanns to go camping and move cattle, and Urick agreed. When Urick's sons discovered that the voluntary easement had been granted, they persuaded Urick to rescind the easement. Urick requested that the Permanns convey the easement back to her. They refused. Urick filed suit and then subsequently died. Urick's son Gliko, as trustee of Urick's estate, brought an action against the Permanns seeking to have the easement rescinded, citing mutual mistake, constructive fraud, undue influence, and lack of consideration. The District Court held that the easement was valid, and Gliko appealed. The Supreme Court considered each of Gliko's rescission arguments in turn. The language of the easement was simple and unambiguous, so there was no mutual mistake. Urick had testified by deposition that no misleading statements were made relating to the easement, so there was no constructive fraud. There was no confidential relationship between Urick and the Permanns, Urick was not possessed of weakness of mind, and no advantage was taken of Urick's necessities or distress, so there was no undue influence. Last, there was no evidence that consideration was meant to be given, so lack of consideration was not a valid ground for rescission. The District Court was affirmed. Gliko v. Permann, 2006 MT 30, 331 M 112, 130 P3d 155 (2006).

Absence of Evidence of Rescission, Release, Waiver, or Accord and Satisfaction of Contract — Reversal Warranted: Plaintiffs owned shares in defendant's corporation and sought to sell the shares back to the corporation. The corporation sent a letter offering to purchase the shares for $64,933.60, and plaintiffs were instructed that to accept the offer, they were to sign the back of the stock certificate and mail it to the corporation. Plaintiffs did so, but included with the certificate a letter stating that by accepting the offer, plaintiffs reserved their rights under federal and state law. The corporation found the language unacceptable and declined to purchase the shares, instead returning the certificate to plaintiffs. Concerned about possessing a signed stock certificate, plaintiffs ultimately visited the corporation and surrendered the endorsed certificate in exchange for a new one. Plaintiffs then brought a breach of contract suit claiming $64,933.60 in damages, asserting that the corporation had breached its offer to repurchase the stock. The corporation denied that a contract offer existed, arguing that plaintiffs' reply was not an acceptance but rather a counteroffer, and asserted that even if a contract did exist, plaintiffs had waived their rights under it by forfeiting the endorsed certificate in favor of a new one and by failing to immediately assert their rights under the contract. A jury found that the corporation had breached its contract, causing damages in the amount of $64,933.60, but then entered a verdict for the corporation on grounds that the corporation had proved at least one of its affirmative defenses of rescission, release, waiver, or accord and satisfaction. On appeal, the Supreme Court noted that only in rare cases should a jury verdict be set aside but reversed the verdict nevertheless on grounds that, even drawing all legitimate inferences in favor of the corporation, there was a complete absence of probative evidence supporting any of the corporation's affirmative defenses. The case was remanded for entry of judgment of $64,933.60 in favor of plaintiffs. Benson v. Diverse Computer Corp., 2004 MT 114, 321 M 140, 89 P3d 981 (2004), followed in Harland v. Anderson Ranch Co., 2004 MT 132, 321 M 338, 92 P3d 1160 (2004).

Federal Law Regarding Nonliability for Borrower's Payment of Fees to Lender Upon Loan Rescission Inapplicable to Mortgage Broker Fees: Plaintiff helped defendant secure a loan, which defendant subsequently rescinded within the applicable 3-day period pursuant to the federal Truth in Lending Act. Plaintiff sent defendant a bill for its brokerage fee and out-of-pocket expenses incurred in securing the loan commitment, as provided in the brokerage contract and an attendant promissory note. Defendant refused to pay the bill, and plaintiff brought an action to enforce the contract and promissory note, and the District Court enforced the note and ordered defendant to pay the bill. Defendant appealed on grounds that 16 U.S.C. 1635(b) of the Truth in Lending Act and 12 CFR 226.23, Regulation Z, clearly provide that when a consumer rescinds a transaction, the consumer is not liable for any amount, including any finance charge. The Supreme Court affirmed the District Court ruling. Although the federal law protects defendant from paying any fees to the lender, it does not address arrangements between a borrower and a mortgage broker, and in fact, portions of Regulation Z at 12 CFR 226.4(a) expressly exclude appraisal and service fees from the definition of a finance charge. Therefore, even though defendant effectively rescinded that mortgage with the lender, the rescission did not affect or alter defendant's obligation to the mortgage broker pursuant to the brokerage contract and promissory note. Mortgage Source, Inc. v. Strong, 2003 MT 205, 317 M 37, 75 P3d 304 (2003).

Dispute Over Contract to Deliver Log Home — No Requirement That Seller Provide Name of Third Party Boom Truck Operator — Rescission Proper Remedy for Material Breach of Contract: Anderson agreed to purchase a log home from Eschenbacher. The home was designed to be constructed on Anderson's homesite. Eschenbacher drafted the purchase contract, which provided that Eschenbacher would act only as a manufacturer, not as a building contractor, and also required Anderson to coordinate and ensure availability of a boom truck to assemble the structure at the site. Anderson contacted a third party to supply a boom truck instead of using Eschenbacher's truck. Eschenbacher then refused to deliver the logs unless Anderson supplied the name of the other boom truck operator. Both parties sued for breach of contract. The District Court concluded that Anderson was under no duty to provide Eschenbacher with the name of the boom truck operator, and the Supreme Court agreed. The contract clearly placed the responsibility for acquiring a boom truck with Anderson, but did not require Eschenbacher to use it, because other language required Anderson to pay any expenses incurred by Eschenbacher for waiting once the logs were delivered, if, for instance, the boom truck that Anderson provided was inadequate. Construing the contract most strongly against the drafter, Eschenbacher, the court found that Eschenbacher could easily have inserted provisions in the contract regarding specifications of an adequate boom truck, but he did not. Eschenbacher materially breached the contract by refusing to deliver the logs until the boom truck dispute was settled. The contract did not specify a remedy; thus, the District Court did not err in granting Anderson rescission of the contract. Eschenbacher v. Anderson, 2001 MT 206, 306 M 321, 34 P3d 87 (2001).

Lack of Justification in Relying on Allegedly False Information — Claim of Negligent Misrepresentation Properly Dismissed: Following termination from employment with Bitterroot International Systems, Inc. (Bitterroot), Knutson sought to exercise his buyout rights under the shareholders' agreement. Bitterroot refused to pay and sought rescission on grounds of negligent misrepresentation, alleging that Bitterroot relied on Knutson's allegedly false information regarding the value of stock acquired through purchase of another company. However, the definition of negligent misrepresentation set out in St. Bank of Townsend v. Maryann's, Inc., 204 M 21, 664 P2d 295 (1983), requires that the party asserting that defense was justified in relying on the allegedly false information. In this case, Spencer, majority shareholder and president of both Bitterroot and the company that was acquired, knew the respective values of both companies and their stocks and knew that the book values were disparate at the time of the transaction. Thus, Spencer's assertion that he was misled by Knutson was neither credible nor supported by the record, and the District Court correctly dismissed Spencer's claim of negligent misrepresentation. Knutson v. Bitterroot Int'l Sys., Inc., 2000 MT 203, 300 M 511, 5 P3d 554, 57 St. Rep. 800 (2000).

Misvaluation of Corporate Stock Not Constituting Breach of Fiduciary Duty: Following termination from employment with Bitterroot International Systems, Inc. (Bitterroot), Knutson sought to exercise his buyout rights under the shareholders' agreement. Bitterroot refused to pay and sought rescission on grounds that Knutson breached his fiduciary duty to Bitterroot, arguing that Knutson's mistaken valuation of stock acquired during the purchase of another business constituted a breach of that duty. Bitterroot did not contend that Knutson acted in bad faith, but only that he was wrong about the stock value. Applying the standard in 35-1-443 (now repealed), the Supreme Court found that Knutson's inaccurate stock valuation did not constitute a breach of fiduciary duty and that the District Court did not err in dismissing Bitterroot's claim that Knutson breached his fiduciary obligation. Knutson v. Bitterroot Int'l Sys., Inc., 2000 MT 203, 300 M 511, 5 P3d 554, 57 St. Rep. 800 (2000). See also 18A Am. Jur. 2d Corporations § 451 and 18B Am. Jur. 2d Corporations § 1705.

Truth Regarding Value of Stock Discoverable by Party Claiming Estoppel — Defense Not Available: Following termination from employment with Bitterroot International Systems, Inc. (Bitterroot), Knutson sought to exercise his buyout rights under the shareholders' agreement. Bitterroot refused to pay and sought rescission on grounds of equitable estoppel, arguing that stock had been mistakenly valued during the purchase of another business, that Spencer, majority shareholder and president of both Bitterroot and the company that was acquired, relied on Knutson's valuation to Spencer's detriment, and that Spencer was unaware of factors that Knutson failed to consider. Spencer may have been mistaken about the value of the stock, but he was in a position to discover all the information necessary to value it and participated in its valuation. The truth regarding the stocks' value was as discoverable to Spencer as to anyone else, and the District Court did not err in dismissing Bitterroot's defense of equitable estoppel. Knutson v. Bitterroot Int'l Sys., Inc., 2000 MT 203, 300 M 511, 5 P3d 554, 57 St. Rep. 800 (2000), following Elk Park Ranch, Inc. v. Park County, 282 M 154, 935 P2d 1131 (1997).

Failure to Timely Enforce Contract Provision Insufficient of Itself to Constitute Waiver — Proof of Waiver — Reasonable Diligence Required of Rescinding Party: Mere failure to take steps to enforce a legal right under a contract in a timely manner is not, by itself, sufficient to constitute proof of waiver. Rather, a party claiming waiver must prove that the language or conduct by the other party showed unequivocally that the party voluntarily and intentionally relinquished the right to receive the full benefit of the contract. (See Pipe Indus. Ins. Fund Trust v. Consol. Pipe Trades Trust, 233 M 162, 760 P2d 711, 45 St. Rep. 1392 (1988).) Even though a party may be entitled to rescind a contract because of failure of consideration, the rescinding party must take action within a reasonable time upon discovering the facts that enable the rescission. Here, the District Court erred in concluding, without first determining whether the provisions of 28-2-1713 were complied with, that purchasers under a contract could rescind for failure of consideration. Norwood v. Serv. Distrib., Inc., 2000 MT 4, 297 M 473, 994 P2d 25, 57 St. Rep. 8 (2000), following Liddle v. Petty, 249 M 442, 816 P2d 1066, 48 St. Rep. 779 (1991).

Specification of Acreage Quantities by Approximation Indicative of Sale of Property in Gross: Language in a deed conveyed property described as "about 7 acres" and "approximately 7 acres". The actual legal description of the property was omitted from the chain of title beginning in 1950 and was not included in any subsequent deed, although the property was resold two more times. In a quiet title action, the District Court ruled that the size of the parcel was unimportant because the property had been conveyed in gross, with each party taking the risk of the actual quantity varying, so the exact quantity was immaterial. The Supreme Court agreed. Although words of estimation alone do not necessarily create a sale in gross, the plain meaning of the words "about" and "approximately" indicated that the parties did not intend to convey a precise number of acres, and the specification of acreage quantities, when qualified by words of approximation, rendered the acreage quantities merely descriptive rather than material to the agreement, thus indicating a sale in gross. Because the conveyance was a sale in gross, the variation in acreage was not grounds for rescission, nor did the acreage discrepancies in the relevant conveyances raise a genuine issue of material fact precluding summary judgment because the grantor's acreage-consistent description of the property boundaries controlled over the inconsistent acreage estimates in the conveyances. Cedar Lane Ranch, Inc. v. Lundberg, 1999 MT 299, 297 M 145, 991 P2d 440, 56 St. Rep. 1207 (1999), following Hardin v. Hill, 149 M 68, 423 P2d 309 (1967), and Turner v. Ferrin, 232 M 146, 757 P2d 335, 45 St. Rep. 946 (1988).

Equipment Rental Agreement Not Mutually Rescinded: Carl Weissman & Sons (CWS) agreed to rent a rock drill to D&L Thomas Equipment (D&L). A clause in the rental agreement required D&L to inspect the drill and notify CWS within 10 days specifying any defects and provided that if CWS was not notified, the drill would be conclusively presumed to have been accepted in its condition at the time of receipt. D&L contended that there were problems with the drill immediately after it was received, but did not notify CWS in writing within the 10-day period specified in the rental agreement. A fax sent by CWS expressed regret that the machine didn't work out and requested that the drill not be returned pending diversion to another location. D&L asserted that the fax constituted proof that the agreement had been canceled. A contract may be rescinded if all the parties consent and if mutual cancellation is clearly expressed and acts and conduct of the parties are clear, convincing, and inconsistent with the existence of the contract. In this case, the fax and the actions of the parties did not amount to a clear expression of the intent necessary to establish mutual rescission. Carl Weissman & Sons v. D&L Thomas Equip. Corp., 1998 MT 213, 290 M 433, 963 P2d 1263, 55 St. Rep. 896 (1998).

Rescission Not Allowed When Return to Precontract Status Not Possible: Lutes sought to rescind a contract based on the fact that he mistakenly believed that the sump system in a business that he purchased had the proper permits. The District Court correctly concluded that rescission was not proper because rescission would not restore Houdashelts, the property sellers, to their precontract position. Houdashelts had sold Lutes a profitable business with a working sump system, permitted or not, and, upon repossession, received back a business that was losing money, that had a dwindling customer base, and that had a large pollution problem that was caused by Lutes. Houdashelt v. Lutes, 282 M 435, 938 P2d 665, 54 St. Rep. 420 (1997).

Mutual Mistake of Any Material Fact as Warranting Rescission of Workers' Compensation Settlement: South injured her back on the job and underwent surgery twice to correct the problems. She entered into a full and final compromise settlement agreement with her insurer. The agreement listed seven jobs that both parties felt were acceptable for South to do. One of the jobs was massage therapy. South began training as a massage therapist but began experiencing back pain again, forcing her to quit the training and to undergo back surgery a third time. South then petitioned the Workers' Compensation Court to rescind the settlement agreement on grounds of mutual mistake of fact. The court denied her petition, treating the current problem as a new and different injury. The Supreme Court clarified Kienas v. Peterson, 191 M 325, 624 P2d 1 (1980), in holding that under fundamental contract principles for rescission, a mutual mistake regarding the nature or extent of a claimant's injury is not the only mutual mistake sufficient to set aside a final settlement agreement. Rather, if a party can show a mutual mistake of any material fact that impacts the contract to such an extent that the intended bargain of the parties is defeated, the contract may be rescinded. The operative question is whether a mutual mistake existed that justified rescission, without limitation to how or when the mistake was made. Even though the parties were not mistaken regarding the nature and extent of South's injury at the time that the contract was formed, both parties mistakenly believed that massage therapy was an appropriate job for South to pursue, and she relied on that fact to her detriment. It was error for the Workers' Compensation Court to fail to consider South's contention of mutual mistake regarding the propriety of the job approved for her to do; thus, she was entitled to rescission of the settlement agreement. South v. Transp. Ins. Co., 275 M 397, 913 P2d 233, 53 St. Rep. 196 (1996).

Modification Proper Despite Wife's Limited Capacity: After the parties' divorce, the husband, Arthur, was given an opportunity to retire early from the railroad. He contacted his ex-wife, Shirley, and the parties modified the divorce settlement to allow him to take early retirement. At the hearing to modify the decree, Shirley's attorney argued that the modification was inequitable and that Shirley had been diagnosed with a schizoaffective disorder so that she was unable to give an informed consent to the modification. The Supreme Court held that the evidence indicated that Shirley was better off under the new agreement and that the evidence also showed that the modification negotiations between the parties were amiable and that Shirley had consulted with her adult children and parents prior to signing the agreement. In re Marriage of Brownell, 263 M 78, 865 P2d 307, 50 St. Rep. 1714 (1993).

Challenge of Validity of Release on Basis of Unconscionability — Summary Judgment Improper: Plaintiff signed a release for personal injuries with an insurance company in exchange for $8,900. Plaintiff later sued insureds, who were granted summary judgment after pleading the affirmative defense of release. However, a release is governed by contract law and may be rescinded for the same reasons that allow rescission of a contract. Therefore, the validity of a release may be challenged on the basis of unconscionability. The Supreme Court reversed the grant of summary judgment after finding the release was unconscionable based on: (1) plaintiff's dire financial situation, lack of education and legal advice, and vulnerability; (2) substantial uncertainty as to the extent of injury and future prognosis at the time of settlement; and (3) haste in executing the release. Taken together, the circumstances raised an issue of fact whether justice was done, precluding summary judgment. Kelly v. Widner, 236 M 523, 771 P2d 142, 46 St. Rep. 591 (1989).

Commission as Evidence of Fiduciary Relationship — Rescission by Principal: The District Court did not err in relying on the explicit definition of the word "commission" in finding that a real estate agent who was granted a commission for the sale of a resort while intending to be one of the ultimate purchasers was acting in a fiduciary capacity in his relationship with the principal. Because the relationship existed, the sales agreement was voidable and subject to rescission by the principal. Boyne, U.S.A., Inc. v. Mallas, 236 M 305, 769 P2d 1235, 46 St. Rep. 380 (1989).

Variation in Acreage of Land Sold in Gross — Not Grounds for Rescission: Generally when land is sold in gross, a variation in acreage from what the parties had contemplated is not grounds for rescission. A bulk real estate transaction in which plaintiffs purchased "96.73 acres, more or less" was found to be a sale in gross, and a 6% acreage variation was held immaterial. Turner v. Ferrin, 232 M 146, 757 P2d 335, 45 St. Rep. 946 (1988), citing Hardin v. Hill, 149 M 68, 423 P2d 309 (1967), and followed in Cedar Lane Ranch, Inc. v. Lundberg, 1999 MT 299, 297 M 145, 991 P2d 440, 56 St. Rep. 1207 (1999).

Valid Release of Insurance Claims as Binding: Plaintiff injured in an automobile accident received $4,362.85 for medical expenses, lost wages, car rental costs, headaches, and inconvenience. In return for the settlement payments, the adjuster obtained a general liability release discharging the insurance company "from all claims, demands, damages, actions, causes of action or suits of any kind or nature whatsoever . . . [for] all injuries, known or unknown". Plaintiff sent a thank you note to the adjuster to express her pleasure with the "settlement and prompt service" but also retained an attorney on the case who attempted to obtain rescission of the release after receiving a copy of plaintiff's medical report. Rescission was denied upon a finding that plaintiff executed a valid release of all claims and that the terms of the agreement and release were clear and unambiguous. Plaintiff was bound by the settlement terms. Hanson v. Oljar, 231 M 272, 752 P2d 187, 45 St. Rep. 602 (1988).

Costs Provided by Contract Allowable Despite Tortious Nature of Claim: In an action by plaintiff to rescind a contract for sale of real property because of alleged fraud, misrepresentation, undue influence, and unconscionability, the award of attorney fees and costs that the contract provided to the successful defendant, relating to his defense and counterclaim of wrongful occupation by the plaintiff, was proper notwithstanding the contention that the action sounded in tort and not in contract (citing Winer v. Jonal Corp., 169 M 247, 545 P2d 1094 (1976)). The underlying action was based on a contract dispute. Westlake v. Osborne, 230 M 364, 750 P2d 444, 45 St. Rep. 277 (1988).

Completion of Survey Not Condition Precedent: Buyer breached buy-sell agreement, claiming he is entitled to rescission because of sellers' refusal to permit a survey of the real property prior to closing of the sale. The court properly held that there is no language in the contract indicating completion of a survey to be a condition precedent to closing. Because the sellers had performed all material conditions precedent, they are entitled to specific performance. Hillstrom v. O'Neil, 226 M 452, 736 P2d 126, 44 St. Rep. 795 (1987).

Alteration of Oral Contract — Rescission — Damages: Plaintiffs had an oral agreement with defendants to pay one-half of defendants' purchase price under defendants' written contract for deed for purchase of certain real property with the understanding that plaintiffs' names would be added to the title as copurchasers. Without plaintiffs' consent, defendants made written assignment of their interests under the written contract to a third party, retaining a life estate to themselves. Plaintiffs refused to make further payments and sued for damages and to quiet title in themselves. The District Court denied plaintiffs' claims and in effect found plaintiffs to be the breaching party. The Supreme Court found plaintiffs were entitled to rescission and reversed the District Court decision. Defendants' assignment while retaining a life estate constituted a material alteration of the oral agreement to which plaintiffs had not consented. Defendants' breach entitled plaintiffs to recover money they had paid on the contract with interest. Forsythe v. Elkins, 216 M 108, 700 P2d 596, 42 St. Rep. 680 (1985).

Laches Defense Unavailable — First Raised on Appeal: Laches could not be raised for the first time on appeal as a defense to action for rescission of contract for the sale of a ranch because it is an affirmative defense that must be set forth in the answer. Deist v. Wachholz, 208 M 207, 678 P2d 188, 41 St. Rep. 286 (1984).

Exemplary Damages: In an action to rescind a contract to purchase an automobile, there was no requirement that plaintiff show malice, oppression, or fraud on the part of the seller in order to recover exemplary damages under 30-14-133. T & W Chevrolet v. Darvial, 196 M 287, 641 P2d 1368, 39 St. Rep. 112 (1982).

Waiver of Right of Rescission: After purchasing automobile from defendant, plaintiff learned of a substantial dangerous defect in the automobile. Plaintiff promptly notified defendant of defect and during week following defendant's inspection of automobile gave notice of rescission of purchase contract. Court held plaintiff acted properly and in a timely fashion in rescinding the contract. T & W Chevrolet v. Darvial, 196 M 287, 641 P2d 1368, 39 St. Rep. 112 (1982).

Failure to Make Contract for Deed Payments: Where buyer of real estate under contract for deed failed to make two monthly payments, notice of default was sent to his address by registered mail as required by the contract, and buyer did not claim the notice at the post office when he knew it was there or make payment, the lower court properly terminated the contract and granted possession of the property to sellers. Hares v. Nelson, 195 M 463, 637 P2d 19, 38 St. Rep. 2036 (1981), followed in Wise v. Sebena, 248 M 32, 808 P2d 494, 48 St. Rep. 309 (1991).

No Rescission When Prior Breach: The plaintiff in a breach of contract action had hired a second contractor to finish building a basement after the first contractor had breached. The defendants argued that the plaintiff had thereby rescinded the contract and that they were thereby entitled to the reasonable value of the work performed to that point. The Supreme Court noted that the trial court decision was based on a prior breach of contract by the defendants and therefore concluded the argument lacked merit. Carriger v. Ballenger, 192 M 479, 628 P2d 1106, 38 St. Rep. 864 (1981).

Contracts — Defaulting Party's Right to Accounting — Contract Entire or Divisible: To determine whether or not a party defaulting on a contract is entitled to an accounting (either contractually or equitably), it must be determined first whether the contract was entire or severable. This depends very largely on contractual terms and on the intention of the parties disclosed by those terms. As a general rule, a contract is entire when by its terms, nature, and purpose it contemplates and intends that each and all of its parts are interdependent and common to one another and to the consideration. A contract contemplating the feeding of cattle by one party until 80% graded "choice", followed by sale and splitting of the proceeds with the supplier of the cattle, was held clearly intended to be entire and nonseverable. The feeder's default and abandonment completely frustrated the purpose, intent, and terms of the joint venture agreement. The feeder thereby forfeited any right it may have had to an accounting under the contract. When the joint venture was destroyed by abandonment by one of the joint venturers, equity would not compel an accounting because a wrongdoer may not take advantage of his own wrong. Roundup Cattle Feeders v. Horpestad, 184 M 480, 603 P2d 1044 (1979), distinguishing Murphy v. Redland, 178 M 296, 583 P2d 1049 (1978).

Impossibility of Performance of Contract: A joint venture was formed, the contract contemplating the feeding of cattle by one party until 80% graded "choice", followed by sale and splitting of the proceeds with the supplier of cattle, who was the second party. A drop in cattle prices which caused the feeder to lose his financing was not a case of commercial impossibility for two reasons. First, in order for commercial impossibility to excuse performance of a contract, the parties thereto must have had no reason to foresee the impossibility at the time they contracted. Fluctuation in cattle prices is foreseeable prior to the breach. On the contrary, a contract against the feeder for damages was upheld. Second, in order for commercial impossibility to excuse performance, the contractual duties must be impossible for anyone to perform. Subjective (personal) impossibility does not inhere to the nature of the act to be performed and does not excuse nonperformance. A loss of financing is personal impossibility. Roundup Cattle Feeders v. Horpestad, 184 M 480, 603 P2d 1044 (1979), distinguishing Murphy v. Redland, 178 M 296, 583 P2d 1049 (1978).

Tender of Performance — Real Estate Contract: Where time is not of the essence, a vendor is not entitled to rescind a real estate buy/sell contract without first tendering performance on his part, such as by tendering a deed and demanding performance by the purchaser and allowing a reasonable time to elapse. Ingalls v. Brady, 180 M 443, 591 P2d 200 (1979).

Franchise Agreement: The court decided that duties of a franchisor by necessary implication were conditions precedent if construing them as covenants or concurrent duties would leave a franchisee without an adequate remedy for a breach of those obligations by franchisor. United Campgrounds, U.S.A. v. Stevenson, 175 M 17, 571 P2d 1161 (1977).

Plaintiff's Duty of Care — Reasonable and Cautious Businessman: In an action for rescission of a contract plaintiff was under a legal duty to execute the sale agreement with the prudence and care of a reasonable and cautious businessman. When the evidence shows a failure to exercise such care, plaintiff cannot obtain relief from a court of equity on the ground of unilateral mistake of fact. Quinn v. Briggs, 172 M 468, 565 P2d 297 (1977).

Expression of Opinion: Sellers' representation that motel was "capable" of producing certain income was an expression of opinion and would not warrant rescission of contract. Beierle v. Taylor, 164 M 436, 524 P2d 783 (1974).

Failure to Furnish Bill of Sale: Sellers' failure to furnish bill of sale for motel furnishings which resulted in no damage to the buyer cannot be the basis for rescission. Beierle v. Taylor, 164 M 436, 524 P2d 783 (1974).

Where Notice of Rescission Stipulated: Where a particular form of notice, or notice for a given length of time, is stipulated for in contract, exact compliance therewith is necessary, and giving of prescribed notice is absolutely an essential prerequisite to rescission or cancellation of contract. Tomsheck v. Doran, 126 M 598, 256 P2d 583 (1953).

Party Seeking Rescission Must Be Free From Fault: This section authorizing rescission of a contract for failure of consideration contemplates that the party seeking rescission must himself be free from fault; where it appeared that the buyer of automobiles under his contract was given the option to fix the time of delivery at "buyer's option when possible" but did not exercise the option until it was impossible for the seller to make delivery of the model specified, he could not make his own neglect the basis for rescission, and judgment in his favor was reversed. Polich Trading Co. v. Billings Hudson Terraplane Co., 114 M 446, 137 P2d 661 (1943).

Defective Title as Grounds for Rescission:

The purchaser under an executory land contract is not entitled to rescind on the ground of failure of title in the vendor so long as the latter is not in default. Wilson v. Corcoran, 73 M 529, 237 P 521 (1925).

One may in good faith lawfully contract to sell land to which he has not perfect or any title, and the fact that his title is imperfect does not authorize the purchaser to rescind the contract; if at the time he is required to make conveyance the vendor is ready, able, and willing to convey the title he contracted to convey, he is not in default. Wilson v. Corcoran, 73 M 529, 237 P 521 (1925).

Distinction Between Cancellation and Rescission: Where purchaser of land under a contract of sale failed to pay installments as they became due, the vendor, seeking cancellation of contract as a cloud upon his title, was not required to allege in his complaint that he had restored or offered to restore partial payments theretofore made as he would have been compelled to do in an action to rescind the contract. Suburban Homes Co. v. North, 50 M 108, 145 P 2 (1914). See also Oscarson v. Grain Growers Ass'n, Inc., 84 M 521, 277 P 14 (1929).

When Rescission Available: A rescission is available where a contract has been made and the consent of the party seeking it actually had, but given by mistake or obtained through duress, menace, fraud, or undue influence. Michalsky v. Centennial Brewing Co., 48 M 1, 134 P 307 (1913).

Compliance With Rules Required: Under this section and 28-2-1713, a complainant undertaking to rescind a contract of purchase of stock, under which he paid certain money and demanding a return of the money, is not entitled to rescission where the existence of none of the grounds of rescission is shown and complainant has not complied with the prescribed rules governing rescission. Cotter v. Butte & Ruby Valley Smelting Co., 31 M 129, 77 P 509 (1904).

Attorney General's Opinions

Early Termination and Renewal of Contract Between Trustees and Superintendent Held Proper: A board of trustees and a District Superintendent may mutually terminate a 3-year employment contract prior to the expiration of its term and enter into another 3-year contract identical to the first except for date of expiration, without violating 20-4-401. 41 A.G. Op. 30 (1985).

28-2-1713. How rescission accomplished.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Transfer of Property by Elderly Parents to Children in Consideration for Support and Maintenance — Applicability of Grantor-Support Theory Rather Than Principles of Contractual Rescission: The parents granted property to their children on the condition that the children would provide support and maintenance for their parents. When the children breached the agreement, the parents sought to rescind the agreement. The District Court rescinded the agreement, and on appeal, the children contended that the formalities of this section should apply. The Supreme Court disagreed, holding that under these circumstances, the equitable principles inapplicable to ordinary conveyances did not apply. Rather, the court applied the equitable principles of the grantor-support theory of rescission set out in De Atley v. Streit, 81 M 382, 263 P 967 (1928). Under De Atley, a court may rescind a grantor-support agreement on numerous grounds, including failure of consideration, fraud in the transaction, or breach of a condition precedent. The children asserted that the theory did not apply because the parents had other means of support and were not under hardship. However, the agreement was rescinded because of the children's breach of their duty, not because of the parents' relative means or hardship. The children effectively excluded their father from decisionmaking at the family company, restricted the parents' traditional use of corporate funds for living expenses, closed the corporate checking account without notice to the parents, resulting in loss of the parents' health insurance premiums, refused to reimburse the parents for their assisted living, and cut off their long-distance telephone line. The children's actions were a material breach of the grantor-support agreement, and the District Court properly rescinded the agreement. Hjartarson v. Hjartarson, 2006 MT 273, 334 M 212, 147 P3d 164 (2006).

Formal Notice Not Always Requisite to Rescission of Contract: Formal notice of rescission is not always a requisite to rescinding a contract. Rather, it is only necessary that the party electing to rescind make a timely communication of that intention in some manner. The bringing of a prompt action is generally considered sufficient. Eschenbacher v. Anderson, 2001 MT 206, 306 M 321, 34 P3d 87 (2001), following Bozdech v. Mont. Ranches Co., 67 M 366, 216 P 319 (1923).

Failure to Timely Enforce Contract Provision Insufficient of Itself to Constitute Waiver — Proof of Waiver — Reasonable Diligence Required of Rescinding Party: Mere failure to take steps to enforce a legal right under a contract in a timely manner is not, by itself, sufficient to constitute proof of waiver. Rather, a party claiming waiver must prove that the language or conduct by the other party showed unequivocally that the party voluntarily and intentionally relinquished the right to receive the full benefit of the contract. (See Pipe Indus. Ins. Fund Trust v. Consol. Pipe Trades Trust, 233 M 162, 760 P2d 711, 45 St. Rep. 1392 (1988).) Even though a party may be entitled to rescind a contract because of failure of consideration, the rescinding party must take action within a reasonable time upon discovering the facts that enable the rescission. Here, the District Court erred in concluding, without first determining whether the provisions of this section were complied with, that purchasers under a contract could rescind for failure of consideration. Norwood v. Serv. Distrib., Inc., 2000 MT 4, 297 M 473, 994 P2d 25, 57 St. Rep. 8 (2000), following Liddle v. Petty, 249 M 442, 816 P2d 1066, 48 St. Rep. 779 (1991).

Chocolate Inventory Destroyed — Contamination Exclusion Inapplicable: After discovering that a worker had been exposed to hepatitis, the owners of Helena's Parrot Confectionery (the Parrot) immediately alerted the city health department. When the state Department of Health and Environmental Sciences (now Department of Public Health and Human Services) subsequently placed an embargo on all candy, the Parrot, without testing for contamination, voluntarily destroyed its existing inventory and submitted a claim for the loss to its insurance company. Citing the high probability of contamination and the contamination exclusion in the insurance contract, the District Court granted summary judgment in favor of the insurance company. Adopting the contamination definitions in Am. Cas. Co. of Reading, Pa. v. Myrick, 304 F2d 179 (5th Cir. 1962), Hi-G, Inc. v. St. Paul Fire & Marine Ins. Co., 391 F2d 924 (1st Cir. 1968), and Auten v. Employers Nat'l Ins. Co., 722 SW 2d 468 (Tex. App. 1987), the Supreme Court reversed, holding that absent proof of "actual" contamination, the contamination exclusion does not bar coverage for the Parrot's losses. Duensing v. Traveler's Co., 257 M 376, 849 P2d 203, 50 St. Rep. 316 (1993).

Contract for Deed — No Right of Buyer to Suspend Performance for Failure of Consideration Not Attributable to Sellers: Petty made the downpayment on a contract for deed that called for conveyance of part of the property to Petty upon downpayment. Petty assumed the property was unzoned. The contract stated that Petty would use the property for a recreational vehicle park and that if after Petty's due diligence Petty could not obtain zoning approval within 30 months after the contract was signed, the purchase price would be reduced by $25,000. The bank that held a preexisting mortgage on the property told Petty it would not release the property until he brought current his payments to the sellers and the bank. Over 30 months passed from the time of the downpayment until the sellers filed suit, during which time Petty made no payments to the sellers or the bank and did not obtain zoning approval. Petty did not request a deed until 27 months after making the downpayment. Petty was not entitled to suspend performance for failure of delivery of the deed and transfer of the property because he was accountable, not the sellers. The award of damages to the sellers was affirmed. Liddle v. Petty, 249 M 442, 816 P2d 1066, 48 St. Rep. 779 (1991), followed in Norwood v. Serv. Distrib., Inc., 2000 MT 4, 297 M 473, 994 P2d 25, 57 St. Rep. 8 (2000).

Duty of Party Rescinding to Act Promptly:

Purchasers bought a ranch in June 1986 but never offered to tender the property back, did not complain of fraud or misrepresentation in the sale until filing suit in late 1987, and treated the property as their own before and even subsequent to the suit. The statutory requirements of rescission were not met. Schweigert v. Fowler, 240 M 424, 784 P2d 405, 47 St. Rep. 1 (1990).

Rescission of a partnership agreement lies where consideration fails, but where there was no such failure upon creation of the relationship, but mere breaches in manner of operation after the relationship was established, it may not be resorted to; where defendant refused for several years to deliver to the partnership two pairs of foxes as part of the consideration to be furnished by him, for propagating silver foxes, plaintiff's complaint impliedly shows on its face, laches, and plaintiff chose to affirm the agreement instead of promptly rescinding it, hence subject to general demurrer. Lommasson v. Hall, 111 M 142, 106 P2d 1089 (1940).

One who bought what at the time he deemed a right to make immediate homestead entry of public land, but which subsequently proved to be no more than a possessory right on unsurveyed land, and with such knowledge entered the land as a homestead when declared open to settlement, made two partial payments under his agreement, and then, after expiration of 2 years, brought an action to rescind and recover back his payments, was not entitled to prevail. Hills v. Johnson, 52 M 65, 156 P 122 (1916).

Conduct Constituting Waiver of Right to Rescind: The District Court properly concluded that plaintiffs waived any right to rescind through conduct that was inconsistent with an intent to rescind, including: (1) encumbering the property with a deed of trust and assignment of contract for deed on the same day the notice of intent to rescind was sent; (2) continued use and occupancy of the property; and (3) disposal of items of personal property transferred under the contract after notice of rescission. Garcia v. Schell, 239 M 475, 781 P2d 274, 46 St. Rep. 1844 (1989).

Restore Value Received: The purchasers, who were allowed to rescind a real estate contract based upon mutual mistake of the parties, may recover the value of their equity in real property conveyed by them to the sellers as partial consideration for the contract subsequently rescinded. Brunner v. LaCasse, 234 M 368, 763 P2d 662, 45 St. Rep. 1978 (1988).

Rescission Barred by Laches: The Supreme Court held that plaintiffs' inability to completely restore defendants to their original condition would not alone foreclose rescission as a remedy. Plaintiffs had notice of circumstances that should have put them on inquiry of possible fraud at the time of sale in 1977 and in 1978 when the net income did not reflect earlier representations. Nevertheless, plaintiffs continued to make payments and operate the business without complaint until 1981. The court held that these facts constituted laches, or a failure to use reasonable diligence to rescind promptly on the part of the plaintiffs. Since the time period between notice of possible fraud and filing of a complaint exceeded the 2-year Statute of Limitations for fraud, the District Court erred in permitting the jury to consider rescission as a remedy for the plaintiffs. McGregor v. Cushman/Mommer, 220 M 98, 714 P2d 536, 43 St. Rep. 206 (1986), followed in Benson v. Pyfer, 240 M 175, 783 P2d 923, 46 St. Rep. 2033 (1989).

Compromise and Settlement — No Grounds for Rescission: Parties to a real estate transaction executed a promissory note in compromise and settlement of a dispute over the property. The sellers filed a complaint to recover on the promissory note. The defendants asserted two affirmative defenses seeking rescission of the note. The District Court granted plaintiffs' motion for summary judgment. The Supreme Court affirmed and held that the record substantiated that the note was supported by adequate consideration. The defendants did not timely rescind the note. There was no evidence that the plaintiffs could be restored to substantially the same position as if the note had not been made, and no issue of material fact precluded entry of summary judgment. Todd v. Berner, 214 M 263, 693 P2d 506, 41 St. Rep. 2462 (1984).

Rescission of Release — Facts Not Requiring Tender: Plaintiff was severely burned after a truck driven by an employee of H. Pierce Manufacturing Co. ran into the rear of her 1970 Ford Mustang, which caught fire. Plaintiff retained James Reno to represent her. Reno began negotiations with Pierce's insurer, St. Paul Fire and Marine Co. At the time Pierce was insured with St. Paul for up to $100,000 and with an excess carrier, Atlantic Co., for up to $2 million. Reno did not inquire as to what the excess carrier's coverage limits were. Reno and the adjuster agreed to a settlement entered by plaintiff for $300,000. Two separate documents consisting of the combined release and indemnification agreements and a subrogation agreement were executed. Reno agreed with the insurers to also pursue their interests against Ford. The insurers later retained independent counsel, and Reno filed an action against Ford. Plaintiff sought to rescind the release. Usually a party seeking to rescind must restore everything of value which they have received under the contract. Here, plaintiff received only $125,000 of the $300,000 settlement, however, and because of the severity of the injury and the acknowledged culpability of the driver and Pierce, plaintiff was entitled to rescind without tendering the settlement sum. Abell v. Ford Motor Co., 39 St. Rep. 1347 (D.C. Mont. 1982) (apparently not reported in Federal Supplement).

Exemplary Damages: In an action to rescind a contract to purchase an automobile, there was no requirement that plaintiff show malice, oppression, or fraud on the part of the seller in order to recover exemplary damages under 30-14-133. T & W Chevrolet v. Darvial, 196 M 287, 641 P2d 1368, 39 St. Rep. 112 (1982).

Waiver of Right of Rescission: After purchasing automobile from defendant, plaintiff learned of a substantial dangerous defect in the automobile. Plaintiff promptly notified defendant of defect and during week following defendant's inspection of automobile gave notice of rescission of purchase contract. Court held plaintiff acted properly and in a timely fashion in rescinding the contract. T & W Chevrolet v. Darvial, 196 M 287, 641 P2d 1368, 39 St. Rep. 112 (1982).

Mutual Mistake — Basis for Rescission: Defendants purchased an irregular tract of land and commenced construction of a commercial building. They were contacted by plaintiff concerning purchase of the building. They consulted an attorney and discussed condominiumizing the building. He suggested as a tax matter that defendant should hold the property long enough to qualify for long-term capital gain treatment. An option to purchase with contract for deed was entered. The deeds and contract were not completed, as a survey was needed for a legal description of the property. The contract contained a provision that defendants provide and pave parking lots north and south of the building. The survey was completed and showed that the building encroached on state and county rights-of-way to the north and south. Plaintiffs then sought to rescind the contract and recover their money. The Supreme Court held that the providing of parking lots was material to the contract and that mutual mistake of fact as to the parking lots was an adequate basis for rescinding the contract. They also held that any findings not made could be implied to support the trial court's decision. Berry v. Romain, 194 M 400, 632 P2d 1127, 38 St. Rep. 1434 (1981).

Effect of Rescission: A technical "rescission" of a contract has the legal effect of entitling each of the parties to be restored to the condition in which he was before the contract was made so far as that is possible, and in determining whether a rescission took place, the courts look not only to the language of the parties but to all the circumstances. Cruse v. Clawson, 137 M 439, 352 P2d 989 (1960).

Divisible Contract Susceptible of Partial Rescission: A contract for installment of furnace, pipes, air ducts, etc., was a divisible one and susceptible of partial rescission and court erred in ruling that the contract was indivisible and in failing to restore every part the purchaser failed in his attempted rescission and was therefore liable for the balance due on the plant. O'Keefe v. Routledge, 110 M 138, 103 P2d 307 (1940).

Restoration Such as Is Reasonably Possible: The object of this section and 28-2-1716, requiring one rescinding a contract to make compensation or restoration, is to place the other party in status quo, i.e., to place him in the same position he was in at the time of the execution of the contract, but absolute and literal restoration is not required, it being sufficient if the restoration be such as is reasonably possible or as may be demanded by the equities of the case. O'Keefe v. Routledge, 110 M 138, 103 P2d 307 (1940), followed in McGregor v. Cushman/Mommer, 220 M 98, 714 P2d 536, 43 St. Rep. 206 (1986), and in Carey v. Wallner, 223 M 260, 725 P2d 557, 43 St. Rep. 1706 (1986).

When Restoration Unnecessary:

Under this section one seeking rescission of a contract must restore or offer to restore to defendant everything of value received under it on condition that the latter shall do likewise. Where plaintiff's tender was refused and defendant threatened to declare a forfeiture unless the balance due was paid, it appearing further that defendant was without right to sell the property involved, it may not be said that plaintiff by remaining in possession waived his right to rescission. Rinio v. Kester, 99 M 1, 41 P2d 405 (1935).

The requirement of this section that before a party can rescind a contract he must restore or offer to restore to the other party everything of value received under it was sufficiently met by an allegation in a taxpayer's complaint that articles purchased under a fraudulent contract by defendant school trustees were in the school building and could be restored to the seller by the court's decree, the rule being that where restoration has been rendered impossible through no fault of plaintiff he may have relief, particularly if the court by its decree is able to bring about restoration. School District v. Richards, 62 M 141, 205 P 206 (1922).

Duty of Party Rescinding to Act Promptly — Fraud:

Where a vendee deems himself entitled to rescission of a land contract on the ground of fraud he must under this section act promptly upon discovery of the facts constituting fraud; if he had information of the facts, no matter from what source received, which if pursued would have resulted in knowledge, it will be held the equivalent of knowledge and failure to act thereon constitutes laches fatal to the action. Lasby v. Burgess, 88 M 49, 289 P 1028 (1930), followed in McGregor v. Cushman/Mommer, 220 M 98, 714 P2d 536, 43 St. Rep. 206 (1986).

Where the plaintiff seeks to rescind a contract on the ground of fraud the defendant is entitled to know when he discovered the facts constituting the fraud; a just ground for rescission may be lost by laches. Ott v. Pace, 43 M 82, 115 P 37 (1911).

The right to set aside a deed to mining property on the ground of fraud may be barred by laches in prosecuting a suit therefor, notwithstanding that the plaintiffs reside in a foreign country and are ignorant of our language and institutions. Streicher v. Murray, 36 M 45, 92 P 36 (1907).

Waiver of Right to Rescind:

Right to rescind a land contract on the ground of breach by the vendor for failure to deposit in escrow state land certificates at a certain time was waived by the purchaser by remaining in possession some 6 years after breach and doing no more than insisting from time to time that the vendor make the deposit. Friedrichsen v. Cobb, 84 M 238, 275 P 267 (1929).

While a party seeking to avoid a contract on the ground of the fraud must rescind promptly on discovery of the fraud or he will be deemed to have ratified it and waived his right to rescind, where the purchasers of farm machinery soon after discovery of defects notified the seller and were repeatedly assured that they would be remedied but without result, the delay in rescinding caused by such promises was justified and did not amount to a waiver of their right to rescind. Advance-Rumely Thresher Co., Inc. v. Wenholz, 80 M 82, 258 P 1085 (1927).

By continuing in possession of ranch property for more than 5 months after commencement of suit to rescind, the vendee waived his right of rescission under this section making it incumbent upon a party desiring to rescind to tender back possession and to keep the tender good by removal from the premises. Fontaine v. Lyng, 61 M 590, 202 P 1112 (1921). See also Beebe v. James, 91 M 403, 8 P2d 803 (1932).

Return to Status Quo: The effect of an agreement of rescission is to undo the contract. Rescission includes the idea of restoration of both parties to their status quo and the return by each to the other of the consideration given and received. Hollingsworth v. Ruckman, 72 M 147, 232 P 180 (1924).

Duty of Party Rescinding to Restore Property:

Under this section one desiring to rescind a contract must act promptly upon discovery of the facts which entitle him to rescind if he is aware of his right to rescind. He must restore or offer to restore to the other party everything of value which he has received from him under the contract. Smith v. Christie, 60 M 604, 201 P 1011 (1921). See also Silfvast v. Asplund, 93 M 584, 20 P2d 631 (1933); Beebe v. James, 91 M 403, 8 P2d 803 (1932); Williams v. Hefner, 89 M 361, 297 P 492 (1931); St. Onge v. Blakely, 76 M 1, 245 P 532 (1926); Edwards v. Muri, 73 M 339, 237 P 209 (1925); Rowe v. Emerson-Brantingham Implement Co., 61 M 73, 201 P 316 (1921).

A person injured by the fraudulent acts of another may elect to rescind or may affirm the transaction and sue for damages. In order to state a cause of action for rescission it is necessary for the complaining party to allege that he has restored to the other party everything of value which was received under the contract, or that he has offered to make restitution upon condition that the offending party do likewise unless it is made to appear that the latter is unable or positively refuses to do so. Como Orchard Land Co. v. Markham, 54 M 438, 171 P 274 (1918).

Duty of Party Rescinding to Act Promptly — Discovery of Facts:

Mistakes of law and mistakes of fact are, as possible bases for rescission, in pari materia; there is not, either as to the duty of discovery or the time of commencing suit, any distinction between them. Brundy v. Canby, 50 M 454, 148 P 315 (1915).

As to either a mistake of law or a mistake of fact, laches may arise from a culpable neglect to discover, but a court is not required to impute laches from a delay in discovery for a period of less than 9 months, merely because the mistake is one of law. Brundy v. Canby, 50 M 454, 148 P 315 (1915).

Whether a case is or is not one of laches depends upon circumstances affecting the party who seeks relief as well as the party against whom relief is sought; where the circumstances are such as to excuse a failure to discover, where also the situation of the parties has not changed, no occasion is offered to apply the doctrine of laches. Brundy v. Canby, 50 M 454, 148 P 315 (1915).

The prompt action required by this section is to occur after discovery. Brundy v. Canby, 50 M 454, 148 P 315 (1915).

To authorize the rescission of a contract of purchase, the buyer must, upon the discovery of facts authorizing a rescission, act promptly; the question of promptness is one for the jury. Hillman v. Luzon Cafe Co., 49 M 180, 142 P 641 (1914).

Pleading:
The rules prescribed by this section touching rescission are inapplicable to an action to enforce an immediate forfeiture of a contract of purchase for the vendee's failure to make any deferred payment, where the contract provides that such failure shall work an immediate forfeiture; hence it is not necessary for the complaint in such last-named action to set out facts sufficient to constitute a cause of action for the rescission of a contract. Fratt v. Daniels-Jones Co., 47 M 487, 133 P 700 (1913).

Where in a suit to rescind a contract for the sale of real estate the merits of the controversy were tried, plaintiffs introducing evidence that they had restored to defendants everything received from the latter under the contract though the complaint failed to allege that plaintiffs had placed defendants in status quo, as required by this section, the pleading will on appeal be treated as amended in this respect. Post v. Liberty, 45 M 1, 121 P 475 (1912).

Where one party to a contract is seeking its rescission, he must act promptly upon discovering the facts that entitle him to rescind; hence if he seeks to rescind on the ground of fraud he must act with reasonable promptness after discovering the fraud, and his complaint should show when the discovery was made; otherwise it is vulnerable to a special demurrer on the ground of being ambiguous, unintelligible, and uncertain. Ott v. Pace, 43 M 82, 115 P 37 (1911).

28-2-1714. When rescission may be adjudged.

Case Notes

Rescission of Waiver of Interest Document on Grounds of Fraud: Kindsfather's son purchased some land from Kindsfather pursuant to a contract for deed. When the son was unable to make the payments, the son executed a document waiving the back interest that was owing and Kindsfather signed the document. Kindsfather subsequently died, and the son sought a declaratory ruling that the waiver of interest document was valid and that upon receipt of the unpaid balance of the contract, the bank would release the warranty deed held in escrow for the son. Kindsfather's personal representative opposed the judgment, and the District Court found the document to be invalid and ordered the son to make all payments due to the estate. On appeal, the Supreme Court affirmed the District Court's decision to rescind the document because it was obtained by fraud. The Supreme Court examined each of the nine elements of actual fraud and determined that a prima facie case of actual fraud was established. In re Estate of Kindsfather, 2005 MT 51, 326 M 192, 108 P3d 487 (2005), following Davis v. Church of Jesus Christ of Latter Day Saints, 258 M 286, 852 P2d 640 (1993).

Punitive Damages Instruction — Malice: The court did not err in giving an instruction on implied malice that advised the jury that it is not necessary to show actual malice to recover punitive damages or in giving an instruction on punitive damages when it was clear from the record and a pretrial order that plaintiffs were bringing this case in tort, separate and distinct from any action arising out of contract. Harrington v. Holiday Rambler Corp., 176 M 37, 575 P2d 578 (1978).

28-2-1715. When rescission may be adjudged for mistake.

Case Notes

Rescission Not Allowed When Return to Precontract Status Not Possible: Lutes sought to rescind a contract based on the fact that he mistakenly believed that the sump system in a business that he purchased had the proper permits. The District Court correctly concluded that rescission was not proper because rescission would not restore Houdashelts, the property sellers, to their precontract position. Houdashelts had sold Lutes a profitable business with a working sump system, permitted or not, and, upon repossession, received back a business that was losing money, that had a dwindling customer base, and that had a large pollution problem that was caused by Lutes. Houdashelt v. Lutes, 282 M 435, 938 P2d 665, 54 St. Rep. 420 (1997).

Restore Value Received: The purchasers, who were allowed to rescind a real estate contract based upon mutual mistake of the parties, may recover the value of their equity in real property conveyed by them to the sellers as partial consideration for the contract subsequently rescinded. Brunner v. LaCasse, 234 M 368, 763 P2d 662, 45 St. Rep. 1978 (1988).

Compromise and Settlement — No Grounds for Rescission: Parties to a real estate transaction executed a promissory note in compromise and settlement of a dispute over the property. The sellers filed a complaint to recover on the promissory note. The defendants asserted two affirmative defenses seeking rescission of the note. The District Court granted plaintiffs' motion for summary judgment. The Supreme Court affirmed and held that the record substantiated that the note was supported by adequate consideration. The defendants did not timely rescind the note. There was no evidence that the plaintiffs could be restored to substantially the same position as if the note had not been made, and no issue of material fact precluded entry of summary judgment. Todd v. Berner, 214 M 263, 693 P2d 506, 41 St. Rep. 2462 (1984).

Doctrine of Restoration: The whole doctrine of restoration under this section and 28-2-1713 is equitable and requires merely that the party against whom rescission is adjudged shall be no worse off than before the contract. Brundy v. Canby, 50 M 454, 148 P 315 (1915).

28-2-1716. Power of court to require party rescinding to do equity.

Case Notes

Rescission Appropriate When Parties Cannot Agree on Exact Calculation of Damages — Literal Restoration Not Required by Section: Property owners and a builder entered an agreement for the construction of a home. The relationship between the parties deteriorated, and the property owners sued for breach of contract and other claims, with the builder denying the claims and asserting counterclaims. The District Court properly determined that the contract had been mutually rescinded. The builder asserted that rescission was improper because it was impossible to fully restore each party to their precontract position given that the parties disagreed as to the final accounting due. The builder also claimed that the District Court's calculation of damages did not account for the builder's intellectual capital, such as expertise and connections. The Supreme Court held that the literal restoration is not required under 28-2-1716 and that it was sufficient that the District Court had balanced the equities of each party's position by compensating the builder for labor and materials it provided and giving the owners a credit for the labor and materials they were owed. Jorgensen v. Trademark Woodworks, LLC, 2018 MT 291, 393 Mont. 381, 431 P.3d 29.

Federal Law Regarding Nonliability for Borrower's Payment of Fees to Lender Upon Loan Rescission Inapplicable to Mortgage Broker Fees: Plaintiff helped defendant secure a loan, which defendant subsequently rescinded within the applicable 3-day period pursuant to the federal Truth in Lending Act. Plaintiff sent defendant a bill for its brokerage fee and out-of-pocket expenses incurred in securing the loan commitment, as provided in the brokerage contract and an attendant promissory note. Defendant refused to pay the bill, and plaintiff brought an action to enforce the contract and promissory note, and the District Court enforced the note and ordered defendant to pay the bill. Defendant appealed on grounds that 16 U.S.C. 1635(b) of the Truth in Lending Act and 12 CFR 226.23, Regulation Z, clearly provide that when a consumer rescinds a transaction, the consumer is not liable for any amount, including any finance charge. The Supreme Court affirmed the District Court ruling. Although the federal law protects defendant from paying any fees to the lender, it does not address arrangements between a borrower and a mortgage broker, and in fact, portions of Regulation Z at 12 CFR 226.4(a) expressly exclude appraisal and service fees from the definition of a finance charge. Therefore, even though defendant effectively rescinded that mortgage with the lender, the rescission did not affect or alter defendant's obligation to the mortgage broker pursuant to the brokerage contract and promissory note. Mortgage Source, Inc. v. Strong, 2003 MT 205, 317 M 37, 75 P3d 304 (2003).

Equity Requires Payment of Prejudgment Interest: Plaintiffs, who rescinded contracts conveying real property, were entitled to prejudgment interest under the equitable theory. They had been deprived of their money for more than 8 years to date of judgment, while defendants received or were able to receive profits from the use of the land for nearly all those years. The act of one plaintiff in allowing another person to cut hay on the land did not constitute exercise of possession of the property sufficient to deny award of prejudgment interest. Brunner v. LaCasse, 234 M 368, 763 P2d 662, 45 St. Rep. 1978 (1988).

Reduction to Present Value of Amount Due Over Time: Court ordered contract for sale of ranch rescinded at request of seller. The buyers had already resold parts of the ranch to third parties at sums to be paid over a period of time and totaling $171,000. The lower court ordered that the full $171,000 due first buyers over time be tendered by first buyers to first seller as a setoff against the money first buyers had paid to first seller, which court ordered first seller to return to first buyers. The ordered setoff was erroneous as to amount, and the case was remanded for a determination of the present value of the $171,000, which figure would be the proper setoff. Deist v. Wachholz, 208 M 207, 678 P2d 188, 41 St. Rep. 286 (1984).

Absolute Restoration to Former Status Not Required — Horse Sale Rescission: The sale item, a mare, while in the possession of the seller and upon transferral to the buyer was with foal. The mare foaled while in the possession of the buyer and subsequently was bred by the buyer and was with foal a second time up through the time of trial. In adjudging a rescission of the contract for sale of the mare, the District Court was proper in allocating to the seller the mare with the unborn second foal and to the buyer the first foal plus the purchase price and the cost of keeping the mare and first foal. Here, even though complete restoration is not possible, the seller is not placed in a worse position by receiving the mare with a different foal. Restoration as contemplated within the meaning of this section does not mean absolute and literal replacement of the parties to their former position. Such restoration as is reasonably possible and demanded by the equities of the case is sufficient. (Citing O'Keefe v. Routledge, 110 M 138, 103 P 307 (1940).) Scott v. Hjelm, 188 M 375, 613 P2d 1385, 37 St. Rep. 1219 (1980). (Dissent by J. Sheehy.)

Restoration Such as Is Reasonably Possible: The object of this section and 28-2-1713, requiring one rescinding a contract to make compensation or restoration, is to place the other party in status quo, i.e., to place him in the same position he was in at the time of the execution of the contract, but absolute and literal restoration is not required, it being sufficient if the restoration be such as is reasonably possible or as may be demanded by the equities of the case. O'Keefe v. Routledge, 110 M 138, 103 P2d 307, 148 ALR 409 (1940), followed in McGregor v. Cushman/Mommer, 220 M 98, 714 P2d 536, 43 St. Rep. 206 (1986).

Allowance of Interest in Discretion of Court as "Justice May Require": While under this section the trial court may in an action for rescission of a contract require the party to whom the relief is granted to make restoration to his opponent, it is not incumbent upon it to allow or disallow interest in accordance with the strict rules of law applying to ordinary transactions, but may allow it to the vendor on certain items and to the vendee on others as "justice may require". Silfvast v. Asplund, 99 M 152, 42 P2d 452 (1935), explained in Brunner v. LaCasse, 234 M 368, 763 P2d 662, 45 St. Rep. 1978 (1988).

Reimbursement Upon Rescission: On rescission of an executory contract for the purchase of livestock, the buyer is entitled to the money paid as part of the purchase price and to be reimbursed for expenses for feed and care of the animals incurred prior to and within a reasonable time after rescission. Apple v. Edwards, 92 M 524, 16 P2d 700, 87 ALR 179 (1932).

Part 21

Payment of Construction Contractors and Subcontractors

Part Compiler's Comments

Effective Date: This part is effective October 1, 1999.

Applicability: Section 12, Ch. 470, L. 1999, provided: "[This act] applies to contracts agreed to on or after July 1, 1999."

Part Case Notes

Substantial Evidence to Support Award of Damages: In an action by the plaintiff contractor to foreclose a construction lien against the defendant homeowners, the District Court awarded contract damages to the plaintiff for $8,317 in contractor's fees, work completed, and materials used. The defendants appealed, arguing the District Court awarded damages to the plaintiff in error. On appeal, the Supreme Court affirmed, finding that the parties had formed an enforceable contract with sufficient consideration between them, even though the contract consisted of a written construction estimate from the plaintiff that did not include some important terms. The Supreme Court found there was sufficient evidence that the plaintiff was entitled to its contractor fee for driveway work, based on an oral modification to the agreement and the defendants' payment of contractor fees for other work, and found there was also sufficient evidence that the plaintiff was entitled to additional money related to labor and materials supplied for masonry and stonework. Vintage Constr., Inc., v. Feighner, 2017 MT 109, 387 Mont. 354, 394 P.3d 179.

Additional Costs Subcontractor's Responsibility: Given the nature of a fixed price contract, which generally places all responsibility for additional costs on the subcontractor, the District Court did not err in denying the subcontractor's claim for additional compensation when the subcontractor failed to submit written change orders in accordance with the contract or otherwise failed to establish oral agreements providing for payment of additional costs. Total Indus. Plant Serv., Inc. v. Turner Indus. Group, LLC, 2013 MT 5, 368 Mont. 189, 294 P.3d 363.

Waiver of Right to Object to Construction Contract Arbitration Provisions — Arbitration Properly Compelled: Plaintiff contracted to construct a pipeline and widen a road for defendant, but disputes arose regarding contract performance. The contract provided that disputes be settled by arbitration. Plaintiff notified defendant requesting arbitration, but defendant indicated a desire to settle the dispute through nonbinding mediation rather than arbitration in order to avoid fees. Subsequent settlement offers by defendant were refused, and plaintiff again requested arbitration. Following additional unsuccessful negotiation, plaintiff filed suit to enjoin arbitration, and defendant moved to stay litigation and compel arbitration. The District Court concluded that the contractual arbitration provisions were unambiguous and that by insisting on arbitration, plaintiff waived any legal objection to the arbitration provisions. Plaintiff appealed, but the Supreme Court affirmed. To establish a knowing waiver, the party asserting waiver must demonstrate the other party's knowledge of the existing right, acts inconsistent with that right, and resulting prejudice to the party asserting waiver. Here, plaintiff, through counsel, clearly had knowledge of its contractual rights regarding arbitration and litigation; letters from plaintiff's counsel were totally inconsistent with the right to object to arbitration; and the subsequent delay in resolving the matter and the additional cost to defendant in having to defend the arbitration provisions in District Court and on appeal were clearly prejudicial to defendant. The District Court correctly concluded that plaintiff waived the right to object to arbitration and properly compelled arbitration. VanDyke Constr. Co., Inc. v. Stillwater Min. Co., 2003 MT 279, 317 M 519, 78 P3d 844 (2003), followed, regarding elements of waiver, in R.C. Hobbs Enterprises, LLC v. J.G.L. Distrib., Inc., 2004 MT 396, 325 M 277, 104 P3d 503 (2004).

28-2-2101. Definitions.

Compiler's Comments

2003 Amendment: Chapter 274 in definition of owner inserted second sentence allowing an owner to contractually designate another person to represent the owner for certain purposes; deleted former definition of owner's representative that read: ""Owner's representative" means an architect, engineer, or other person who represents the owner and is designated in the contract as the person representing the owner for the purposes of the administration or oversight of the performance of the construction contract"; and made minor changes in style. Amendment effective October 1, 2003.

Applicability: Section 7, Ch. 274, L. 2003, provided: "[This act] applies to construction contracts entered into on or after October 1, 2003."

28-2-2102. Performance entitles contractor or subcontractor to payment.

Case Notes

Contractor Obligated by Prompt Payment Act to Pay Subcontractors — Arbitrator's Interim Award Upheld on Appeal — Attorney Fees and Costs Awarded to Party Defending Arbitrator's Award. M.K. Weeden Constr., Inc. v. Simbeck & Associates, Inc., 2022 MT 149, 409 Mont. 305, 514 P.3d 401.

28-2-2103. Payment to contractor and subcontractor.

Compiler's Comments

2003 Amendment — Code Commissioner Correction: Chapter 274 in (1)(a) at beginning deleted "If a contractor performs a construction contract according to the terms of the contract and requests, either directly to the owner or to owner's representative, payment for performance of the contract, the owner shall pay the contractor, within 30 days after receipt by the owner or the owner's representative of the request for payment, for work performed or materials provided in accordance with the contract"; inserted (1)(a) requiring that unless an alternative billing cycle is established, construction contracts define a monthly billing cycle; inserted (1)(b) providing that unless an alternative billing cycle is established, a request for payment is considered approved within 21 days unless the request for payment is disapproved; inserted (1)(c) concerning disapproval of a request for payment; inserted (1)(d) allowing an owner to withhold an amount sufficient to pay direct expenses; inserted (1)(e) requiring an owner to furnish a written statement specifying a condition for which approval of the payment is being withheld; inserted (1)(f) requiring payment within 7 days of approval unless an alternative billing cycle is established; inserted (1)(g) requiring an owner to notify a subcontractor who has not been paid of a progress payment or final payment made to the general contractor; inserted (1)(h) providing that payment is not required unless the contractor provides the owner a billing statement or estimate for work performed or material supplied; in (2) at beginning increased from 3 working days to 7 days the time within which a contractor must pay a subcontractor for work performed or materials provided; inserted (2)(b) providing that payment is not required unless the subcontractor provides a billing statement or invoice; inserted (2)(c) allowing the general contractor to disapprove the request for payment based on a written claim of certain conditions; in (3)(a) at beginning increased from 3 working days to 7 days the time within which a subcontractor must pay another subcontractor the amount due for work performed or materials provided; inserted (3)(b) providing that payment is not required unless the subcontractor provides a billing statement or invoice; and made minor changes in style. Amendment effective October 1, 2003.

As introduced, [section 1] of House Bill No. 438 (Ch. 274, L. 2003) amended this section by inserting an exception clause at the beginning of (1)(a), (1)(b), and (1)(f), referencing [section 2] of the bill (codified as 28-2-2115), which established an alternative billing cycle. House Bill No. 438

was subsequently amended by adding a new [section 1], amending 28-2-2101, but the internal reference to [section 2] in this section was not revised to reflect that amendment. Pursuant to sec. 138, Ch. 114, L. 2003, the code commissioner corrected the reference in the exception clause at the beginning of (1)(a), (1)(b), and (1)(f) of this section to reflect the original intent of House Bill No. 438 to provide an exception for an alternative billing cycle in 28-2-2115.

Applicability: Section 7, Ch. 274, L. 2003, provided: "[This act] applies to construction contracts entered into on or after October 1, 2003."

28-2-2104. Obligations upon delay of payment.

Compiler's Comments

2009 Amendment: Chapter 254 in (2) in first sentence after "30 days" deleted "plus 3 working days"; in (3) after "Acceptance of" deleted "progress payments or"; and made minor changes in style. Amendment effective October 1, 2009.

2005 Amendment: Chapter 244 in (3) deleted former first sentence that read: "Interest is not required to be paid pursuant to this section unless the owner, contractor, or subcontractor, as appropriate, has been notified of the requirements of this section at the time the request for payment is made." Amendment effective October 1, 2005.

Case Notes

Interest Assessment on Construction Lien Not Applicable to Residential Construction Improvements Less Than $400,000—Remand: As a discovery sanction and because the total cost of plaintiff's residential construction project exceeded $400,000, the District Court assessed interest against plaintiff on defendant's construction lien. The Supreme Court reversed and remanded. Although the total construction project cost exceeded $400,000, defendant's construction lien was based on improvements totaling only $16,763.81. The exception to the interest assessment clearly did not apply to the contract between the parties, nor could plaintiff be assessed interest as a discovery sanction based on a statute that did not apply. Weimar v. Lyons, 2007 MT 182, 338 M 242, 164 P3d 922 (2007).

Posttrial Motions to Amend Judgment, to Limit Punitive Damages, and for Attorney Fees Properly Denied: In a construction contract case, defendants filed numerous posttrial motions, including motions to amend the judgment, to limit the punitive damages award, and for attorney fees and costs. The motions were denied, and defendants appealed, but the Supreme Court affirmed. The motion to amend the judgment was unsupported by any authority. The motion to limit punitive damages was based on the statutory limit of 3% of net worth enacted by the 2003 Legislature, effective October 1, 2003, but the cause of action accrued prior to October 1, 2003, and the statutory limit did not apply retroactively. For the motion for attorney fees and costs to be granted, defendants would have to have been the prevailing party in the action, but defendants failed to provide any argument explaining how they were the prevailing party. Accordingly, the District Court did not err in denying the posttrial motions. Murphy Homes, Inc. v. Muller, 2007 MT 140, 337 M 411, 162 P3d 106 (2007).

28-2-2105. Prevailing party entitled to costs and attorney fees.

Case Notes

Contractor Obligated by Prompt Payment Act to Pay Subcontractors — Arbitrator's Interim Award Upheld on Appeal — Attorney Fees and Costs Awarded to Party Defending Arbitrator's Award. M.K. Weeden Constr., Inc. v. Simbeck & Associates, Inc., 2022 MT 149, 409 Mont. 305, 514 P.3d 401.

Sufficient Evidence Required to Show Issue of Material Fact—Contracts: The plaintiff entered into a contract with the defendant to provide the defendant with crushed aggregate material from his gravel pit. The defendant no longer needed the aggregate material and refused to pay the final invoices. The Supreme Court held that the District Court properly granted summary judgment to the plaintiff because the defendant failed to present sufficient evidence to establish that an issue of material fact existed regarding the amount of material extracted by the defendant. In addition, the Supreme Court awarded reasonable attorney fees, trial costs, and appeal costs to the plaintiff under 28-2-2105 and remanded the case to determine the fees and costs. Moore v. Goran, LLC, 2017 MT 208, 388 Mont. 340, 400 P.3d 729.

No Error in Denial of Untimely Motion to Amend Arbitration Award Containing Mathematical Error in Calculation of Attorney Fees: Defendant filed a motion under former Rule 59(g), M.R.Civ.P. (now superseded), to modify an arbitrated award of attorney fees that was $110,000 higher than the amount claimed by plaintiff's counsel. The District Court denied the motion and the Supreme Court affirmed on grounds that the award was time barred. Although a motion to amend an award is proper to modify an arbitration award that contains a mathematical error, the motion must be filed within 90 days of delivery of a copy of the award to the applicant pursuant to 27-5-313, or a correction may be requested of the arbitrator pursuant to 27-5-217. Defendant never requested a change of the award by the arbitrator and failed to challenge the calculation until more than 1 year after the award. Thus, even though the award was significantly inflated because of the mathematical error, the District Court did not abuse its discretion in denying defendant's motion under former Rule 59(g) to alter or amend the judgment. Dick Anderson Constr., Inc. v. Monroe Constr. Co., LLC, 2009 MT 416, 353 M 534, 221 P3d 675 (2009).

28-2-2107. Exception for certain residential dwellings.

Compiler's Comments

2001 Amendment: Chapter 364 substituted "residential projects or improvements to real property intended for residential purposes with a total cost of less than $400,000" for "improvements to real property intended for residential purposes that consist of four or fewer residential units". Amendment effective October 1, 2001.

Applicability: Section 4, Ch. 364, L. 2001, provided: "[This act] applies to contracts entered into or renewed after October 1, 2001."

Case Notes

Interest Assessment on Construction Lien Not Applicable to Residential Construction Improvements Less Than $400,000—Remand: As a discovery sanction and because the total cost of plaintiff's residential construction project exceeded $400,000, the District Court assessed interest against plaintiff on defendant's construction lien. The Supreme Court reversed and remanded. Although the total construction project cost exceeded $400,000, defendant's construction lien was based on improvements totaling only $16,763.81. The exception to the interest assessment clearly did not apply to the contract between the parties, nor could plaintiff be assessed interest as a discovery sanction based on a statute that did not apply. Weimar v. Lyons, 2007 MT 182, 338 M 242, 164 P3d 922 (2007).

28-2-2110. Limit on retainage.

Compiler's Comments

2005 Amendment: Chapter 244 in (1) after "exceed" substituted "5%" for "10% if the construction contractor is performing by the terms of the contract"; and inserted (3) requiring retainage to be released upon final acceptance of each portion of work for which a separate price is stated in construction contract. Amendment effective October 1, 2005.

Effective Date: This section is effective October 1, 2001.

Applicability: Section 4, Ch. 364, L. 2001, provided: "[This act] applies to contracts entered into or renewed after October 1, 2001."

28-2-2111. Construction contract indemnification provisions.

Compiler's Comments

Effective Date — Applicability: Section 3, Ch. 305, L. 2003, provided: "[This act] is effective July 1, 2003, and applies to construction contracts entered into or renewed on or after July 1, 2003."

28-2-2115. Alternative billing cycle.

Compiler's Comments

Effective Date: This section is effective October 1, 2003.

Applicability: Section 7, Ch. 274, L. 2003, provided: "[This act] applies to construction contracts entered into on or after October 1, 2003."

28-2-2116. Construction contracts — void provisions.

Compiler's Comments

Effective Date: This section is effective October 1, 2003.

Applicability: Section 7, Ch. 274, L. 2003, provided: "[This act] applies to construction contracts entered into on or after October 1, 2003."

Case Notes

Contractual Term Forbidding Construction Delay Pending Dispute Resolution — Failure to Approve Proposed Change Order Different From Failure to Make Monthly Progress Payments: A contractor argued that a provision of the contract that prohibited the contractor from delaying work pending the resolution of "any" and "all" disputes, including change orders submitted by the contractor, was void under 28-2-2116. The District Court disagreed. The court noted that the contract also contained an explicit exception to the prohibition in cases where monthly progress payments were not made. The District Court disagreed with the contractor's contention that a change order is the same as a monthly progress payment, and the Supreme Court affirmed on appeal. JEM Contracting, Inc. v. Morrison-Maierle, Inc., 2014 MT 21, 373 Mont. 391, 318 P.3d 678.

28-2-2117. Suspension of performance — termination.

Compiler's Comments

Effective Date: This section is effective October 1, 2003.

Applicability: Section 7, Ch. 274, L. 2003, provided: "[This act] applies to construction contracts entered into on or after October 1, 2003."

Part 22

Residential Construction — Disclosure and Warranty Requirements

28-2-2201. Residential construction contracts — disclosure and warranty requirements.

Compiler's Comments

Effective Date: This section is effective October 1, 2009.

Case Notes

Contract for Project Management of Repairs and Remediation Not Subject to Statutory Contract Requirements: When the written contract had an express purpose of environmental remediation and repairs, contemplated a two-phase remediation process consisting of the repairs and the reconstruction of a main house, and instructed the plaintiff to facilitate hiring a general contractor to reconstruct the main house, the District Court properly concluded that the plaintiff was a project manager rather than a general contractor under the contract. The contract was not subject to the statutory requirements under this section, and the plaintiff was entitled to the expectancy damages that arose when the defendant breached the contract. Flathead Management Partners, LLC v. Jystad, 2019 MT 289, 398 Mont. 121, 454 P.3d 679.

Contract to Build Home Not in Writing — Contract Void — Quantum Meruit Award Proper: The plaintiff sued the defendant, whom he had hired to build a home, after the defendant had filed a lien against the home because the plaintiff refused to pay the final invoice. The plaintiff claimed that the lien was invalid because the parties' agreement was not in writing, in violation of 28-2-2201. The District Court denied the plaintiff summary judgment, ordered the plaintiff to pay the invoice, and awarded the defendant attorney fees. The plaintiff appealed, arguing that the District Court had erred in awarding damages in equity because 28-2-2201 required the defendant's absolute forfeiture of damages. The Supreme Court disagreed and affirmed the award, holding that even though the contract between the parties was void, the statute did not preclude an award of equitable damages. Mandell v. Ward, 2016 MT 205, 384 Mont. 377, 377 P.3d 1228.

District Court Conclusion That Claims Were Inseparable for Calculation of Attorney Fee Award in Error — Remanded to Assess Reasonable Fees: The plaintiff sued the defendant he had hired to build a home after the defendant had filed a lien against the home because the plaintiff refused to pay the final invoice. The plaintiff claimed that the lien was invalid because the parties' agreement was void as it was not reduced to writing in violation of 28-2-2201. The District Court agreed that the contract was void but still ordered the plaintiff to pay the invoice under the theory of quantum meruit. The District Court also awarded the defendant attorney fees. The District Court concluded that the claims in contract and in equity against the defendant were inseparable and therefore awarded the defendant nearly all of his attorney fees. On appeal, the Supreme Court reversed the award of attorney fees, holding that the claims were not inseparable, and remanded the matter for the District Court to order a reasonable amount of fees. Mandell v. Ward, 2016 MT 205, 384 Mont. 377, 377 P.3d 1228.

28-2-2202. Disclosure and warranty requirements for sales of newly constructed residences.

Compiler's Comments

Effective Date: This section is effective October 1, 2009.

CHAPTER 3
INTERPRETATION OF CONTRACTS

Chapter Case Notes

Ambiguous Contract — Contract Construction — Award of Certain Damages Reversed: The plaintiff, a real estate brokerage firm, entered into an investment agreement with the defendant, a Montana corporation, to make three installment payments in exchange for a 33.33% interest in the plaintiff business. The defendant made the first two installment payments but refused to make the final payment. Following a bench trial, the District Court found that the contract was ambiguous, the mutual intention of the parties at the time of contracting was for the defendant to be an equal owner after making three payments, and that the defendant breached the investment agreement by not making the third payment while the plaintiff breached the operating agreement by withholding access to various financial records and information. The District Court awarded prejudgment interest, attorney fees and costs, and damages to both parties. Both parties appealed. The Supreme Court held that the District Court correctly ascertained the parties' mutual intent and that the agreement was ambiguous. However, the Supreme Court also held that the District Court lacked sufficient evidence to award damages for the plaintiff's breach of the operating agreement claims. AWIN Real Estate, LLC v. Whitehead Homes, Inc., 2020 MT 225, 401 Mont. 218, 472 P.3d 165.

Doctrine of Election of Remedies Inapplicable — Position of Blameless Party After Contractual Breach — Making Whole but No More: The plaintiff brought a suit for damages 6 years after the defendants breached a contract to buy the plaintiff's interests in Dealerspan, LLC, a software company, resulting in the defendants' forfeiture of their interests in Dealerspan. Defendants argued that the doctrine of election of remedies barred damages because the plaintiff elected to pursue forfeiture and thus had rescinded the contract. However, the subject of the contract was the sale of the plaintiff's interests, and the forfeiture of the defendants' interests in Dealerspan did not return the parties to their original positions before executing the contract, so the forfeiture and contractual damages were not inconsistent. Nevertheless, the contract was not designed to place the plaintiff in a better position under the defendants' breach than under the defendants' performance, so the plaintiff could recover only damages covering the difference between the contract purchase price and the value of the forfeited interests, subsequent profits from the business, and profits from selling Dealerspan's physical assets. Bottrell Family Investments Ltd. Partnership v. Diversified Financial, Inc., 2015 MT 185, 379 Mont. 504, 352 P.3d 620.

Title Policy Ensured Right of Access, Not "Legal Access" — No Coverage Under Clear Language of Title Policy: The plaintiffs purchased title insurance for real property they acquired. The policy insured against loss or damage from "lack of a right of access to and from the land". Later, the plaintiff learned that although they had access to the property from permissive, adjacent landowners, they did not have what they considered "legal access" to the property. The plaintiffs filed suit against the title company, arguing that the policy required the title company to provide them legal access to the property, such as a recorded easement dedicated to their use. The title company argued that the plaintiffs had access to their property and that the policy did not provide for any certain kind of access. The District Court agreed and granted the title company summary judgment. On appeal, the Supreme Court affirmed, noting that the language of the policy was clear in insuring against loss from not having "a right of" access and that the plaintiffs clearly had a right of access based on easements filed earlier. James v. Chicago Title Ins. Co., 2014 MT 325, 377 Mont. 264, 339 P.3d 420.

Interpretation of "Occupying" in Insurance Contract — Reasonable Connection Test — District Court Affirmed: When an employee of another subcontractor backed over him with a concrete truck, the foreman of a concrete finishing company was dragged up to 50 feet by the truck and later died from his injuries. His estate sought medical payments under the concrete truck's policy. The insurer denied the claim, contending that the policy's definition of "occupying" included only those who were "in, upon, getting in, on, out or off" the vehicle and thus the foreman was not occupying the vehicle at the time of the accident. The District Court agreed and granted summary judgment in favor of the insurer. The estate appealed. The Supreme Court affirmed, concluding that under the "reasonable connection" test, the foreman was not an occupant of the concrete truck because he was not associated with the truck for any purpose other than the accident. Estate of Richerson v. Cincinnati Ins. Co., 2011 MT 266, 362 Mont. 324, 264 P.3d 1087.

Diesel Fuel Properly Considered Pollutant for Purposes of Commercial Liability Insurance Policy Exclusion: A petroleum company held commercial liability and property insurance policies that contained a standard absolute pollution exclusion clause disclaiming coverage for spills resulting from pollutants, which were defined to include liquid irritants or contaminants. The company also held a coverage extension that provided coverage for expenses to extract pollutants from land or water. When a diesel fuel spill occurred on the company's property, the company sought insurance reimbursement under the policies and also submitted claims to the Montana Petroleum Tank Release Compensation Board for reimbursement for corrective action costs. The insurer denied the claim, and after the company subrogated the claim to the Board, the Board sought reimbursement from the insurer, but the insurer denied all reimbursement requests, so the Board sued to recover corrective costs from the insurer. The District Court concluded that diesel fuel was a pollutant and that coverage was therefore excluded under the commercial general liability portion of the policy. On appeal, the Board asserted that the court erred in denying coverage, but the Supreme Court affirmed. The terms of the pollution exclusion clause were not ambiguous, and when viewed from the objective perspective of the average consumer, diesel fuel was properly included in the definition of pollutant. The District Court correctly denied coverage under the commercial general liability portion of the policy disclaiming coverage for spills resulting from pollutants. Mont. Petroleum Tank Release Comp. Bd. v. Crumleys, Inc., 2008 MT 2, 341 M 33, 174 P3d 948 (2008), distinguished in High Country Paving, Inc. v. United Fire & Cas. Co., 2022 MT 72, 408 Mont. 202, 507 P.3d 1165, holding that a technical violation of the Property and Casualty Insurance Policy Language Simplification Act, 33-15-333 through 33-15-340, may not be used to invalidate unambiguous policy exclusions that would result in an increase of the risk assumed.

Application of Banking Standards, Not Livestock Industry Standards, to Loan Transaction Involving Cattle — Bank-Customer Relationship Not Giving Rise to Fiduciary Responsibilities: A bank loaned money to a couple to fund their cattle breeding operation. When the couple failed to make loan payments, the bank brought an action to collect and foreclose, and the couple brought a counterclaim that the bank's actions breached the covenant of good faith and fair dealing and the bank's fiduciary duty toward the couple. After the couple paid the amount owing, they became the plaintiffs and the case proceeded on the breach of covenant and fiduciary duty claim. The District Court granted the bank summary judgment on the claim, and on appeal, plaintiffs asserted that the court improperly applied banking standards to the case rather than livestock industry standards, constituting a breach of good faith. The Supreme Court disagreed. In Montana, the relationship between a bank and its customer is generally described as that of debtor and creditor and does not give rise to fiduciary duties except when special circumstances place a bank into the role of adviser. In this case, the bank acted as a creditor and not an adviser, and did not force the cattle sale but simply sought to enforce the repayment provisions of its contract with plaintiffs, so no special circumstances existed. The bank acted in accordance with the contract provisions and comported with prudent banking policy and reasonable commercial standards. It was appropriate for the District Court to apply commercial banking standards to the analysis of the bank's relationship with plaintiffs and plaintiffs' ability to service their loans. Summary judgment for the bank was proper. McCoy v. First Citizens Bank, 2006 MT 307, 335 M 1, 148 P3d 677 (2006).

Buy-Sell Agreement Not Subject to Financing Contingency Absent Specific Contractual Funding Language: A buy-sell agreement stated that the buyer had sufficient funds to close the sale of a ranch and was not relying upon any contingent source of funds unless otherwise stated in the agreement, but there was no third-party financing specified in the agreement. Nevertheless, when the buyer was not able to close the sale for lack of funds, both parties sought to recover the earnest money, and the buyer asserted that the contract language was clear and unambiguous in conditioning the sale on financing. The District Court disagreed, and on appeal, the Supreme Court concurred. The buyer represented that it had sufficient funds, and nowhere in the agreement or in an addendum extending the closing date was it specified that completing financing meant that the buyer had to obtain a loan from a third party. The District Court's award of the earnest money to the seller was affirmed. Sec. Abstract & Title Co. v. Smith Livestock, Inc., 2006 MT 265, 334 M 172, 146 P3d 732 (2006).

Failure of Insurer to Pay Within Sixty-Day Period Specified in Insurance Contract — No Error in Interpretation of Contract: An insurance contract required the insurer to pay for a loss within 60 days after the insurer received proof of loss and: (1) the parties reached an agreement; (2) there was a final judgment; or (3) the insured filed an appraisal with the insurer. The insured sought money damages because the claim was not paid within the 60-day period following the joint appraisal, which resulted in plaintiffs' alleged mental anguish and emotional distress. However, given a lengthy dispute over the amount of damages, the significant disparity between estimates, and plaintiffs' rejection of the joint appraisal, the District Court found that the agreement contemplated by the contract that would trigger the 60-day payment period was never reached. Plaintiffs appealed on grounds that the District Court misinterpreted the contract. The Supreme Court affirmed. The rejected joint appraisal did not constitute an agreement. Because the contractual requirements for the 60-day payment period were not met, the District Court did not err when it declined to conclude that the insurer should have made payment within 60 days of the joint appraisal. Nelson v. Farmers Union Mut. Ins. Co., 2003 MT 101, 315 M 268, 68 P3d 689 (2003).

Allowance for Suspension Without Pay Contained in Policies Covered by Employment Manual — Suspension Proper: A doctor was suspended without pay by a health care facility for failing to sign outstanding warrants. The doctor contended that the suspension was improper because the employment contract allowed for suspension without pay only under specific circumstances, none of which were present in this case. However, the employment contract also contained a provision requiring the doctor to follow the facility policies and procedures, and that reference clearly incorporated the facility's employment manual into the employment contract. The employment contract was not inconsistent with the employment manual, nor was the disciplinary procedure used by the facility to suspend the doctor inconsistent with the employment contract. Thus, the District Court correctly held that the doctor was properly suspended without pay and that the suspension did not violate the employment contract. The doctor's claim for wages during the suspension also failed absent evidence of the hours worked and the ability to calculate the value of those hours. Marias Healthcare Serv., Inc. v. Turenne, 2001 MT 127, 305 M 419, 28 P3d 491 (2001).

Contested Ownership of Independent Business — Standard of Review of Judgment on Pleadings: Hedges claimed ownership of an independent Melaleuca business, allegedly acquired through a written transfer of the business by Johnson, the former owner, before Johnson's death. As corepresentatives of Johnson's estate, the Woodhouses claimed ownership of the same business by virtue of a residuary devise in Johnson's will. The uncontroverted facts in the pleadings served as the factual basis for the parties' competing motions for judgment on the pleadings. A movant for judgment on the pleadings must establish that no material fact exists and that movant is entitled to judgment as a matter of law, and pleadings are to be construed in the light most favorable to the nonmoving party, whose allegations are taken as true. The conclusions of law standard of review is applied. The District Court properly looked to Johnson's Melaleuca contract, which required that Melaleuca accept signed and acknowledged forms in respect to transfer of a business during a business owner's lifetime and approve the transfer in writing. The contractual restrictions on assignment of a Melaleuca contract were not met by Johnson's written transfer of the business to Hedges, and the court correctly concluded that Johnson's assignment was not valid. Judgment on the pleadings for Woodhouses was affirmed. Hedges v. Woodhouse, 2000 MT 220, 301 M 180, 8 P3d 109, 57 St. Rep. 905 (2000).

Plain Language of Policies Providing Insurance on Rental Car Construed — Primary Versus Excess Coverage: Hudson used a credit card to rent a 1995 Ford Mustang convertible from P.C. Rental, Inc. (P.C.). Three days later, Hudson lost control of the car, resulting in damages rendering the vehicle a total loss. At the time of the accident, P.C. had a commercial lines policy through Empire Fire and Marine Insurance Company (Empire) that included liability and physical damage coverage. Hudson did not own a vehicle and was not covered under a personal policy, but auto rental insurance was provided by the company whose credit card Hudson used for the rental. Empire paid P.C. the agreed actual cash value of the vehicle, minus a $1,000 policy deductible, then sold the damaged vehicle for salvage and received an additional $1,108. The credit card company, Visa U.S.A. (Visa), also paid P.C. about $7,800 to cover P.C.'s deductible and lost rental fees. P.C. then brought a breach of contract action against Hudson for failing to return the vehicle in the same condition in which it was rented, as required by the rental agreement. Hudson alleged that Chase Manhattan Bank (Chase), as issuer of the credit card, was responsible for damages sustained to the rental car under the terms of the rental insurance. Hudson subsequently filed for bankruptcy and assigned all rights in the third-party action against Chase to P.C. P.C. then amended the complaint to include the credit card company as defendant, alleging that the rental insurance provided coverage on a 24-hour basis for damage to a car rented with the credit card up to the full value of the car. Visa denied P.C.'s allegations regarding the rental insurance, alleged that Visa had met its obligations under the policy by covering P.C.'s deductible and lost rental fees, and moved for summary judgment, which was granted. The District Court concluded that Hudson was an insured under the liability policy provided to P.C. by Empire and thus Empire was not entitled to subrogate against its own insured. The court determined that because both policies provided damage coverage for the same vehicle, it was necessary to look to the "other insurance" clauses of the policies. The Empire policy stated that its coverage was primary, while the Visa policy stated that its coverage was excess coverage, so Empire was not entitled to recover any of the amount that it paid to P.C. from Visa. On appeal, the Supreme Court affirmed. Given the nature of the coverage available, no determination of whether Hudson was an insured under Empire's physical damage coverage was necessary or possible under the policies. The District Court did not err when it concluded that, based on the clear language of the policies, P.C.'s physical damage coverage was primary and Visa's rental insurance was excess. P.C. Rental, Inc. v. Chase Manhattan Bank, 2000 MT 106, 299 M 315, 998 P2d 1168, 57 St. Rep. 430 (2000).

Tender of Payment of Attorney Fees Conditioned on Release of Files Upheld — Right of Patent Assignee to Files Upheld — Construction of Agreement as Assignment and Not License of Patent: Millhollin invented a device to align conveyor belts, which he called a "belt trapper". Millhollin also entered into an agreement with The Conveyor Company (TCC), in which Millhollin gave TCC the exclusive right to make, use, and sell the belt trapper in the United States and foreign countries and in which, in return, TCC agreed to pay Millhollin royalties and other amounts. After deciding that the fees charged by Conover, Millhollin's lawyer, for certain work in connection with the patents were too high, TCC tendered Conover the balance of his fees, conditioned upon Conover turning over his files in the matter to TCC. Millhollin then sent TCC a notice of its default on the contract. After no action was taken by TCC to cure the default, Millhollin declared the agreement terminated and filed a declaratory judgment action. The District Court held that TCC had the right to tender payment conditioned upon receipt of the files. Citing Advance-Rumely Thresher Co., Inc. v. Hess, 85 M 293, 279 P 236 (1929), and 28-1-1211, the Supreme Court held that a tender of payment may be conditional as long as the condition is one that the tenderer has a right to insist upon. The Supreme Court then analyzed the relationship between TCC and Millhollin as set forth in the written agreement between them and found that the agreement transferred by assignment all of Millhollin's rights in the belt trapper to TCC. Consequently, the Supreme Court held that the files in the hands of Conover were property belonging to TCC and that TCC could therefore withhold payment to Conover conditioned upon release of those files without breaching its agreement with Millhollin. Millhollin v. The Conveyor Co., 1998 MT 41, 287 M 377, 954 P2d 1163, 55 St. Rep. 136 (1998).

Application of Procuring Cause Doctrine to Exclusive Listing Agreements: The procuring cause doctrine, which permits a broker to show that the broker's part of the contract was performed and that the principal reaped a benefit from the efforts, is not confined to consideration of nonexclusive listing agreements. It applies in all situations unless the parties agree otherwise in the listing contract. Lane v. Smith, 255 M 218, 841 P2d 1143, 49 St. Rep. 974 (1992), clarifying Flinders v. Gilbert, 141 M 442, 378 P2d 385 (1963), and followed in Hall & Hall, Inc. v. Hyde, 264 M 190, 870 P2d 1362, 51 St. Rep. 257 (1994).

Unambiguous Contract — No Interpretation Needed: When the words of a contract are clear, certain, and unambiguous, the language alone controls and there is nothing for the courts to interpret or construe. In the construction of contracts, the courts may look not only to the language employed but also to the subject matter and the surrounding circumstances and may avail themselves of the same light that the parties possessed when the contract was made. The District Court did not err when it found that the term "concrete" included, specifically, precast concrete panels. Morning Star Enterprises, Inc. v. R.H. Grover, Inc., 247 M 105, 805 P2d 553, 48 St. Rep. 112 (1991), followed in Nyquist v. Nyquist, 255 M 149, 841 P2d 515, 49 St. Rep. 927 (1992).

No Express Warranties Found in Repair Contracts, Protective Covenants, and Preliminary Declaration: The plaintiffs, a condominium owners' association and its individual members, sued Big Sky of Montana Realty, Inc., the successor in interest of Big Sky of Montana, Inc., for breach of express warranties in failing to originally construct and later repair construction defects in fireplaces in the Deer Lodge Condominiums at Big Sky, Montana, in accordance with applicable fire and building codes. The plaintiffs based their claim of express warranty upon the repair contracts, claiming that the contracts called for the repairs to be done according to applicable plumbing, electrical, and building codes. Plaintiffs also based their claim of express warranty on protective covenants that require compliance with the same codes and on the preliminary declaration for the condominiums that required compliance with those codes. The plaintiffs contended that the declaration ran with the land because it had to be recorded. The District Court granted the defendants' motion for summary judgment, dismissing Big Sky of Montana Realty, Inc. The Supreme Court held that the District Court correctly found that no express warranties existed. Ass'n of Unit Owners of Deer Lodge Condominium v. Big Sky of Mont., Inc., 245 M 64, 798 P2d 1018, 47 St. Rep. 1814 (1990).

Termination of Contract Not Sole Remedy: The Supreme Court, relying on its holding in Glacier Campground v. Wild Rivers, Inc., 184 M 543, 597 P2d 689 (1978), ruled that the language of the contract between the parties was not ambiguous and did not limit the plaintiffs to termination as their only remedy for the defendants' breach of contract. Belue v. Gebhardt, 240 M 358, 784 P2d 396, 46 St. Rep. 2192 (1989). See also Kaufman Bros. v. Home Value Stores, Inc., 2012 MT 121, 365 Mont. 196, 279 P.3d 157, in which the Supreme Court reaffirmed the principle that under a conditional sales agreement, plaintiffs are entitled to invoke one of two inconsistent remedies: either to affirm the contract and sue for the balance of the purchase price or to terminate the contract, retain the money paid, and repossess the property, the election of one precluding the election of the other; the court concluded that the plaintiffs' breach of contract action was precluded under the election of remedies doctrine because the plaintiffs elected to terminate the contract.

Bank Claim to Property Alleged as Fixtures — Inferior to Owners' Property Rights: Mills took out a loan to acquire personal property to be used in a roller-skating facility, including a removable heating system, and paid off the loan about 18 months later. Mills later sold the roller-skating facility, including the heating system, to Davises. The transaction was financed through the Little Horn State Bank. The contract provided that in case Davises defaulted, possession of the real and personal property would return to Mills and Davises would retain no further interest. Davises defaulted and entered an agreement and release with the bank whereby the property was deeded to the bank in consideration of the bank satisfying the mortgage debt. Mills later offered to sell the heating system to the bank, but the bank refused and advised Mills that the bank claimed the property as fixtures pursuant to Davises' mortgage, whereupon Mills removed the heating system. However, because Mills were at all times the owners of the personal property, the bank obtained no more interest than that held by Davises. Therefore, the bank's claim to the heating system as fixtures was inferior and subject to the property rights of Mills. Little Horn St. Bank v. Mill, 233 M 372, 760 P2d 91, 45 St. Rep. 1563 (1988).

Performance Combined With Terms — Valid Contract: An agreement for development of a mineral interest did not include every item that might have been included with respect to operational aspects; however, the parties performed under the agreement for 3 years. The Supreme Court cited Wilkerson v. School District, 216 M 203, 700 P2d 617, 42 St. Rep. 745 (1985), in holding that a contract is not invalid simply because it does not contain all the provisions or conditions the parties might have incorporated into it. Therefore, performance under the agreement, combined with the actual terms provided, demonstrated the existence of a valid contract. Somont Oil Co., Inc. v. Nutter, 228 M 467, 743 P2d 1016, 44 St. Rep. 1685 (1987).

Tenant's Estate in Land — Tenant's Share in PIK Benefits: An oral lease granted two-thirds of crops grown to the tenant Popp. The land was later included in the federal payment in kind program (PIK), but in the absence of a written lease, the payments were made to landlords Frank and Gountanis rather than to Popp. The District Court awarded two-thirds of the PIK benefits to Popp. On appeal, Frank questioned whether a lease which required a percentage of crops to go to the tenant but which did not contemplate later federal benefits required the tenant to share in those benefits when the fruits of his labor did not create any entitlements under the federal program. The Supreme Court, in affirming the award, held that Popp had an estate interest in the land for the duration of his tenancy and that the award to Frank and Gountanis was in derogation of Popp's interest. Popp v. Gountanis, 221 M 267, 718 P2d 340, 43 St. Rep. 801 (1986).

Irrigation Contract — Interpretation of Limitations on Water Usage: Where the plaintiff irrigator brought an action against an irrigation company, claiming the company had violated its contract with the plaintiff by failing to provide him with sufficient water to irrigate his land, the District Court did not err in holding that it was the plaintiff who violated the contract since there was substantial evidence showing that the blockage of the irrigation ditch by the plaintiff resulted in the plaintiff's taking of more than the 400 miner's inches of water a year allowed by the contract. The District Court did err, however, in prohibiting the plaintiff from diverting water by pumping and from irrigating land not historically irrigated. There was no language in the contract restricting the method of irrigation or the number or location of acres to be irrigated. As long as the plaintiff used no more water than his contractual entitlement, the District Court could not limit the means or place of irrigation. Griffel v. Cove Ditch Co., 207 M 348, 675 P2d 90, 41 St. Rep. 1 (1984).

"Occupying" Defined — Motor Vehicle Insurance Coverage: Sayers rode in Galetti's vehicle to Storm's vehicle, which was stalled, with the intention of jump starting it. At the time of the accident, the Galetti vehicle and the Storm vehicle were facing each other and Sayers was between the two vehicles leaning under the hood of the Storm vehicle. An uninsured motorist struck the

rear of the Storm vehicle, propelling it forward into the Galetti vehicle and severely injuring Sayers. The Supreme Court held that Sayers was occupying Galetti's vehicle under Galetti's insurance policy's definition of occupying and that Sayers was entitled to stack the uninsured motorist limits of liability on the insurance policies covering automobiles not involved in the accident. Sayers and Galetti each had two vehicles covered by uninsured motorist provisions, and Storm had three vehicles covered by uninsured motorist provisions. Sayers v. Safeco, 192 M 336, 628 P2d 659, 38 St. Rep. 814 (1981), distinguished in Chilberg v. Rose, 273 M 414, 903 P2d 1377, 52 St. Rep. 1038 (1995), and followed in Estate of Richerson v. Cincinnati Ins. Co., 2011 MT 266, 362 Mont. 324, 264 P.3d 1087. Sayers was followed and Chilberg was distinguished in Farmers Alliance Mut. Ins. Co. v. Holeman, 1998 MT 155, 289 M 312, 961 P2d 114, 55 St. Rep. 601 (1998).

Jury Instruction on Procuring Cause — Real Estate Listing: Defendant contended it was error for the court to give instructions on procuring cause in a case involving payment of a real estate commission. The instructions given were contractual interpretation instructions taken almost verbatim from Montana statutes. A contract is to be construed so as to make it definite, operative, and reasonable; words are to be understood in their usual sense, and technical words are to be interpreted in the sense used in the business to which they relate. In this case, the court did just that. In addition, because the instructions set forth the actual law of Montana for the construction of contracts, they are part of the contract itself. Barrett v. Ballard, 191 M 39, 622 P2d 180, 37 St. Rep. 2038 (1980).

Chapter Law Review Articles

Right of Foreign Corporation to Sue Upon Contracts in Montana Courts—Doing Business—Failure to Qualify—Subsequent Qualification, Niklas, 26 Mont. L. Rev. 218 (1965).

Part 1
General Provisions

Part Case Notes

No Factual Issue of Waiver Under Contractual Consent to Assignment Clause — Summary Judgment Proper: The Nicholsons entered a contract option with J.G.L. Distributing (JGL) that gave JGL 5 years to purchase the Nicholsons' property. The option contained a consent to assignment clause that required JGL to obtain the Nicholsons' written consent before assignment to a third party. JGL subsequently assigned an interest in the property to plaintiff but did not notify the Nicholsons. Plaintiff spent money improving the property but missed a payment. The Nicholsons then notified JGL that the option expired and that they intended to sell the property to someone else. Plaintiff sued JGL and the Nicholsons, JGL counterclaimed against plaintiff and filed cross-claims against the Nicholsons, the Nicholsons counterclaimed against JGL, and all three parties moved for summary judgment. The District Court dismissed plaintiff's claim because plaintiff was not a party to the contract. The court also held that the consent to assignment clause was valid and enforceable, but that even though JGL breached the agreement by not notifying the Nicholsons of the assignment and by missing a payment, the breach was not material and did not serve to terminate JGL's right to exercise the option. The court then concluded that forfeiture would be too harsh a remedy, excused the forfeiture, and granted JGL 20 days to pay the Nicholsons the full purchase price. On appeal, the Supreme Court affirmed. Plaintiff failed to show a genuine issue of material fact that the Nicholsons waived their rights under the consent to assignment clause. The breach of contract by JGL was incidental rather than material, so the District Court's holding that forfeiture would be too harsh was not erroneous. Thus, the District Court correctly applied the antiforfeiture statute when it granted JGL equitable relief under 28-1-104 because JGL's breach was not grossly negligent, willful, or fraudulent. It was only when the Nicholsons discovered that they could sell the property at a greater profit that they acted to strictly enforce the timely payment provision of the contract, so application of the antiforfeiture statute was appropriate to avoid an unjust result. R.C. Hobbs Enterprises, LLC v. J.G.L. Distrib., Inc., 2004 MT 396, 325 M 277, 104 P3d 503 (2004). See also Erban v. Monforton, 227 M 531, 740 P2d 677 (1987), Norwood v. Serv. Distrib., Inc., 2000 MT 4, 297 M 473, 994 P2d 25 (2000), and VanDyke Constr. Co., Inc. v. Stillwater Min. Co., 2003 MT 279, 317 M 519, 78 P3d 844 (2003).

Justiciable Controversy Required:

The Supreme Court applied the rationale in Hardy v. Krutzfeldt, 206 M 521, 672 P2d 274 (1983), in holding that plaintiff's request for a declaratory judgment regarding the legality of closing school board meetings to the public amounted to a request for an advisory opinion that would have no impact on present or future rights of the parties. Because plaintiff did not seek to void the meetings, a justiciable controversy did not exist and a declaratory judgment action could not be maintained. Flesh v. Bd. of Trustees, 241 M 158, 786 P2d 4, 47 St. Rep. 161 (1990).

When a declaratory judgment had been sought on the issue of whether a right of first refusal of real property was invalid under the rule against perpetuities, it should have been dismissed by the District Court because no justiciable controversy existed. Relying on Hardy v. Krutzfeldt, 206 M 521, 672 P2d 274, 40 St. Rep. 1823 (1983), the Supreme Court noted that in this case there was no pending sale or offer for sale or purchase or offer to purchase the affected property. Neither had a third party challenged the clause's application to him. Parker v. Weed, 220 M 49, 713 P2d 535, 43 St. Rep. 162 (1986).

The parties were all heirs of Robert Hardy. He created trusts that became operative upon his death. The trusts were terminated, and the heirs entered negotiations for the division of a ranch making up the corpus of the trust. An agreement was entered dividing the ranch into seven tracts. The agreement provided that prior to the sale of any tract the other six heirs were to be given the right of first refusal. If all declined and a contract was entered into with a third party, all six had the right to meet the offer, with the first to accept to be given priority. The plaintiffs filed a complaint for declaratory relief seeking to have the provisions on first refusal declared an unreasonable restraint on alienation. The District Court granted summary judgment to defendants. On appeal, the Supreme Court remanded with instructions to dismiss. The court held that there was no justiciable controversy as no attempts had been made to sell any of the tracts. The court held that the Uniform Declaratory Judgments Act could not be used as a platform for the courts in Montana to plunge into indefinite, amorphous ponds of contract interpretation. Hardy v. Krutzfeldt, 206 M 521, 672 P2d 274, 40 St. Rep. 1823 (1983), relied on in Parker v. Weed, 220 M 49, 713 P2d 535, 43 St. Rep. 162 (1986).

Finding of Perpetual Contractual Obligation Invalid: A contract between the city of Billings and an adjoining county water district does not, as the District Court found, bind the parties to a perpetual obligation until the consent of both parties to terminate the contract is obtained. The Supreme Court found that the life of the contract is indefinite, not perpetual, and may be terminated by the Public Service Commission if the Commission finds such action necessary and within its jurisdiction over rates and service. Billings v. P.S.C., 193 M 358, 631 P2d 1295, 38 St. Rep. 1162 (1981).

28-3-101. Rules of interpretation to be uniform.

Case Notes

Influence of Parties' Course of Conduct: In extended litigation, the city of Billings and the police union differed on interpretation of a contract. Regarding a dispute on interpreting a contract provision, the District Court granted summary judgment to the city based on extrinsic evidence of intent and course of conduct. The Supreme Court affirmed that decision, explaining that course of conduct is entitled to controlling weight if there is ambiguity. Watters v. Billings, 2019 MT 255, 397 Mont. 428, 451 P.3d 60.

Error to Deny Jury Trial on Plaintiffs' Claims for Breach of Contract — Interpretation: Appellants, as developers, entered into subdivision improvement agreement with respondent city. The court held that it was error for trial court to deny appellants a jury trial on their claims for breach of contract based on allegations that the parties either failed to attach like meanings to the word "crossing" (to be installed over a city drain) or, alternatively, that the crossing to be constructed under SID is not comparable to the one contemplated by the parties at time of entering agreement. If, as here, contract term is ambiguous, intention of parties is left to jury. A claim of differing uses of the word "crossing" puts the existence, as well as meaning, of the present contract at issue for a jury determination. Gray v. Billings, 213 M 6, 689 P2d 268, 41 St. Rep. 1910 (1984).

Contract Remedies: In the absence of a contractual provision expressly limiting the remedies available, a party may pursue any remedy that law or equity affords, as well as the remedies specified in the contract. Glacier Campground v. Wild Rivers, Inc., 182 M 389, 184 M 543, 597 P2d 689 (1978).

Reservation of Oil and Gas Rights: Where a deed of land contained a clause following the description of the land which said "including one-half of all oil and gas rights owned by the parties", it must be considered that it was the intention of the parties to exclude from the deed the other one-half interest in the oil and gas and that such one-half remained with the grantor. Wyrick v. Hoefle, 136 M 172, 346 P2d 563 (1959).

28-3-102. What law and usage to govern interpretation.

Case Notes

Valid Choice-of-Law Provision Governing Entire Contract Properly Applied to Attorney Fee Provision: A contract between a borrower and a bank contained a choice-of-law provision stating that all disputes arising out of the contract would be resolved under Michigan law. The contract also provided that the borrower was required to reimburse the bank's costs and expenses but did not provide for the bank to reimburse the borrower's costs and expenses. The District Court found that the choice-of-law provision applied and that the bank breached the contract. The District Court performed a separate choice-of-law analysis and determined that Montana law applied to the attorney fee provision. It awarded attorney fees to the borrower, reasoning that the nonreciprocal attorney fee provision in the contract would be statutorily reciprocal under 28-3-704. On appeal, the Supreme Court reversed, holding that Michigan law governed all disputes regarding the contract, including disputes regarding attorney fees, and that under Michigan law there was no authority to award attorney fees to the borrower under the contract. Masters Group Int'l, Inc. v. Comerica Bank, 2021 MT 161, 404 Mont. 434, 491 P.3d 675.

Choice of Law — Nonbeneficiary Third Party Cannot Assert Defenses and Counterclaims Arising From Contract: The defendant set up Limegrove Corporation for tax purposes, and he informally ran the day-to-day operations. Limegrove's sole shareholder was a trust for the defendant's children. To secure a property loan for a Montana-based property to be held by Limegrove, the defendant signed a promissory note and a term loan agreement, both subject to New York law, and Limegrove and the plaintiff bank signed a trust indenture security agreement subject to Montana law. Because judicial foreclosures must occur where the property is located, the parties correctly agreed that the subsequent foreclosure action on the property was governed by Montana law, but the parties disagreed on which state governed the defendant's defenses and counterclaims. Because the defendant was not a party to the trust indenture, his defenses and counterclaims could not arise from it, and because New York law did not offend Montana public policy, the District Court did not err in concluding that New York law governed the defendant's defenses and counterclaims. HSBC Bank USA, N.A. v. Anderson, 2017 MT 257, 389 Mont. 106, 406 P.3d 416.

Ohio Law Governs Employment Contract Claim — Subject Matter Jurisdiction Not Necessarily Precluded — Reversed to Consider Application of Doctrine Forum Non Conveniens: The plaintiff was an Ohio resident who worked for the defendant, a company whose principal place of business was Montana. After he was terminated, the plaintiff filed a wrongful discharge suit against the defendant in Montana. The defendant filed a motion to dismiss for lack of subject matter jurisdiction, which the District Court granted. On appeal, the Supreme Court ruled that although the District Court correctly ruled that Ohio law governed the plaintiff's employment contract claim, it erred in concluding that it therefore lacked subject matter jurisdiction over the claim. The Supreme Court also concluded that, based on the record, it could not determine whether an alternative forum was available for the plaintiff's claim, and it therefore vacated the District Court's dismissal and remanded for consideration of whether dismissal under the doctrine of forum non conveniens was appropriate. Harrington v. Energy West, Inc., 2015 MT 233, 380 Mont. 298, 356 P.3d 441.

No Choice-of-Law Provision in Insurance Contract — Place of Performance "Anywhere in the World" — Montana Law Applied: The parties entered into an insurance contract that did not contain a choice-of-law provision. Instead, the contract provided that the place of performance of the contract was "anywhere in the world". After the plaintiffs filed a lawsuit in Montana, the defendants argued that Washington law applied. The plaintiffs argued that Montana law applied, and the trial court agreed. The District Court concluded that because the suit was filed in Montana by Montana workers, and given the language in the contract, Montana was an anticipated place of performance, and on appeal the Supreme Court affirmed. Tidyman's Management Serv. v. Davis, 2014 MT 201, 376 Mont. 72, 330 P.3d 1135.

Insurance Contract Choice of Law Provision — Montana Law Incorrectly Applied to Nevada Policy: The District Court conducted a conflict of law analysis and concluded that Montana law governed Tenas's entitlement to damages for an accident that occurred in Montana under a personal auto policy that Tenas's mother obtained in Nevada. On appeal, the Supreme Court reversed. Nevada was determined to have a materially greater interest than Montana based on the fact that: (1) Nevada was the place of contracting; (2) although Montana represented a place of performance under the policy, place of performance weighed heavily toward Nevada because Tenas and her mother were mere visitors to Montana; (3) Tenas and her mother resided in Nevada, so that state had a greater interest regarding domicile, residence, nationality, place of incorporation, and place of business of the parties; and (4) a policy choice of law provision required application of Nevada law to resolve any disputes. Given Nevada's greater interest, the District Court improperly applied Montana law to the dispute. Tenas v. Progressive Preferred Ins. Co., 2008 MT 393, 347 M 133, 197 P3d 990 (2008). See also Casarotto v. Lombardi, 268 M 369, 886 P2d 931, 51 St. Rep. 1350 (1994), Mitchell v. St. Farm Ins. Co., 2003 MT 102, 315 M 281, 68 P3d 703 (2003), Wamsley v. Nodak Mut. Ins. Co., 2008 MT 56, 341 M 467, 178 P3d 102 (2008), Modroo v. Nationwide Mut. Fire Ins. Co., 2008 MT 275, 345 M 262, 191 P3d 389 (2008), and Newman v. Scottsdale Ins. Co., 2013 MT 125, 370 Mont. 133, 301 P.3d 348.

Forum Selection Clause Valid by Operation of Choice of Law Clause: In a contract containing a paragraph that contained both a choice of law clause for Washington state and a forum selection clause that included Spokane, Washington, the Supreme Court determined that the choice of law clause was valid under the factors set out in Modroo v. Nationwide Mutual Fire Insurance Company, 2008 MT 275, 345 M 262, 191 P3d 389 (2008), and since Washington law recognizes forum selection clauses and Appleway chose Spokane as the venue, Montana venue is improper. Polzin v. Appleway Equipment Leasing Inc., 2008 MT 300, 345 M 508, 191 P3d 476 (2008), followed in San Diego Gas & Electric Co. v. Ninth Judicial District Court, 2014 MT 191, 375 Mont. 517, 329 P.3d 1264.

Challenge to Contract or to Arbitration Clause — When Arbitration Appropriate: Plaintiffs defaulted on a loan with defendant, and nonjudicial foreclosure proceedings were begun. The loan contract contained an arbitration clause, but plaintiffs challenged the validity of the contract as a whole, not the validity of the arbitration clause. On defendant's motion, the District Court ordered arbitration, and plaintiffs appealed. The Supreme Court held that under federal law, when a complaint specifically challenges a contract arbitration clause, the doctrine of severability set out in Prima Paint Corp. v. Flood & Conklin Mfg. Co., 388 US 395 (1967), in conjunction with the Federal Arbitration Act, allows a court to hear the challenge. However, when, as here, a complaint challenges a contract as a whole, Prima Paint and Buckeye Check Cashing, Inc. v. Cardegna, 546 US 440 (2006), require a court to grant a motion to compel arbitration if the contract contains an arbitration provision. Thus, despite plaintiffs' contention that the contract itself was void ab initio, the District Court was affirmed. Martz v. Beneficial Mont., Inc., 2006 MT 94, 332 M 93, 135 P3d 790 (2006). However, see Thompson v. Lithia Chrysler Jeep Dodge of Great Falls, 2008 MT 175, 343 M 392, 185 P3d 332 (2008), in which a narrow exception to the Martz rule established that when a party challenges a contract containing an arbitration clause on the ground that the parties never entered a contract, the court, not arbitration, is the appropriate forum to decide whether a contract existed, prior to compelling arbitration.

Contract Interpretation Applicable to Restrictive Covenants — How Ambiguity Resolved — Restrictive Covenants Strictly Construed: General rules of contract interpretation apply to restrictive covenants, and any person having an interest under a restrictive covenant may seek declaratory relief concerning any question of construction arising under the covenant. When a restrictive covenant has been reduced to writing, the intent of the parties is to be ascertained, when possible, from the writing alone, and when the language of a covenant is clear, a court must apply the language as written. Restrictive covenants are strictly construed, and ambiguities in covenants are resolved to allow free use of property. The determination of whether an ambiguity exists in a restrictive covenant is a question of law for a court to decide, but mere disagreement between the parties as to interpretation of a restrictive covenant does not automatically create an ambiguity. Creveling v. Ingold, 2006 MT 57, 331 M 322, 132 P3d 531 (2006). See also Newman v. Wittmer, 277 M 1, 917 P2d 926 (1996), and Toavs v. Sayre, 281 M 243, 934 P2d 165 (1997).

No Contractual Definition of Cause — Discretionary Termination of Professional Sports Team Coach Related to Legitimate Business Needs Warranted: Cole was fired as a professional hockey coach because of the team's poor performance. Cole's 5-year employment agreement contained a clause, drafted by Cole, providing that if Cole was terminated without cause, he would receive 1 year's salary and a bonus. Although the contract did not contain a definition of cause, the District Court found that the termination was without cause. The Supreme Court disagreed. Applying de novo review of the District Court's summary judgment to interpret the employment contract terms in their ordinary and popular sense and construing any uncertainty in the contract language against Cole, who drafted it, the Supreme Court held that discharging the coach of a poorly performing professional sports team was a discretionary decision related to the legitimate needs of the business and constituted cause, so the employer had a legitimate business reason to terminate the coach. Thus, Cole was not entitled to recover under the contract. Cole v. Valley Ice Garden, LLC, 2005 MT 115, 327 M 99, 113 P3d 275 (2005).

Jurisdiction of Montana Courts Over Wrongful Discharge Case Involving Montana Citizen When Montana Law Applies — Dismissal for Lack of Jurisdiction Reversed: Plaintiff was a Montana resident hired by a Florida corporation, which was operated out of Oklahoma, to lay fiber optic cable throughout the country. While working in Indiana, plaintiff had a dispute with a supervisor and was fired. Plaintiff brought an action in Montana, claiming a violation of the Wrongful Discharge From Employment Act. The District Court held that under 39-2-912, the Montana courts lacked subject matter jurisdiction and dismissed the claim. On appeal, the Supreme Court reversed. Even though plaintiff never signed a written employment contract, the court held that a contract provision may be broad enough to indicate that an entire contract be governed by the laws of the state governing the particular provision. The fact that the defendant corporation paid income taxes, unemployment insurance premiums, and wages in Montana indicated an intent to be governed by Montana law. The court also concluded that under sections 187 and 188 of Restatement (Second) of Conflict of Laws (1971), the local law of the state with the most significant relationship to the transaction applies to questions of contract interpretation absent an effective choice of law by the parties. Plaintiff was considered a Montana resident despite the fact that employment required travel to other states, and the court concluded that it was appropriate to apply the Wrongful Discharge From Employment Act to the case even though the Act does not expressly provide for extraterritorial jurisdiction. Montana courts have subject matter jurisdiction in cases involving a Montana resident when Montana law applies, so plaintiff's case should not have been dismissed for lack of subject matter jurisdiction. Burchett v. MasTec N. America, Inc., 2004 MT 177, 322 M 93, 93 P3d 1247 (2004). See also Dailey v. Transitron Electronic Corp., 475 F2d 12 (5th Cir. 1973), and Harrington v. Energy West, Inc., 2015 MT 233, 380 Mont. 298, 356 P.3d 441.

Law of Place of Performance to Control Contract Legal Construction and Effect: Unless the terms of an insurance contract provide otherwise, the law of the place of performance generally controls a contract's legal construction and effect, and when an insurance contract designates the place of performance to be any state where a claim arises, performance occurs where the insured obtains judgment. It follows that the place of performance is also the place where an insured is entitled to receive benefits, has incurred accident-related expenses, or is entitled to judgment. The policies in question here contemplated that the insurer perform its contractual duty anywhere in the United States, even though the policies were purchased in California. The District Court held that California law applied, but the Supreme Court reversed. Montana was the place of performance pursuant to the policies because Mitchell, the plaintiff insured, was working and living in Montana at the time of the accident, the underinsured tortfeasor's vehicle was insured in Montana, Mitchell's medical expenses were incurred in Montana, Mitchell settled with the tortfeasor's insurers for the policy limit giving rise to an underinsured motorist claim in Montana, and judgment concerning the accident would be rendered and paid in Montana. Mitchell v. St. Farm Ins. Co., 2003 MT 102, 315 M 281, 68 P3d 703 (2003), followed in Wamsley v. Nodak Mut. Ins. Co., 2008 MT 56, 341 M 467, 178 P3d 102 (2008), and Tidyman's Management Serv. v. Davis, 2014 MT 201, 376 Mont. 72, 330 P.3d 1135. See also Restatement (Second) of Conflict of Laws 6 (1971), and Kemp v. Allstate Ins. Co., 183 M 526, 601 P2d 20 (1979).

Question of Fault and Question of Entitlement to Collect Damages Separate: Dill suffered damages after being hit as a pedestrian by a vehicle operated by Jardine. State Farm Mutual Automobile Insurance Company (State Farm) provided both liability insurance for Jardine and underinsured motorist coverage for Dill. Meeting all the conditions precedent in the policy, Dill recovered the maximum policy amount from Jardine pursuant to Jardine's policy, then, consistent with the general release executed on Dill's behalf in settling with Jardine, Dill demanded underinsured motorist benefits under Dill's policy, which State Farm refused to pay. The District Court held that Dill's claim against State Farm would not be ripe for adjudication until after Jardine's fault was established and damages assessed in a negligence action. However, the question of whether anyone was at fault and the question of whether an insured is legally entitled to collect damages from an underinsured driver are not the same. A person can be legally entitled to collect damages without first proving fault in court, as Dill did here; conversely, an insured might prove fault on the part of the defendant and yet not be entitled to collect damages. Once an insured demonstrates a legal entitlement to damages, principles of contract law define the coverage afforded by an underinsured motorist policy; tort law is relevant only as far as fault is concerned. Under a writ of supervisory control, the Supreme Court looked to the clear language of the policy and found no issues of fault for a factfinder to resolve. The only questions remaining were whether Dill was legally entitled to collect damages and, if so, in what amount. Regardless of whether anyone was at fault, having already received money from State Farm, Dill was obviously legally entitled to receive damages. Thus, the case was reversed for a trial to determine the amount of damages, if any, that Dill was entitled to under the underinsured motorist policy. Dill v. District Court, 1999 MT 85, 294 M 134, 979 P2d 188, 56 St. Rep. 350 (1999).

Choice of Applicable State Law — Application of Motor Vehicle Insurance Policy Stating Oregon Subrogation Law: Generally, the law of the place where an insurance contract was made governs questions of execution and validity of the contract, while the law of the place of performance controls the legal construction and effect of the contract. In a motor vehicle insurance contract made in Oregon and performed in Montana, a choice of law provision that required application of Oregon subrogation law violated Montana public policy and was unenforceable. Youngblood v. Am. St. Ins. Co., 262 M 391, 866 P2d 203, 50 St. Rep. 1601 (1993).

Motor Vehicle Insurance Policy Governed by Contract Law: The insurer argued that it was not liable to compensate the plaintiff for an injury suffered while in Canada because the plaintiff would not have been able to recover under Canadian tort law. The Supreme Court held that the liability of the insurer was governed by the terms of the contract and those terms were to be construed pursuant to the contract laws of the place in which the contract had been entered. St. Farm Mut. Auto. Ins. Co. v. Estate of Braun, 243 M 125, 793 P2d 253, 47 St. Rep. 1043 (1990), followed in Dill v. District Court, 1999 MT 85, 294 M 134, 979 P2d 188, 56 St. Rep. 350 (1999).

Coverage Denied When Property Destroyed by Arson: The plaintiff left part of her property in her ex-husband's home after their divorce because she had no place to store it. The home and contents had been insured prior to the divorce, and both spouses had been named as insureds on the policy. The ex-husband set fire to the dwelling and committed suicide. The plaintiff filed a claim with the insurance company for her property that was destroyed in the fire. The Supreme Court reversed the lower court and ruled that even though the plaintiff was an innocent coinsured, the contract expressly stated that no losses caused by the intentional act of any insured were covered. Woodhouse v. Farmers Union Mut. Ins. Co., 241 M 69, 785 P2d 192, 47 St. Rep. 89 (1990), followed in Tyler v. Fireman's Fund Ins. Co., 255 M 174, 841 P2d 538, 49 St. Rep. 958 (1992).

Conflict of Law — Express Contractual Provision Controls: Plaintiff was injured due to a faulty handrail in a missile silo on which he was working. Defendant sought indemnification from the construction company pursuant to a contract between the parties. The contract was executed in Washington and was to be performed in Montana. Under 28-3-102, the contract would be interpreted according to Montana law. However, the contract contained a provision whereby the parties agreed the terms of the contract would be governed by Washington law. When the language of a contract is clear and unambiguous, it is the court's duty to enforce the contract as made by the parties. Therefore, Washington law controlled the issue. Steinke v. The Boeing Co., 525 F. Supp. 234, 38 St. Rep. 1966 (D.C. Mont. 1981).

California Release of Tortfeasor — Montana Law Applicable: The release of a tortfeasor involved in a Montana accident signed in California by a New York resident, is subject to Montana law since the right to sue for the tort accrued in Montana and the release did not specify which law applies. Kussler v. Burlington N., Inc., 186 M 82, 606 P2d 520 (1980).

Conflicts — Place of Performance of Insurance Contract: This section is not a declaration of the rule of lex loci contractus, the law of the place where the contract was made. Rather, it is a declaration that generally a contract is to be interpreted under the rule of lex loci solutionis, the law of the place of performance. Under this statute, it is only when the contract does not indicate a place of performance that the interpretation would fall under the rule of lex loci contractus. Montana was found to be the place of performance of an insurance contract that provided for payment to a person legally entitled to recover because the judgment providing for recovery was obtained in Montana. Montana law was, therefore, applied. Kemp v. Allstate Ins. Co., 183 M 526, 601 P2d 20 (1979).

Assignment: The validity of an assignment must be determined by the law of the place of assignment. Capital Fin. Corp. v. Metropolitan Life Ins. Co., 75 M 460, 243 P 1061 (1926).

Life Insurance Contract: A contract of life insurance made in this state between one of its residents and a foreign company is governed by the laws of this state. Capital Fin. Corp. v. Metropolitan Life Ins. Co., 75 M 460, 243 P 1061 (1926).

Farm Lease: The lease was not void for failing to designate the time and place for a division of the crops provided for, since under this section any uncertainty in that respect was determinable by the custom or usage observed in the vicinity in the light of the surrounding facts and circumstances bearing upon the transaction. McDonald v. McNinch, 63 M 308, 206 P 1096 (1922).

Sale of Sheep: A telegram, "Wire lowest price you will sell the 7,000 S. & W. yearling ewes", and an answering telegram, "Lowest price on S. & W. yearling ewes eleven fifty this subject to immediate acceptance", together with custom and usage and this section and 28-3-201 and 28-3-402, evidenced a complete contract for the sale of the sheep, where defendant's offer was accepted within 24 hours, as against an objection that there was no meeting of the minds of the parties upon the price to be paid for the sheep, in that price could only be determined upon delivery and that the offer was not accepted immediately. Story v. Stanfield, 275 F 401 (1921).

Law Review Articles

Contract Theories Applied to War Bonds, Milne, 4 Mont. L. Rev. 70 (1943).

Conflict of Laws: Does R.C.M. 1935, § 7537, Require the Conclusion That the "Place of Performance" Governs the Essential Validity of a Contract?, Williams, 2 Mont. L. Rev. 74 (1941).

Part 2
General Rules of Interpretation

Part Case Notes

Complaint Failed to Allege Bodily Injury — Self-Serving Affidavits in Response to Motion for Summary Judgment Insufficient Evidence of Physical Manifestations of Injury to Trigger Coverage Under Bodily Injury Clause. Farmers Ins. Exch. v. Minemyer, 2023 MT 138, 413 Mont. 60, 532 P.3d 837.

No Duty to Defend Under Property Damage Clause — "Property Damage" Defined as Loss of Use of Tangible Property Not Physically Injured — Allegation of Economic Loss Does Not Constitute Loss of Use. Farmers Ins. Exch. v. Minemyer, 2023 MT 138, 413 Mont. 60, 532 P.3d 837.

Damage From Rain Event Discovered Months Later Sudden and Accidental: The roof of an RV sustained a large tear, likely from an overhanging tree branch, that went unnoticed by the owners. Soon after, the RV was parked uncovered in a storm during which a large amount of rain fell in a short period of time. Water entered the RV through the tear, seeped through cavities in the wall panel, and eventually became evident to the owners months later. The defendant insurance company covered the roof repair but declined to cover the repair of the wall panel. The owners filed suit to recover for the wall panel repair and associated expenses, and the parties filed cross-motions for summary judgment. The District Court ruled in favor of the defendant insurance company, finding that because the damage from the water entering the wall cavity did not become evident for months after the storm, it was not "sudden" as required for coverage under the policy. On appeal, the Supreme Court disagreed, finding that the wall panel would have needed to be removed for repairs as soon as the water entered, and the value of the RV was diminished as soon as the water became trapped. The Supreme Court reversed the grant of summary judgment and remanded the case. Kaul v. State Farm Mut. Auto. Ins. Co., 2021 MT 67, 403 Mont. 387, 482 P.3d 1196.

Failure to Notify of Claim Pursuant to Plain Language of Insurance Policy — No Coverage — Summary Judgment Proper: The plaintiffs sued a construction company for faulty construction of their home and were awarded a default judgment in the amount of nearly $2 million after the construction company failed to appear. The plaintiffs then secured a judgment and requested payment from the construction company's insurance company. The insurance company denied coverage on the basis that its insured never provided notice of the claim as required by the insurance policy and that the insured's failure to provide notice resulted in prejudice to the insurance company. The District Court agreed and granted the insurance company's motion for summary judgment. On appeal, the Supreme Court affirmed the grant of summary judgment, given that the notice requirements in the insurance policy were simple and clear and that by not receiving notice, the insurance company had been deprived of the ability to adequately investigate and litigate the claim against its insured. Steadele v. Colony Ins. Co., 2011 MT 208, 361 Mont. 459, 260 P.3d 145. See also Estate of Gleason v. Cent. United Life Ins. Co., 2015 MT 140, 379 Mont. 219, 350 P.3d 349, expressly adopting the notice-prejudice rule in the first party insurance coverage context. However, see Atlantic Casualty Ins. Co. v. Greytak, 2015 MT 149, 379 Mont. 332, 350 P.3d 63.

Objective Determination of Whether Ambiguity Exists in Contract — Ambiguity Not Created by Disagreement Over Interpretation of Contract Language: The determination whether an ambiguity exists in a contract is made on an objective basis. A conclusion of ambiguity is not compelled by the fact that parties to a document, or their attorneys, have or suggest opposing interpretations of a contract or even disagree as to whether the contract is reasonably open to just one interpretation, nor does ambiguity exist just because a claimant says so. Rather, an ambiguity exists only if the language is susceptible to at least two reasonable but conflicting meanings. In the present case, plaintiffs' backup position was that language in a right-of-way contract was ambiguous, but the three circumstances proffered by plaintiffs, even when considered collectively, did not demonstrate that the contract language was susceptible to at least two reasonable but conflicting meanings. Thus, the trial court did not err in concluding that the language was unambiguous, which was in fact plaintiffs' primary position. Mary J. Baker Revocable Trust v. Cenex Harvest St., Cooperatives, Inc., 2007 MT 159, 338 M 41, 164 P3d 851 (2007), followed in Wills Cattle Co. v. Shaw, 2007 MT 191, 338 M 351, 167 P3d 397 (2007).

Ambiguity Regarding Whether Settlement Contingent on Alternate Financing — Summary Judgment Improper: Plaintiff sought to foreclose on a loan made to defendant, alleging that defendant's liabilities exceeded the value of the collateral, resulting in default pursuant to the terms of the note. The parties made several attempts to settle the issue, resulting in defendant's payoff to plaintiff, but in an amount that the plaintiff claimed was insufficient. The District Court granted summary judgment to plaintiff and ordered enforcement of the settlement agreement. However, a letter memorializing the settlement agreement, when considered with the parties' other correspondence, created an ambiguity regarding whether the settlement was contingent on alternate financing. Because there was more than one reasonable interpretation regarding the parties' intention, the parties' affidavits and testimony were admissible to determine intention and raised an issue of fact that precluded summary judgment. The case was remanded for further proceedings. Stockman Bank v. Potts, 2002 MT 178, 311 M 12, 52 P3d 920 (2002).

Material Misrepresentation on Application for Credit Life and Disability Insurance — Denial of Coverage Warranted: Schlemmer applied to the North Central Life Insurance Company (North Central) for credit life and disability insurance but misrepresented his health history. If he had answered correctly on the application, he would have been ineligible for the insurance. Nevertheless, he averred by his signature that he understood the form and that his application statements were true, so the policy was issued. Schlemmer later filed a claim for disability payments. North Central investigated, found that Schlemmer had been treated within the previous 2 years for hypertension, chronic obstructive lung disease, and disease or disorder of the kidneys, contrary to his statements in the application, and denied the claim and refunded Schlemmer's premiums. Schlemmer sued for damages, claiming that the application and underwriting procedures used by North Central violated 33-18-201, commonly known as the unfair claims settlement practices law, breached the covenant of good faith and fair dealing, and constituted fraud. Schlemmer also maintained that the District Court erred in failing to rule on whether North Central's agent had knowledge of Schlemmer's condition, which might have created a question of material fact. The Supreme Court affirmed the District Court's rulings that: (1) Schlemmer's claim of ignorance of the contents of the written application could not prevail because the application language was clear and unambiguous and Schlemmer did not deny signing it; (2) Schlemmer materially misrepresented his health on the application; (3) the material misrepresentation was legally sufficient to allow North Central to deny coverage under the policy; and (4) Schlemmer's argument that North Central's agent knew or should have known about Schlemmer's health was mere speculation insufficient to create an issue of fact to defeat North Central's properly supported motion for summary judgment. Further, the Supreme Court declined to consider Schlemmer's argument that the misrepresentation could not serve as a basis to rescind the policy because he did not apply for benefits until more than 2 years after applying for the insurance, pursuant to 33-22-205, because Schlemmer never raised the issue at the District Court level. Schlemmer v. N. Cent. Life Ins. Co., 2001 MT 256, 307 M 203, 37 P3d 63 (2001).

Property Description of "2 Acres, More or Less" Not Ambiguous: A property agreement provided that Tract 1 be "2 acres, more or less". Although the phrase "more or less" may not be particularly precise, it is a phrase commonly understood by its plain and ordinary meaning and is not subject to two interpretations. More or less means "approximately", regardless of whether one party would prefer "less", while the other party "more". The property agreement was clear, unambiguous, and enforceable. Schwend v. Schwend, 1999 MT 194, 295 M 384, 983 P2d 988, 56 St. Rep. 754 (1999).

Gradual Accumulation of Smoke and Soot — "Sudden and Accidental" Construed — Damage Not Covered Under Pollution Exception to All-Risk Homeowner's Policy: During a 4- or 5-week holiday season, the Sokoloskis burned scented candles in their home, which caused a discharge of smoke and soot, damaging their home and belongings. Their insurer denied coverage under a pollution exclusion because smoke and soot were defined as pollutants in the policy. The District Court held that coverage was barred under the exclusion and that the damages were not sudden and accidental. The Supreme Court affirmed on both issues. The very use of the words "sudden" and "accidental" reveals a clear intent to state two separate requirements, so that "sudden" means more than "unexpected". "Sudden", even if it includes the concept of unexpectedness, also encompasses a temporal element because unexpectedness is already expressed by the word "accidental". Having determined that the damage was not sudden, the Supreme Court did not address the additional requirement of being accidental. Under the clear language of the policy definitions and exclusion clause, coverage was properly barred and summary judgment proper. Sokoloski v. Am. W. Ins. Co., 1999 MT 93, 294 M 210, 980 P2d 1043, 56 St. Rep. 392 (1999), citing N. Ins. Co. of N.Y. v. Aardvark Assoc., Inc., 942 F2d 189 (3rd Cir. 1991), and followed in Travelers Cas. & Sur. Co. v. Ribi Immunochem Research, Inc., 2005 MT 50, 326 M 174, 108 P3d 469 (2005).

Enforceability of Clear and Unambiguous Contract Language: When the language of a contract is clear and unambiguous, the contract does not require application of the rules of construction and it is a court's duty to enforce the contract as made by the parties. Keller v. Dooling, 248 M 535, 813 P2d 437, 48 St. Rep. 554 (1991).

Injury to Tangible Property Required Before Economic Loss Covered — Plagiarism: After arriving at a settlement agreement based on a charge of plagiarism, an insured sought recovery from his insurance company under a business policy that provided that the company would "pay on behalf of the insured all sums which the insured shall become legally obligated to pay as damages because of bodily injury, property damage or personal injury caused by an occurrence to which the insurance applies". When the insurer refused to pay, the District Court properly granted summary judgment to the company because the charges of plagiarism did not allege direct physical injury to tangible property, but alleged only economic loss. The longstanding rule in Montana is that in order for economic losses to be covered by insurance, a direct physical injury to tangible property must occur. Graber v. St. Farm Fire & Cas. Co., 244 M 265, 797 P2d 214, 47 St. Rep. 1595 (1990).

Performance Combined With Terms — Valid Contract: An agreement for development of a mineral interest did not include every item that might have been included with respect to operational aspects; however, the parties performed under the agreement for 3 years. The Supreme Court cited Wilkerson v. School District, 216 M 203, 700 P2d 617, 42 St. Rep. 745 (1985), in holding that a contract is not invalid simply because it does not contain all the provisions or conditions the parties might have incorporated into it. Therefore, performance under the agreement, combined with the actual terms provided, demonstrated the existence of a valid contract. Somont Oil Co., Inc. v. Nutter, 228 M 467, 743 P2d 1016, 44 St. Rep. 1685 (1987).

Ambiguity of Contract Clause — Conclusion of Law: Contract ambiguities are questions of fact, and on appeal the Supreme Court would ordinarily limit their review to the "clearly erroneous" standard of review. The initial determination of whether or not an ambiguity exists is one of law. Thus, the determination by the District Court that a default clause is ambiguous is a conclusion of law freely reviewable. When on review the Supreme Court finds that the clause is not ambiguous, the court is free to rely on its own interpretation of the clause. SAS Partnership v. Schafer, 200 M 478, 653 P2d 834, 39 St. Rep. 1883 (1982).

28-3-201. Interpretation giving effect to contract favored.

Case Notes

Multiple Contract Interpretations Argued to Court But Only One Reasonable — No Ambiguity Present: The District Court denied the plaintiffs' motion for partial summary judgment on a contract interpretation issue. The plaintiffs argued that a supplemental benefits package purchased by the owner of a motorboat on her insurance policy had the effect of deleting an entire section of the insurance policy, including a watercraft exclusion that would have arguably resulted in coverage for a motorboat accident. The District Court noted that such an interpretation of the policy would also remove several categories of coverage listed in a subheading of the supposedly deleted section, leaving the insured with less coverage despite paying an additional premium for the supplemental endorsement. On appeal, the Supreme Court affirmed, concluding that because there was only one reasonable interpretation of the contract, no ambiguity existed that could be construed against the insurer. Young v. Hammer, Hewitt, Jacobs, & Floch, PLLC, 2021 MT 180, 405 Mont. 65, 491 P.3d 725.

Partnership Governed by Partnership Agreement — Jurisdiction: The plaintiff appealed the judgment of the District Court that invalidated her efforts to force out her twin brother from the family's limited liability partnership created to steward the family ranch and property in eastern Montana. The brother counterclaimed on the issue of attorney fees, alleging that the District Court did not have authority to grant the award. Noting that under 35-10-106, the partnership agreement controlled the rights and duties of the partners, the Supreme Court reversed in part, concluding that the District Court erred by holding that the brother's interest was not subject to the buy-out provision of the partnership agreement and, therefore, judicial dissolution was not necessary. The Supreme Court held that, under Rule 6, M.R.Civ.P. (Title 25, ch. 20), the District Court did not have jurisdiction to award attorney fees because the award was made more than 60 days after the motion for fees was filed. Thus the Supreme Court reversed the District Court's order awarding attorney fees and remanded for further proceedings. The court affirmed the remainder of the District Court's judgment. Ballou v. Walker, 2017 MT 197, 388 Mont. 283, 400 P.3d 234.

Insurance Company Indemnification Agreement Valid — Partial Summary Judgment on Pleadings Proper: The District Court did not err in granting partial summary judgment on the pleadings to a plaintiff insurance company. The District Court properly limited its decision on partial summary judgment to the issue of whether the indemnity agreements allowed the plaintiff to seek indemnity for appropriate expenses while reserving the issue of damages and the amount of damages for the trier of fact. Moreover, the indemnity agreements did not violate 28-2-701 and 28-2-702 because they did not provide the plaintiff with carte blanche indemnification and the defendant insured was not required to indemnify the plaintiff for any illegal actions. Ohio Farmers Ins. Co. v. Jem Contracting, Inc., 2016 MT 343, 386 Mont. 49, 386 P.3d 613.

Contradicting Clauses in Separate Contracts Construed Against Drafter — Employee Waiver — Health Insurance: The plaintiff health insurance company filed a breach of contract action against the defendant, an employer providing health insurance for its employees. The contracts between the parties required the defendant to cover 75% or more of its employees; however, a subsequent contract allowed the defendant's employees to waive coverage. The District Court granted summary judgment in favor of the defendant, finding that the two provisions in the contracts were ambiguous and the contract should be interpreted against the drafter. On appeal, the Supreme Court affirmed, holding that the contracts must be interpreted as part of the same transaction and that giving effect to both contract provisions is not reasonably practical, that the ambiguity is construed against the drafter, that the newer specific contract controlled over the older general contract, and that the waiver provision was meant to modify the minimum employee participation provision. Mont. Health Network, Inc. v. Great Falls Orthopedic Associates, 2015 MT 186, 379 Mont 513, 353 P.3d 483.

Agreement to "Participate in an Alternative Financing Method" — Void for Lack of Certainty: In anticipation of a subdivision development, property owners entered into a waiver whereby they agreed not to challenge the creation of a special improvement district (SID) for the purpose of making road and intersection improvements. The waiver provided that in the event the improvements were not financed through a SID, the property owners would "participate in an alternative financing method" to reimburse the plaintiff for the improvements. After unilaterally improving the road, the plaintiff sought reimbursement from the bank that had acquired the interest in the property governed by the waiver. The bank refused to pay and argued that the contract was void for lack of certainty. The District Court granted the bank's motion to dismiss and the Supreme Court affirmed, agreeing that there was no mutual consent regarding alternative financing of the improvements. Covenant Inv., Inc. v. First Sec. Bank, 2014 MT 14, 373 Mont. 353, 317 P.3d 197.

Covenants Intended to Remain in Effect Until Rejected by Property Owners — Failure of Sufficient Tract Owners to Vote to Amend Covenants: Subdivision property owners entered covenants that would automatically extend for "successive period" of 10 years. The covenants could also be amended by a two-thirds vote of the owners of the original tracts. Some of the owners contended that the covenant extension language was ambiguous because it was not clear if the covenants would be renewed only for a single 10-year period or for successive 10-year periods. The District Court held that the language was not ambiguous, but rather contained a typographical error, and that successive 10-year periods applied. Plaintiffs appealed, but the Supreme Court affirmed. Taken as a whole the covenant language intended that the covenants remain in effect until affirmatively rejected by the property owners. In this case, five of the eight original tract owners voted to amend the covenants, so without the required two-thirds vote, the covenants remained unamended. Brewer v. Hawkinson, 2009 MT 346, 353 M 154, 221 P3d 643 (2009). See also Creveling v. Ingold, 2006 MT 57, 331 M 322, 132 P3d 531 (2006).

Ambiguous Employment Contract — Question of Parties' Intent Properly Submitted to Jury: West's employment contract contained two different provisions regarding how West would be compensated in the event of termination of employment. The District Court construed the ambiguous clauses against the employer who drafted the contract and submitted the issue to the jury. On appeal by the employer, the Supreme Court examined the contract language and affirmed. The employment agreement was ambiguous on the issue of whether West would be paid trailing commissions or bonuses if West were terminated for cause, so the District Court did not err in ordering that the parties' intent on the issue be submitted to the jury. West v. The Club at Spanish Peaks, LLC, 2008 MT 183, 343 M 434, 186 P3d 1228 (2008), following Eschenbacher v. Anderson, 2001 MT 206, 306 M 321, 34 P3d 87 (2001).

Unambiguous Release of Claims Against Attorney for Malpractice — Parties Bound by Terms of Release: Rich was injured in two automobile accidents and retained attorney Ellingson to represent her in claims against her insurer. The first claim was dismissed when Ellingson failed to serve a timely summons on the insurer after filing the claim. Rich sued Ellingson for malpractice and received a settlement of $175,000 from Ellingson's malpractice insurer. As part of the settlement, Rich signed a release providing that Ellingson was released from any future malpractice claims arising from representation of Rich. Rich's second accident claim was subsequently dismissed when the statute of limitations had run, and Rich again sued Ellingson for malpractice. Ellingson contended that the suit was barred by the release. The District Court agreed and dismissed the claim, and Rich appealed. Considering the document as a whole, the Supreme Court held that the release clearly and unambiguously barred future claims arising from Ellingson's representation of Rich in the multiple actions against Rich's insurer. Rich's latent discontent with the release, without more, was an insufficient basis upon which to premise an alteration of the express, unambiguous agreement. The District Court was affirmed. Rich v. Ellingson, 2007 MT 346, 340 M 285, 174 P3d 491 (2007). See also Hanson v. Oljar, 231 M 272, 752 P2d 187 (1988).

Validity of Forum Selection Language in Employment Contract: A clause in an employment contract provided that in case of disputes, venue for enforcement of the contract would be in the state District Courts of Lewis and Clark County, Montana, or in the district of choice set by the independent contractor. A dispute arose, and plaintiff independent contractor sought to enforce the contract in Lewis and Clark County. Defendant moved to dismiss for lack of personal jurisdiction, and the motion was granted on grounds that the contract's forum clause did not give the court personal jurisdiction over defendant, a resident of Illinois. Plaintiff appealed, and the Supreme Court reversed. As held in May v. Figgins, 186 M 383, 607 P2d 1132 (1980), parties to a contract may agree in advance to submit to the jurisdiction of a given court, and as such, forum selection clauses are prima facie valid and should be enforced unless the resisting party shows that the agreement was not deliberately and understandably made and that the contractual language did not clearly, unequivocally, and unambiguously express a waiver of personal jurisdiction. In this case, the parties knowingly consented to personal jurisdiction in Montana and the forum selection clause was clear and unambiguous. The case was remanded for further proceedings in the Montana court. Milanovich v. Schnibben, 2007 MT 128, 337 M 334, 160 P3d 562 (2007).

Contract Interpretation Applicable to Restrictive Covenants — How Ambiguity Resolved — Restrictive Covenants Strictly Construed: General rules of contract interpretation apply to restrictive covenants, and any person having an interest under a restrictive covenant may seek declaratory relief concerning any question of construction arising under the covenant. When a restrictive covenant has been reduced to writing, the intent of the parties is to be ascertained, when possible, from the writing alone, and when the language of a covenant is clear, a court must apply the language as written. Restrictive covenants are strictly construed, and ambiguities in covenants are resolved to allow free use of property. The determination of whether an ambiguity exists in a restrictive covenant is a question of law for a court to decide, but mere disagreement between the parties as to interpretation of a restrictive covenant does not automatically create an ambiguity. Creveling v. Ingold, 2006 MT 57, 331 M 322, 132 P3d 531 (2006). See also Newman v. Wittmer, 277 M 1, 917 P2d 926 (1996), and Toavs v. Sayre, 281 M 243, 934 P2d 165 (1997).

Agreement to Agree to Future Lease Terms Unenforceable: Defendant agreed to lease plaintiff farmland on a cash per acre basis for 5 years with an option to extend the lease on terms to be determined later. Toward the end of the 5-year lease, defendant offered to sell the land to plaintiff, but plaintiff declined, so defendant sold the land to a third party, and plaintiff filed a complaint alleging breach of the lease agreement. Both parties moved for summary judgment, and the District Court concluded that because the lease extension language constituted an agreement to agree and was vague and unenforceable, defendant was entitled to summary judgment. On appeal, the Supreme Court affirmed. Because the parties failed to include complete and material terms for determining the duration and payments for another lease term in the negotiation clause, the clause was rendered unenforceable, and specific performance was unavailable to enforce an agreement to agree to material terms in the future. Additionally, damages were not clearly ascertainable and calculation of damages was also untenable under the lease extension, so plaintiff could not recover damages. GRB Farm v. Christman Ranch, Inc., 2005 MT 59, 326 M 236, 108 P3d 507 (2005), following Steen v. Rustad, 132 M 96, 313 P2d 1014 (1957), Riis v. Day, 188 M 253, 613 P2d 696, (1980), and Quirin v. Weinberg, 252 M 386, 830 P2d 537 (1992), and followed in Bitterroot Int'l Sys., Ltd. v. W. Star Trucks, Inc., 2007 MT 48, 336 M 145, 153 P3d 627 (2007).

Dispute Over Contract to Deliver Log Home — No Requirement That Seller Provide Name of Third Party Boom Truck Operator — Rescission Proper Remedy for Material Breach of Contract: Anderson agreed to purchase a log home from Eschenbacher. The home was designed to be constructed on Anderson's homesite. Eschenbacher drafted the purchase contract, which provided that Eschenbacher would act only as a manufacturer, not as a building contractor, and also required Anderson to coordinate and ensure availability of a boom truck to assemble the structure at the site. Anderson contacted a third party to supply a boom truck instead of using Eschenbacher's truck. Eschenbacher then refused to deliver the logs unless Anderson supplied the name of the other boom truck operator. Both parties sued for breach of contract. The District Court concluded that Anderson was under no duty to provide Eschenbacher with the name of the boom truck operator, and the Supreme Court agreed. The contract clearly placed the responsibility for acquiring a boom truck with Anderson, but did not require Eschenbacher to use it, because other language required Anderson to pay any expenses incurred by Eschenbacher for waiting once the logs were delivered, if, for instance, the boom truck that Anderson provided was inadequate. Construing the contract most strongly against the drafter, Eschenbacher, the court found that Eschenbacher could easily have inserted provisions in the contract regarding specifications of an adequate boom truck, but he did not. Eschenbacher materially breached the contract by refusing to deliver the logs until the boom truck dispute was settled. The contract did not specify a remedy; thus, the District Court did not err in granting Anderson rescission of the contract. Eschenbacher v. Anderson, 2001 MT 206, 306 M 321, 34 P3d 87 (2001).

Shareholders' Agreement Enforceable Independent of Stock Exchange — Different Intent Contained in Separate Agreements Separately Enforceable: Following his termination from employment with Bitterroot International Systems, Inc. (Bitterroot), Knutson sought to exercise his buyout rights under the shareholders' agreement. Bitterroot refused to pay, contending that an earlier merger transaction and the subsequent shareholders' agreement should be read together and citing Rumph v. Dale Edwards, Inc., 183 M 359, 600 P2d 163 (1979), for the proposition that when construing an agreement that is part of a larger transaction, the intention of the parties must be determined by examining the entirety of the larger transaction. However, Rumph was distinguishable here because all the agreements in question occurred at different times and did not reference or depend upon each other. Each agreement was clear and unambiguous. Under Gerdes v. Omaha Home for Boys, 89 NW 2d 849 (Nebr. 1958), a court may not avoid the language of a complete, unambiguous contract by consolidating it with another writing if the effect of doing so would be to avoid an essential part of the contract. The District Court properly concluded that the shareholders' agreement was enforceable independent of the stock exchange between the parties. Knutson v. Bitterroot Int'l Sys., Inc., 2000 MT 203, 300 M 511, 5 P3d 554, 57 St. Rep. 800 (2000), followed in O'Brien v. O'Brien, 2022 MT 246, 411 Mont. 101, 532 P.3d 831.

Contract Providing for Both Termination and Renegotiation — Plain Language to Determine Parties' Standing: Paragraph 7 of a contract provided that the contract terminated on June 30, 1996. Paragraph 10 provided for renegotiation of the contract upon 30 days' written notice from either party. The District Court found the provisions to be at odds with each other. The law favors giving effect to each provision of a contract, and courts must interpret contractual provisions so as to allow each provision to be effective. Courts are without authority to insert components in or erase components from unambiguous contract provisions. Upon review, the Supreme Court looked to the plain language in the contract and found that paragraph 10 did not render the contract vague or indefinite; rather, it provided for a continuing contractual relationship if, after notice, a successful renegotiation was accomplished. The District Court erred, and the case was reversed and remanded for further proceedings. Hennen v. Omega Enterprises, Inc., 264 M 505, 872 P2d 797, 51 St. Rep. 369 (1994), followed in Corwin v. Bd. of Pub. Educ., 272 M 14, 898 P2d 1227, 52 St. Rep. 589 (1995).

Interpretation of Repugnancies in Partnership Dissolution Agreement: Plaintiff claimed that one paragraph of a partnership dissolution agreement conveyed all of the first partner's 50% interest to the second partner, while a later paragraph reconveyed the 50% interest back to the first partner. This interpretation would have rendered both paragraphs meaningless and repugnant. To resolve any repugnancy and give effect to both paragraphs, the District Court properly interpreted the first paragraph as conveying a present interest and the later paragraph as an executory promise to convey a future interest. Bretz v. Ayers, 232 M 132, 756 P2d 1115, 45 St. Rep. 936 (1988).

Amount of Rent — Essential Lease Term Requiring Certainty: Appellants signed a lease with an option to renew the lease. Although the appellants properly gave notice of intent to exercise the option, the renewal provision failed for lack of certainty regarding the amount of the rent because a determination of the amount of the rent upon renewal was based on bids from third parties. In this case, there was no such bid and therefore no means of determining the amount of the rent. The renewal provision of the lease was void for lack of certainty regarding the essential term of rent. Riis v. Day, 188 M 253, 613 P2d 696, 37 St. Rep. 1093 (1980), followed in Nentwig v. United Indus., Inc., 256 M 134, 845 P2d 99, 49 St. Rep. 1172 (1992), and GRB Farm v. Christman Ranch, Inc., 2005 MT 59, 326 M 236, 108 P3d 507 (2005).

Right of First Refusal in Lease: Contract was interpreted as sustaining lessees' right of first refusal of purchase. Tribble v. Reely, 171 M 201, 557 P2d 813 (1976), distinguished in Wymo Land Co. v. Luggie, 1998 MT 50, 288 M 21, 955 P2d 171, 55 St. Rep. 208 (1998).

Reasonable Interpretation: Where the language of the contract is contradictory or ambiguous so that it is susceptible of two constructions, one of which is fair, customary, and such as prudent men would naturally execute, and the other makes the contract inequitable, unusual, or such as reasonable men would not be likely to enter into, the interpretation which makes a rational and probable agreement must be preferred. Davis v. Park Sec. Corp., 117 M 393, 159 P2d 323 (1945).

Operation and Effect:

A contract must receive such an interpretation as will make it lawful, operative, definite, reasonable, and capable of being carried into effect; it may be explained by reference to the circumstances under which it was made and the matter to which it relates, and however broad may be its terms, it extends only to those things concerning which it appears that the parties intended to contract, particular clauses being subordinate to its general intent. Custer v. Missoula Pub. Serv. Co., 91 M 136, 6 P2d 131 (1931).

Of two constructions of a contract one of which will render it valid and the other void, the former will be adopted if it can be done without violence to the ascertained intention of the parties. Linse v. Zastrow, 63 M 241, 207 P 119 (1922).

If of two constructions one will render the contract in question valid and the other void, the former should be adopted if it can be done without doing violence to the ascertained intention of the parties. Finley v. School District, 51 M 411, 153 P 1010 (1915).

Guaranty: To construe the guaranty as running to the bank only when in fact the bank did not have any interest in the note or account at the time the guaranty was executed would render the guaranty meaningless and such a construction will not be adopted unless it is compelled by its very terms themselves. Schauer v. Morgan, 67 M 455, 216 P 347 (1923).

Offer and Acceptance: A telegram, "Wire lowest price you will sell the 7,000 S. & W. yearling ewes", and an answering telegram, "Lowest price on S. & W. yearling ewes eleven fifty this subject to immediate acceptance", together with custom and usage and this section, 28-3-102, and 28-3-402, evidenced a complete contract for the sale of the sheep, where defendant's offer was accepted within 24 hours, as against an objection that there was no meeting of the minds of the parties upon the price to be paid for the sheep, in that price could only be determined upon delivery and that the offer was not accepted immediately. Story v. Stanfield, 275 F 401 (9th Cir. 1921).

When Courts Cannot Compel Performance: Where a contract leaves the matter of rates or prices uncertain it cannot be specifically enforced unless they can be made certain by means provided in the contract itself. Thus a contract between a city and a water company under the terms of which the city bound itself to either purchase the company's plant at the end of 20 years or renew the contract for 20 years longer, "upon such terms as are mutually agreed upon at that time" was not specifically enforceable, inasmuch as the courts cannot compel parties to agree or make an agreement for them. Livingston Waterworks v. Livingston, 53 M 1, 162 P 381 (1916).

Role of Court: The contract in question was susceptible to two interpretations, one which would render the contract valid and the other which would render it void. The interpretation upholding the validity of the contract would be adopted if it could be done without doing violence to the ascertained intention of the parties. Finley v. School District, 51 M 411, 153 P 1010 (1915).

28-3-202. Effect to be given to every part of contract.

Case Notes

District Court Incorrectly Determined Plain Language of Subdivision Covenant Unambiguous — Related Documents Constituting Instrument Not Reviewed — Negative Easement — Ambiguity Interpreted Against Drafter Not Dispositive — Disputed Facts Whether County Acted Arbitrarily or Capriciously — Doctrine of Impossibility or Impracticality Not Applicable — Attorney Fees Award Reversed. Lewis & Clark County v. Wirth, 2022 MT 105, 409 Mont. 1, 510 P.3d 1206.

Policy Provision Regarding Definition of Loss — Insurer's Claim of No Obligation to Indemnify Defendant Unsuccessful — Indemnification Not Precluded. Rolan v. New West Health Serv., 2022 MT 1, 407 Mont. 34, 504 P.3d 464.

Breach of Contract Claim — Contract Clear and Unambiguous — Judgment on Pleadings Proper: The parties entered into a contract for the defendants to purchase an airplane from the plaintiff. The contract provided that the defendants would conduct an inspection of the plane; however, they withdrew their offer without inspecting the plane. The plaintiff filed suit alleging breach of contract, and the District Court granted the plaintiff judgment on the pleadings. The defendants appealed, arguing that the language in the contract was ambiguous and that extrinsic evidence should be allowed. The Supreme Court affirmed the judgment on the pleadings, holding that the language in the contract was clear and unambiguous and that the District Court had been correct to exclude extrinsic evidence. Kalispell Aircraft Co., LLC v. Patterson, 2019 MT 142, 396 Mont. 182, 443 P.3d 1100.

Misrepresentation Based on Mistake — Coverage Not Excluded Under Policy: The plaintiff sued the defendant, the insurer of the homeowner from whom she purchased a home. After closing on the home, the plaintiff had found the basement of the home flooded and later learned the homeowner had not disclosed that the basement had previously flooded. The defendant denied coverage to the previous homeowner, claiming that the homeowner had intentionally misled the plaintiff and that intentional misrepresentations were not covered by either the homeowner's home policy or rental policy. The District Court agreed and granted the defendant summary judgment. On appeal, the Supreme Court agreed that the home policy expressly excluded coverage; however, it reversed and remanded the case to the District Court based on its conclusion that the renter's policy did provide coverage because the homeowner had stated that his misrepresentation to the plaintiff was based on mistake. Huckins v. United Serv. Auto Ass'n, 2017 MT 143, 387 Mont. 514, 396 P.3d 121.

Contradicting Clauses in Separate Contracts Construed Against Drafter — Employee Waiver — Health Insurance: The plaintiff health insurance company filed a breach of contract action against the defendant, an employer providing health insurance for its employees. The contracts between the parties required the defendant to cover 75% or more of its employees; however, a subsequent contract allowed the defendant's employees to waive coverage. The District Court granted summary judgment in favor of the defendant, finding that the two provisions in the contracts were ambiguous and the contract should be interpreted against the drafter. On appeal, the Supreme Court affirmed, holding that the contracts must be interpreted as part of the same transaction and that giving effect to both contract provisions is not reasonably practical, that the ambiguity is construed against the drafter, that the newer specific contract controlled over the older general contract, and that the waiver provision was meant to modify the minimum employee participation provision. Mont. Health Network, Inc. v. Great Falls Orthopedic Associates, 2015 MT 186, 379 Mont 513, 353 P.3d 483.

Genuine Issue of Material Fact Concerning Termination of Written Easement: A written instrument creating an easement provided that if the grantee ceased to use a road or "any segment thereof" for 5 years or longer, the easement would terminate. The successor in interest to the grantee used the easement several times over the years, but the successor in interest to the grantor locked a gate for approximately 10 years and blocked off 40 feet of the easement. The District Court granted summary judgment to the successor in interest to the grantee, but the Supreme Court found that the District Court erred by failing to give meaning to the phrase "any segment thereof" within the written instrument creating the easement, creating an issue of material fact as to whether the easement had terminated. Whary v. Plum Creek Timberlands, L.P., 2014 MT 71, 374 Mont. 266, 320 P.3d 973.

No Breach of Duty to Defend When Insured Fully Defended — Duplicative Counsel by Coinsurer Unnecessary: The parents of a woman who died in a car accident sought compensation from two different insurers of the driver's parents and his estate. The two insurers worked together to ensure that their insureds were defended, although only one of the insurers paid the costs of counsel. As a part of a consent judgment, the rights of the insureds were assigned to the decedent woman's parents. The parents then argued that the insurer who did not pay the costs of defending had breached its duty to defend and was estopped from denying coverage. The District Court agreed and granted the parents summary judgment. The District Court also ordered the insurer to pay the full amount of the consent judgment as well as attorney fees and costs. On appeal, the Supreme Court reversed, ruling that as long as the insureds were fully defended, the duty to defend did not require both insurers to provide separate counsel when their combined efforts would be duplicative. St. Farm Fire and Cas. Co. v. Schwan, 2013 MT 216, 371 Mont. 192, 308 P.3d 48.

Partnership Agreement — Definition of "Practice of Medicine" — Application to Psychologists: Former partners of a medical clinic sued the clinic, claiming they were entitled to full partnership interest payments under a partnership agreement. The agreement provided for a reduction of partnership interest payments if a former partner continued to engage in the "practice of medicine" within 3 years of disassociation. The plaintiffs, who were psychologists still working in the community, claimed the phrase "practice of medicine" was a technical term that did not include psychologists. The District Court disagreed and concluded that under contract law, the ordinary and plain meaning of the phrase should be followed and that the ordinary meaning of the phrase included the practice of psychology. The plaintiffs appealed to the Supreme Court, which affirmed the District Court's grant of summary judgment in favor of the clinic. Krajacich v. Great Falls Clinic, LLP, 2012 MT 82, 364 Mont. 455, 276 P.3d 922.

Covenants Intended to Remain in Effect Until Rejected by Property Owners — Failure of Sufficient Tract Owners to Vote to Amend Covenants: Subdivision property owners entered covenants that would automatically extend for "successive period" of 10 years. The covenants could also be amended by a two-thirds vote of the owners of the original tracts. Some of the owners contended that the covenant extension language was ambiguous because it was not clear if the covenants would be renewed only for a single 10-year period or for successive 10-year periods. The District Court held that the language was not ambiguous, but rather contained a typographical error, and that successive 10-year periods applied. Plaintiffs appealed, but the Supreme Court affirmed. Taken as a whole the covenant language intended that the covenants remain in effect until affirmatively rejected by the property owners. In this case, five of the eight original tract owners voted to amend the covenants, so without the required two-thirds vote, the covenants remained unamended. Brewer v. Hawkinson, 2009 MT 346, 353 M 154, 221 P3d 643 (2009). See also Creveling v. Ingold, 2006 MT 57, 331 M 322, 132 P3d 531 (2006).

Genuine Issue of Material Fact Whether Dam Operation Damaged Lakeshore Properties — Summary Judgment Improper — Class Action Vacated: Flathead Lake landowners brought a class action suit against defendant operators of Kerr Dam for operating outside the scope of their easements in a manner that continuously eroded and damaged plaintiffs' lakeshore properties. The District Court rejected plaintiffs' argument that the dam operator was not allowed to affect plaintiffs' properties above an elevation of 2,893 feet, concluding instead that defendants' easements covered entire parcels. The court concluded that erosion, including wave action erosion, was within the scope of the easements and held that any duty defendants had to not cause unreasonable damage to plaintiffs' properties applied only to damage unrelated to use of the easement. Therefore, summary judgment was granted to defendants, and plaintiffs appealed. The Supreme Court first agreed that the District Court's contour line theory was correct. The "2,893 feet" clause did not establish the vertical limit argued by plaintiffs because although the dam operators' right to flood, subirrigate, drain, or otherwise affect the shoreline was not unlimited, it was not restricted to a maximum elevation of 2,893 feet at each parcel, but rather extended to whatever part of each parcel was affected when the lake was held at 2,893 feet above mean sea level as measured at the dam. The court also agreed that the right to cause some erosion was necessary to the enjoyment of the right to perpetually flood, subirrigate, and drain and was thus included by implication in the easements. However, further factual development and trial were necessary to address the question of whether the erosion was reasonable, necessary, and within the scope of the easements, which could not be resolved by summary judgment. Additionally, the question of whether defendants breached their obligation to not cause unreasonable damage to the shoreline properties and to not unreasonably interfere with plaintiffs' enjoyment also required further factual development and possibly trial. Therefore, the order certifying the case as a class action was vacated and the case was remanded for further consideration. Mattson v. Mont. Power Co., 2009 MT 286, 352 M 212, 215 P3d 675 (2009).

On remand, the District Court decertified the class as to one defendant and denied the plaintiffs' motion for certification as to another defendant on the basis that the question of whether the erosion caused unreasonable damage to or unreasonably interfered with the plaintiffs' properties required an individual, property-by-property analysis that was improper for class certification. On appeal, the Supreme Court reversed, concluding that class certification to both defendants was proper because the reasonableness of the erosion presents a common question that is incapable of being resolved on a property-by-property basis since an aggregate of the benefits and burdens imposed on all of the shoreline properties must be considered together to determine reasonableness. Mattson v. Mont. Power Co., 2012 MT 318, 368 Mont. 1, 291 P.3d 1209.

Express Lease Provision Required for Survival of Overriding Royalty: An overriding royalty applies only to the lease out of which it was created. In the case of an oil or gas lease or sublease, if a party wishes an overriding royalty to survive the expiration of the lease or sublease, an express provision must be included in the lease or sublease to accomplish survival of the overriding royalty. Ritter v. Bill Barrett Corp., 2009 MT 210, 351 M 278, 210 P3d 688 (2009), following Edward v. Prince, 221 M 272, 719 P2d 422 (1986).

Lack of Express Utility Easements Not Condition Adversely Affecting Title: The buyer of condominium units refused to close on the sale because the sale agreement did not expressly state the existence of utility easements for each parcel. The District Court determined that the lack of express utility easements was not a condition that adversely affected title and held that the buyer breached the contract by refusing to close the sale. On appeal, the Supreme Court affirmed. The entire property was part of the sale, including all units and appurtenances. If the buyer wanted each unit to have a stated right to access the utility areas, the buyer could affirmatively grant that right to each unit after acquiring the property. Also, the buyer could have required the express establishment of the easements in a written addendum to the contract to be a condition precedent to closing, but the buyer did not do so. The buyer failed to establish that the absence of individual unit easements was an adverse condition of title that allowed the buyer to refuse to close the sale. Apple Park, L.L.C. v. Apple Park Condominiums, L.L.C., 2008 MT 284, 345 M 359, 192 P3d 232 (2008).

Ambiguity of Contract Raising Genuine Issues of Fact — Summary Judgment Improper: In a dispute over the sale of aircraft, the District Court considered summary judgment motions from both parties, granted summary judgment for plaintiff on claims of breach of contract and express warranty, and denied defendant's summary judgment counterclaim of breach of contract and express warranty. The Supreme Court examined the contract and found ambiguities regarding whether defendant accepted the aircraft "as is" at signing or maintained the right to inspect and reject the aircraft prior to closing, as well as the parties' extension of the closing date. The ambiguities raised genuine issues of material fact regarding breach of contract and express warranty that were not appropriate for summary judgment, and the Supreme Court reversed for trial on the issues. Corporate Air v. Edwards Jet Center, Mont., Inc., 2008 MT 283, 345 M 336, 190 P3d 1111 (2008).

Tort Claims Not Precluded by Contract Claims Arising From Same Event: In a dispute over the sale of aircraft, the District Court considered summary judgment motions from both parties and granted defendant summary judgment on plaintiff's tort claims on grounds that plaintiff had relied on a contract theory of relief and thus elected to be made whole under the contract. Plaintiff appealed on grounds that tort liability can exist with contract liability and that recovery on a contract theory does not necessarily preclude recovery on tort theories such as fraud. Defendant responded that summary dismissal of the tort claims was proper because plaintiff should not be allowed to make a double recovery and that because plaintiff's claims were commercial, tort damages are not available except in rare cases when a separate tort claim arises from the contractual relationship. Without ruling on the validity of the tort claims, the Supreme Court held that consideration of plaintiff's fraud-based claims was not precluded by the fact that plaintiff also made separate contract claims arising out of the same event. The tort claims were required to be considered individually and could not be dismissed under a blanket rationale that the tort claims and contract claims were mutually exclusive. The District Court's summary judgment was reversed, and the issue was remanded for further consideration. Corporate Air v. Edwards Jet Center, Mont., Inc., 2008 MT 283, 345 M 336, 190 P3d 1111 (2008).

Total Compensation in Condemnation to Include Value of Condemned Property and Severance Damages: The city of Whitefish condemned 7,234 square feet of plaintiff's property, but conveyed to plaintiff 10,175 square feet of city property contiguous to plaintiff's lot. The conveyance was intended as severance damages to offset the harm of condemnation. The parties entered an agreement that plaintiff would grant possession of the condemned property to the city and that the city would pay plaintiff $130,000 to convey the 10,175 square foot adjacent lot. The agreement also stated that the parties were unable to agree on the value of the condemned property, the severance damages to plaintiff's remaining property, and the value of the conveyed property.

Eventually plaintiff filed a complaint for inverse condemnation and breach of the agreement when the parties were unable to agree on the property values and severance damages. The District Court held that the only issue for the jury was to determine the amount that plaintiff was entitled to for compensation, and the jury was not asked to determine any severance damages owing to plaintiff. The court also disallowed any evidence of the $130,000 payment because that money was considered for severance damages only and could not be considered by the jury in determining plaintiff's compensation for the condemned property. The court further disallowed the city from presenting any evidence regarding the conveyed property because it had not yet been deeded to plaintiff, and absent unity of ownership, the conveyed property could not be considered when determining the fair market value of plaintiff's remaining property after the condemnation. Last, the court determined that plaintiff's "cost-to-cure" damages were noncompensable because plaintiff's access remained the same after condemnation. During trial, various experts presented differing values for the condemned property. The jury ultimately found for plaintiff and held that the city owed $161,000 for the condemned property. The District Court also awarded plaintiff $94,788.23 as litigation expenses. The city appealed, and plaintiff cross-appealed. The Supreme Court held that the District Court misinterpreted the agreement and improperly limited the issues presented to the jury. The court noted that total compensation in an eminent domain case involves both the value of the condemned property and severance damages, including depreciation suffered as a result of condemnation. In order for the jury to consider all circumstances surrounding the condemnation, a new trial was required, so the case was reversed and remanded. K&R Partnership v. Whitefish, 2008 MT 228, 344 M 336, 189 P3d 593 (2008).

Question Whether Condition Precedent Satisfied and Contract Formed — Remand: The parties negotiated for the purchase of a new vehicle, and the terms of the contract documents set the interest rate at 3.9%. The plain language of the contract was clear that there was no binding contract until the contract terms were accepted by a bank or finance company. A week after negotiations when the bank would not accept the 3.9% rate, the car dealer notified the buyers that they would have to sign new finance papers with a higher annual percentage rate of 4.9%, but the buyers refused. The buyers then sued the dealer, but the District Court compelled arbitration and stayed the proceedings. On appeal, the car dealer asserted that the contract language was not binding to the dealer unless financing was obtained and that the condition precedent applied only to the dealer and not the buyers. The Supreme Court disagreed. The totality of the contract language demonstrated that the condition precedent also applied to the buyers, even though that was not expressly stated. The total sales price and the corresponding finance charge agreed to by the buyers were based on financing at 3.9%, and a change in rate required renegotiation by both parties, so the condition precedent applied to both parties. Because there were questions of disputed fact whether the condition precedent was satisfied and a contract formed, the case was remanded to District Court for further factfinding and discovery. Thompson v. Lithia Chrysler Jeep Dodge of Great Falls, 2008 MT 175, 343 M 392, 185 P3d 332 (2008).

Ambiguity in Collective Bargaining Agreement — Duty to Bargain in Good Faith: The Bonner school district involuntarily transferred and reassigned several teachers, which affected the subjects taught and the teachers' areas of expertise. The Bonner Education Association responded by filing an unfair labor practices claim, alleging that the school district had violated 39-31-305 and 39-31-401 by refusing to bargain for the transfers and reassignments. The school district contended that a management rights provision in the collective bargaining agreement allowed the district to unilaterally transfer and reassign teachers because that right was not limited by explicit provisions elsewhere in the agreement. The Supreme Court disagreed, noting that the agreement contained two other clauses that provided conflicting provisions. An integration clause, or zipper clause, seemingly waived the Association's statutory right to bargain for teacher transfers and reassignments as terms and conditions of employment, while a professional advantages clause could be interpreted to protect teachers from involuntary transfers and reassignments. These conflicting clauses made the agreement ambiguous as a matter of law. However, 39-31-305 provides a statutory duty to bargain regarding any question arising under a collective bargaining agreement, and 39-31-401 provides that it is an unfair labor practice to refuse to bargain in good faith. Regarding the school district's argument concerning management rights, the court held that requiring collective bargaining has no effect on an employer's fundamental right to manage and operate and does not impose on management the duty to concede to union demands, but only obligates the employer to bargain in good faith, in conformity with the purpose of state employment law. In light of the ambiguity in the collective bargaining agreement in this case, the school district committed an unfair labor practice by refusing to bargain for teacher transfers and reassignments. Bonner School District No. 14 v. Bonner Educ. Ass'n, 2008 MT 9, 341 M 97, 176 P3d 262 (2008).

Unambiguous Release of Claims Against Attorney for Malpractice — Parties Bound by Terms of Release: Rich was injured in two automobile accidents and retained attorney Ellingson to represent her in claims against her insurer. The first claim was dismissed when Ellingson failed to serve a timely summons on the insurer after filing the claim. Rich sued Ellingson for malpractice and received a settlement of $175,000 from Ellingson's malpractice insurer. As part of the settlement, Rich signed a release providing that Ellingson was released from any future malpractice claims arising from representation of Rich. Rich's second accident claim was subsequently dismissed when the statute of limitations had run, and Rich again sued Ellingson for malpractice. Ellingson contended that the suit was barred by the release. The District Court agreed and dismissed the claim, and Rich appealed. Considering the document as a whole, the Supreme Court held that the release clearly and unambiguously barred future claims arising from Ellingson's representation of Rich in the multiple actions against Rich's insurer. Rich's latent discontent with the release, without more, was an insufficient basis upon which to premise an alteration of the express, unambiguous agreement. The District Court was affirmed. Rich v. Ellingson, 2007 MT 346, 340 M 285, 174 P3d 491 (2007). See also Hanson v. Oljar, 231 M 272, 752 P2d 187 (1988).

No Wrongful Discharge Claim When Employment for Specific Term: Plaintiff physician signed a 1-year employment contract with defendant medical center that provided that the employment terms could be extended or renewed by mutual agreement in writing. Although the initial contract expired, plaintiff continued to work by oral agreement for 2 more years. The parties then signed an addendum to the initial contract that set an employment expiration date 6 months later. Plaintiff received a letter 5 days before the expiration date, terminating the employment on the expiration date. Plaintiff filed a wrongful discharge suit, alleging that the termination was unlawful. Defendant moved for summary judgment on grounds that because the addendum provided a specific term of employment, plaintiff had no wrongful discharge claim. The District Court granted summary judgment for defendant, and plaintiff appealed, but the Supreme Court affirmed. A claim for relief that is predicated on discharge from employment is barred if the employment is for a specific term under a written contract and that term has expired. In this case, the addendum constituted a ratification of the original agreement that constituted a contract for a specific term of employment, and by executing the addendum, the parties ratified the original agreement calling for employment for a specific term. The fact that the termination date was stated in the contract recitals did not void the date, because the recitals were consideration for the agreement and the parties intended that the recitals be part of the agreement. Plaintiff's argument that because he did not read the addendum he should not be held to its terms was also without merit because one who executes a contract is presumed to know its contents. Stowers v. Community Medical Center, Inc., 2007 MT 309, 340 M 116, 172 P3d 1252 (2007).

Lessor Fully Compensated for Loss of Truck Under Rental Agreement — Agreed Value of Truck Inapplicable to Damage Claim: Plaintiff leased a truck to defendant for construction work. The truck had an agreed value of $250,000 and a rental rate of $12,000 a month. While in defendant's possession, the truck was heavily damaged. Plaintiff initially sought to repair the truck, but eventually it was stripped of usable parts, and the remaining shell was sold for $15,000. Plaintiff received $114,500 from its insurer, based on the insurer's calculation that the truck had a $126,000 cash replacement value minus the $2,500 policy deductible owed to plaintiff by defendant and minus a $9,000 salvage value. Plaintiff then sued defendant for the unpaid balance of the agreed value, including the monthly payments because the agreed value had not been paid. The District Court noted that even though the parties did not have a signed, enforceable, written contract, defendant had properly insured the truck pursuant to a reasonable lease term, identifying plaintiff as beneficiary, and held that defendant had no independent obligation to pay damages beyond the deductible. Because plaintiff had recovered all damages to which it was entitled, judgment was entered for defendant, and plaintiff appealed. The Supreme Court found that the language of the rental agreement did not require the lessee to pay the agreed value if the truck was damaged or destroyed, so defendant was not liable for the agreed value. Plaintiff failed to show the actual replacement cost of the truck and failed to establish that the District Court's finding was clearly erroneous, so the court did not err in holding that plaintiff was not entitled to additional compensation for replacing the truck. Additionally, plaintiff did not demonstrate what additional rental payments were owed, so defendant had no further obligation to pay damages for loss of use. The District Court did not err in holding that plaintiff was fully compensated under the rental agreement, and judgment was affirmed. Performance Mach. Co., Inc. v. Yellowstone Mtn. Club, LLC, 2007 MT 250, 339 M 259, 169 P3d 394 (2007).

Easement Limited to Historical Size and Location of Grant: In 1949, plaintiffs' predecessor in interest granted an easement to defendant's predecessor in interest to allow the construction of radio towers on a portion of a 160-acre parcel, conditioned on location and maintenance of the property. Defendant subsequently notified plaintiffs that he intended to expand the radio facilities beyond the original construction site. Plaintiffs sued, asserting that the expansion would encompass property not included in the original grant, while defendant contended that the easement encompassed the entire 160 acres described in the grant, so the facilities could be expanded onto other portions of the parcel or relocated elsewhere within the parcel. The District Court found for plaintiffs, and on appeal, the Supreme Court affirmed. Under the rules of contract construction, the grant language clearly limited placement of the radio facilities on a portion of the 160-acre parcel to be chosen by defendant's predecessor in interest. Thus, the easement did not encumber the full 160-acre parcel, but rather was limited in size and location to the historical location of the radio facilities. The original grant also required that wires, ground radial antennas, conduits, and transmission lines be buried to a minimum depth of 12 inches, and the District Court did not err in ordering defendant to bury the equipment pursuant to the maintenance portion of the grant. Anderson v. Stokes, 2007 MT 166, 338 M 118, 163 P3d 1273 (2007).

Y2K Computer Problems Considered Faulty Design and Inherent Vice — Insurance Coverage Precluded by Policy Exclusions: The state filed insurance claims related to remediation of problems associated with the Y2K transition. The claims were denied, and the state sued. The District Court held that the claims were precluded from coverage by policy language that excluded coverage for damage caused by faulty design and inherent vice. On appeal, the Supreme Court affirmed. An inherent vice is an existing defect, disease, or decay or the inherent nature of a commodity that will cause it to deteriorate over time and also means a loss not covered by a policy that is not related to an extraneous cause but to a loss entirely from internal decomposition or some quality that brings about its own injury or destruction and that must be inherent in the property for which recovery is sought. The state's Y2K problem was an excluded inherent vice because the date field was an inherent problem that brought about its own problem. The faulty design and inherent vice policy exclusions were not ambiguous and clearly excluded the claimed losses. Even though the state did not receive copies of the policies, the policies were renewals of existing policies that contained identical coverage provisions and exclusions, so the state could not reasonably claim that it was unaware of the relevant policy terms and exclusions, and the insurer could rely on valid exclusions in the policy when the state had notice of the exclusions. St. v. Allendale Mut. Ins. Co., 2007 MT 83, 337 M 49, 154 P3d 1233 (2007), following Port of Seattle v. Lexington Ins. Co., 48 P3d 334 (Wash. App. 2002), and GTE Corp. v. Allendale Mut. Ins. Co., 372 F3d 598 (3rd Cir. 2004).

Insurance Coverage for Intentional Dumping of Hazardous Waste Denied Under Policy Exclusion: For more than 3 years, defendant disposed of hazardous waste solvents into a sanitary landfill. The solvents migrated into the ground water, and neighbors sued defendant for personal injury and property damages. Defendant sought coverage from plaintiff insurer to remediate the damages and costs for the third-party suits, and the insurer eventually sought a declaration that it owed no duty to provide insurance coverage and defense costs for the environmental claims. Defendant's insurance policy contained a pollution exclusion that barred coverage for environmental damage unless the pollution was sudden or accidental. The District Court granted plaintiff summary judgment, and defendant appealed. The Supreme Court applied general rules of contract law, strictly construing the policy provisions in favor of defendant, but affirmed summary judgment absent ambiguity in the policy language. Under the policy, the initial disposal, rather than the migration and any resulting damages, had to be sudden and accidental in order to fall within the pollution exclusion clause. Defendant's routine intentional disposal of waste over a period of years could not be considered sudden or accidental, so defendant was unable to establish that the claims fell within the basic scope of coverage. Thus, plaintiff had no duty to defend defendant, and summary judgment for plaintiff was proper. Travelers Cas. & Sur. Co. v. Ribi Immunochem Research, Inc., 2005 MT 50, 326 M 174, 108 P3d 469 (2005). See also Bozeman v. AIU Ins. Co., 272 M 349, 900 P2d 929 (1995), and Makarka v. Great Am. Ins. Co, 14 P3d 964 (Alaska 2000).

No Duty to Defend Property Damage or Fraud Claim When No Property Damage or Fraud Asserted: Defendant contended that plaintiff insurer had a duty to defend and provide coverage under defendant's commercial general liability policy, which provided coverage for property damages. However, the claim did not seek compensation for property damages for physical injury to tangible property, but rather for sums fraudulently paid to defendant based on a breach of contract. Because allegations in the complaint did not set forth facts that brought the event within the policy provisions and specifically excluded coverage for a fraud claim, the insurer had no duty to defend the claim. Generali-U.S. Branch v. Alexander, 2004 MT 81, 320 M 450, 87 P3d 1000 (2004), following Graber v. St. Farm Fire & Cas. Co., 244 M 265, 797 P2d 214 (1990). See also Farmers Ins. Exch. v. Minemyer, 2023 MT 138, 413 Mont. 60, 532 P.3d 837, holding that claims for purely economic loss do not create a duty to defend against property damage when no direct physical injury occurred.

Coordination of Habendum and Pugh Clauses in Oil and Gas Lease — Shut-In Gas Well Considered Producing Well for Lease Purposes — Lease Extended on Section With Producing Well, Terminated on Undeveloped Sections for Lack of Timely Rental Payments: Plaintiff's oil and gas leases had habendum clauses, which provided that the primary leases would be extended as long as oil or gas was produced or drilling operations continued on any of the leased property, and Pugh clauses, which provided that production would not serve to extend the primary term of a lease unless the lessee paid an annual per-acre rental fee prior to the end of the primary term. By the end of the primary term, plaintiff had only one shut-in well developed on the leasehold. Depending on the habendum clauses, plaintiff concluded that there was not a producing well on the leasehold, so the Pugh clauses did not take effect and rental payments were not required. Depending on the Pugh clauses, defendants concluded that because there were no producing wells on the leasehold and because the rental fee on the shut-in well was 2 days late, all of plaintiff's leases were canceled. In reconciling the clauses, the District Court correctly found that: (1) the Pugh clauses required that rental payments be paid on or before the expiration of the primary term in order to extend leases on undeveloped sections; and (2) because time is of the essence in oil and gas leases and plaintiff did not pay timely rental, the leases expired by their own terms on all sections except the section containing the shut-in well, which was considered a producing well, and that lease would continue under the habendum clause as long as plaintiff used reasonable diligence in marketing the gas. Sandtana, Inc. v. Wallin Ranch Co., 2003 MT 329, 318 M 369, 80 P3d 1224 (2003).

Attempted Sale of Parcel in Violation of Contract — Plantiff Allowed to Block Sale: Defendants contracted to purchase several parcels of property from plaintiff. When defendants ended up in default, defendants decided to sell one of the parcels to pay off part of the contract balance. Plaintiff attempted to block the sale, and the District Court confirmed plaintiff's ability to do so under the terms of the contract. Defendants appealed, but the Supreme Court affirmed. A provision of the contract allowed the subsequent sale of the parcels by defendants, but only after the principal balance was paid. Because defendants were in default when the attempted sale was made, sale of the tract was not permitted by the terms of the contract. The District Court did not err in holding that plaintiff had a contractual right to block the sale. Weter v. Archambault, 2002 MT 336, 313 M 284, 61 P3d 771 (2002).

Declaration Divided Into Two Parts — Restrictive Covenants Not Enforceable on Property Not Subject to Declaration — Attorney Fee Provisions of One Part Not Enforceable in Other Part: The Milltown Water User's Association's Declaration of Covenants, Conditions, and Restrictions is divided into two parts. Part I provides for the operation and maintenance of the Milltown water system and allows for the award of attorney fees and costs. Part II establishes the Milltown Addition Homeowners' Association (MAHA) and places various restrictive covenants on the use and development of affected properties. MAHA sued to enforce the restrictive covenants in Part II and for monetary damages pursuant to Part II's enforcement provisions. In addition, MAHA sought and was awarded attorney fees and costs under Part I. The appellants appealed the part of the District Court's injunction that enjoined the appellants from keeping junk vehicles on any property that they might own and the award of attorney fees and costs under the declaration. On appeal, the Supreme Court held that the District Court order was overly broad and must be narrowed to apply only to property owned by the appellants and subject to the declaration and that MAHA was not entitled to attorney fees and costs under Part I. Milltown Addition Homeowners' Ass'n v. Geery, 2000 MT 341, 303 M 195, 15 P3d 458, 57 St. Rep. 1460 (2000).

Gradual Accumulation of Smoke and Soot — "Sudden and Accidental" Construed — Damage Not Covered Under Pollution Exception to All-Risk Homeowner's Policy: During a 4- or 5-week holiday season, the Sokoloskis burned scented candles in their home, which caused a discharge of smoke and soot, damaging their home and belongings. Their insurer denied coverage under a pollution exclusion because smoke and soot were defined as pollutants in the policy. The District Court held that coverage was barred under the exclusion and that the damages were not sudden and accidental. The Supreme Court affirmed on both issues. The very use of the words "sudden" and "accidental" reveals a clear intent to state two separate requirements, so that "sudden" means more than "unexpected". "Sudden", even if it includes the concept of unexpectedness, also encompasses a temporal element because unexpectedness is already expressed by the word "accidental". Having determined that the damage was not sudden, the Supreme Court did not address the additional requirement of being accidental. Under the clear language of the policy definitions and exclusion clause, coverage was properly barred and summary judgment proper. Sokoloski v. Am. W. Ins. Co., 1999 MT 93, 294 M 210, 980 P2d 1043, 56 St. Rep. 392 (1999), citing N. Ins. Co. of N.Y. v. Aardvark Assoc., Inc., 942 F2d 189 (3rd Cir. 1991), and followed in Travelers Cas. & Sur. Co. v. Ribi Immunochem Research, Inc., 2005 MT 50, 326 M 174, 108 P3d 469 (2005).

Contract Providing for Both Termination and Renegotiation — Plain Language to Determine Parties' Standing: Paragraph 7 of a contract provided that the contract terminated on June 30, 1996. Paragraph 10 provided for renegotiation of the contract upon 30 days' written notice from either party. The District Court found the provisions to be at odds with each other. The law favors giving effect to each provision of a contract, and courts must interpret contractual provisions so as to allow each provision to be effective. Courts are without authority to insert components in or erase components from unambiguous contract provisions. Upon review, the Supreme Court looked to the plain language in the contract and found that paragraph 10 did not render the contract vague or indefinite; rather, it provided for a continuing contractual relationship if, after notice, a successful renegotiation was accomplished. The District Court erred, and the case was reversed and remanded for further proceedings. Hennen v. Omega Enterprises, Inc., 264 M 505, 872 P2d 797, 51 St. Rep. 369 (1994), followed in Corwin v. Bd. of Pub. Educ., 272 M 14, 898 P2d 1227, 52 St. Rep. 589 (1995).

Oil Lease Construed to Make All Provisions Effective: Texaco argued that the one productive well it had drilled was sufficient to extend the lease on all lands covered by the lease for as long as the well produced. The Supreme Court held that the general duration clause in the lease relied on by Texaco was modified by a subsequent provision that limited the lease extension to the 320-acre spacing unit on which the producing well was located. Fed. Land Bank of Spokane v. Texaco, Inc., 250 M 471, 820 P2d 1269, 48 St. Rep. 998 (1991).

Complaint Alleging Events Not Within Policy Coverage — No Duty to Defend: As set out in Atcheson v. Safeco, 165 M 239, 527 P2d 549 (1974), the general rule is that an insurer has a duty to defend when a complaint filed against its insured sets forth facts that bring an event within the policy provisions. However, when the complaint alleges events not within the coverage of the policy and the insurer would not be obligated to indemnify the insured if the complaining party recovered, then the insurer has no duty to defend. Graber v. St. Farm Fire & Cas. Co., 244 M 265, 797 P2d 214, 47 St. Rep. 1595 (1990), followed in Brabeck v. Employers Mut. Cas. Co., 2000 MT 373, 303 M 468, 16 P3d 355, 57 St. Rep. 1596 (2000), and Generali-U.S. Branch v. Alexander, 2004 MT 81, 320 M 450, 87 P3d 1000 (2004).

Termination of Lease and Royalty Interest — No Error in Summary Judgment: The District Court did not err in granting a summary judgment when several contracts relating to the same matter and made as substantially one transaction clearly showed that a lease assignment incorporating by reference the exhibit which created an overriding royalty interest in defendant included language that the assignors were owners of the overriding royalty interest of which the defendant received a one-fourth interest and which terminated with the lease. Edward v. Prince, 221 M 272, 719 P2d 422, 43 St. Rep. 805 (1986).

Responsibility for Water and Sewer Hookup Determined by Complete Reading of Contract: The Supreme Court reversed a District Court decision that a subcontractor was obligated to connect water and sewer lines to houses in a project. A complete reading of the contract showed that the subcontractor only had to cap the lines at terminal points. The whole of a contract is to be taken together to give effect to every part if reasonably practicable, each clause helping to interpret the other. Bender v. Rookhuizen, 211 M 366, 685 P2d 343, 41 St. Rep. 1418 (1984). See also Monte Vista Co. v. The Anaconda Co., 231 M 522, 755 P2d 1358, 45 St. Rep. 809 (1988).

Ambiguous Phrase — Entire Contract to Determine Intent: A coal contract was entered on March 31, 1974. In 1976, the Montana Department of State Lands (functions now transferred to Department of Environmental Quality) determined that Decker was precluded under Title 82, ch. 4, part 2, from disturbing a certain portion of land within the mine area contemplated by the contract. It was conceded this would increase mining costs. The contract contained a price adjustment provision that allowed for price adjustments due to new government regulation. Decker contended the nondisturbance determination was a "new regulation" even though the statute under which the Department acted was enacted in 1973. The court in construing "new regulation" looked to the entire contract to determine mutual intent. The court determined, in light of adjustment provisions for all other cost increases, that "new regulation" meant increases required by government action taken after the effective date of the contract. Austin v. Decker Coal Co., 701 F2d 420 (5th Cir. 1983).

Requirement of Annual Amortization Payments Consistent With Purpose of Land Exchange Agreement: Shortly after entering into a land purchase agreement, the parties changed the agreement into a tax-free land exchange agreement. The new agreement gave buyer 3½ years to acquire like-kind property to be exchanged for seller's ranch. The like-kind property was to be purchased with funds placed periodically by buyer in an escrow account. Several years later a dispute arose concerning the nature and timing of the payments. Buyer submitted the questions to the District Court in a declaratory judgment action. The District Court interpreted the contract in a manner generally favorable to seller, and buyer appealed, claiming that the District Court's decision was unreasonable, contrary to the parties' intentions, and improper under the rules of construction of contracts. The Supreme Court affirmed, ruling that the District Court's interpretation had not been unreasonable since: (1) its decision on the timing of the rental payments was reflective of the parties' intentions as shown by their past performance; (2) its decision on the timing of the amortization payments was consistent with the rule of construction requiring that a contract be construed in such a way as to give effect to all of its provisions; and (3) its ruling on the intention of the parties was supported by the evidence. Finally, 28-3-206 did not entitle buyer to have ambiguities construed in his favor; even though buyer claimed that the nature of the agreement was changed solely for seller's benefit, the agreement was prepared by an attorney for both parties, not by one party alone. Lewis v. Murphy, 199 M 368, 649 P2d 740, 39 St. Rep. 1459 (1982).

Amount of Rent — Essential Lease Term Requiring Certainty: Appellants signed a lease with an option to renew the lease. Although the appellants properly gave notice of intent to exercise the option, the renewal provision failed for lack of certainty regarding the amount of the rent because a determination of the amount of the rent upon renewal was based on bids from third parties. In this case, there was no such bid and therefore no means of determining the amount of the rent. The renewal provision of the lease was void for lack of certainty regarding the essential term of rent. Riis v. Day, 188 M 253, 613 P2d 696, 37 St. Rep. 1093 (1980), followed in Nentwig v. United Indus., Inc., 256 M 134, 845 P2d 99, 49 St. Rep. 1172 (1992), and GRB Farm v. Christman Ranch, Inc., 2005 MT 59, 326 M 236, 108 P3d 507 (2005).

Contract for Joint Purchase of Property — Construction of Contract as a Whole: Where the appellant and respondent entered into an agreement whereby the respondent agreed to loan appellant the down payment for the purchase of real property on a contract for deed, the District Court correctly looked to the clear language of the instrument as a whole to determine the intentions of the parties, and phrases relied on by the appellant would not be taken out of context to reach the result urged by the appellant. Downs v. Smyk, 185 M 16, 604 P2d 307 (1979).

Right of First Refusal in Lease: Contract was interpreted as sustaining lessees' right of first refusal of purchase. Tribble v. Reely, 171 M 201, 557 P2d 813 (1976), distinguished in Wymo Land Co. v. Luggie, 1998 MT 50, 288 M 21, 955 P2d 171, 55 St. Rep. 208 (1998).

Duty of Insurance Company to Defend: Insurance company that had agreed to defend taxidermist against liability for the risks incurred by shipping had a duty to defend him against complaint of customer alleging delivery of substituted animal heads. Atcheson v. Safeco Ins. Co., 165 M 239, 527 P2d 549 (1974).

Indemnity Clause: Printed indemnity clause on back of purchase order was inoperative where typed portion of purchase order merely accepted offer of seller with specific reference to attached modifications and made no mention of indemnity clause. Hoerner Waldorf Corp. v. Bumstead-Woolford Co., 158 M 472, 494 P2d 293 (1972).

Purchase of Liquor License: Where agreement to buy liquor license stated that $9,000 was the consideration for the license, and also, in another part of the agreement, it was stated that the assignee would assume the assignor's lease to certain premises, the agreement was construed to mean that the parties actually intended that both the money and the assumption of the lease were consideration for purchase of the liquor license. Kintner v. Harr, 146 M 461, 408 P2d 487 (1965).

Insurance Contract: In construing an insurance contract effect must be given to every part of the insurance policy. Kansas City Fire & Marine Ins. Co. v. Clark, 217 F. Supp. 231 (D.C. Mont. 1963), affirmed in 329 F2d 647 (9th Cir. 1964).

Construction of Deeds:

A quitclaim deed and assignment of contract for deed may be construed as security for the payment of a promissory note. Kraus v. Newman, 137 M 388, 352 P2d 261 (1960).

Where a deed of land contained a clause following the description of the land which said "including one-half of all oil and gas rights owned by the parties", it must be considered that it was the intention of the parties to exclude from the deed the other one-half interest in the oil and gas and that such one-half remained with the grantor. Wyrick v. Hoefle, 136 M 172, 346 P2d 563 (1959).

General Language Prevails: Mere isolated tracts, clauses, and words will not be allowed to prevail over the general language utilized in the instrument. Steen v. Rustad, 132 M 96, 313 P2d 1014 (1957).

Intention of Parties:

A court in interpreting a written instrument will not isolate certain phrases of that instrument in order to garner the intent of the parties, but will grasp the instrument by its four corners and in the light of the entire instrument ascertain the paramount and guiding intention of the parties. Steen v. Rustad, 132 M 96, 313 P2d 1014 (1957).

In the construction of a contract the intention of the parties at the time of contracting must be pursued if possible, which intention must be gathered from the entire instrument and not from particular words or phrases or disjointed parts of it, and in the ascertainment of such intention the subject matter of the contract and the purposes of its execution are material. St. v. Rosman, 84 M 207, 274 P 850 (1929).

The intention of the parties to a deed is to be ascertained from the language thereof, viewed in its entirety, and not as it is presented in particular sentences or paragraphs. R. M. Cobban Realty Co. v. Donlan, 51 M 58, 149 P 484 (1915).

Lease With Option to Buy: Plaintiff's option to buy was exclusive and not conditioned upon defendant's decision to sell where instrument did not use the term "first option to buy" and the entire language of the agreement showed that plaintiff was given an exclusive option to buy the property described under the lease. His method of exercising his option was by tendering $1,500 to the defendant, as called for by "Plan No. 2". Steen v. Rustad, 132 M 96, 313 P2d 1014 (1957).

Farm Leases: Under this section farm lease contracts are to be read as a whole and not by particular paragraphs or sentences, and under 28-3-206 and 28-3-306 any ambiguities in such a lease should be construed against the lessor. Tenant was entitled to compensation for summer-fallowing he did during the last year of his holding where he did not renew and the lease was given to another; and where lease required 80 acres to be summer-fallowed, but tenant found only 74.5 acres of tillable land, he substantially complied. Letz v. Lampen, 110 M 477, 104 P2d 4 (1940).

Verbal Clarity: In the construction of a contract its language is to be resorted to in the first instance, but the conclusion to be reached depends not upon the verbal clarity of the particular sentences or paragraphs but upon the view to be taken of it in its entirety. Roecher v. Commercial Nat'l Bank, 87 M 570, 289 P 388 (1930).

28-3-203. When several contracts taken together.

Case Notes

General 365
Construction of Agreements 367
Parties to Agreements 369
Separate or Void Transactions 370

GENERAL

Contradicting Clauses in Separate Contracts Construed Against Drafter — Employee Waiver — Health Insurance: The plaintiff health insurance company filed a breach of contract action against the defendant, an employer providing health insurance for its employees. The contracts between the parties required the defendant to cover 75% or more of its employees; however, a subsequent contract allowed the defendant's employees to waive coverage. The District Court granted summary judgment in favor of the defendant, finding that the two provisions in the contracts were ambiguous and the contract should be interpreted against the drafter. On appeal, the Supreme Court affirmed, holding that the contracts must be interpreted as part of the same transaction and that giving effect to both contract provisions is not reasonably practical, that the ambiguity is construed against the drafter, that the newer specific contract controlled over the older general contract, and that the waiver provision was meant to modify the minimum employee participation provision. Mont. Health Network, Inc. v. Great Falls Orthopedic Associates, 2015 MT 186, 379 Mont 513, 353 P.3d 483.

Property Covenants and Settlement Agreement Substantially One Transaction: The plaintiffs sued the subdivision property owners over amendments to the covenants. Prior to trial, all but one of the subdivision property owners settled with the plaintiffs. The settlement included executing new covenants. The District Court then ruled against the remaining defendant and awarded attorney fees. The Supreme Court held that the settlement agreement and covenants should be viewed as one transaction. Houden v. Todd, 2014 MT 113, 375 Mont. 1, 324 P.3d 1157.

Express Lease Provision Required for Survival of Overriding Royalty: An overriding royalty applies only to the lease out of which it was created. In the case of an oil or gas lease or sublease, if a party wishes an overriding royalty to survive the expiration of the lease or sublease, an express provision must be included in the lease or sublease to accomplish survival of the overriding royalty. Ritter v. Bill Barrett Corp., 2009 MT 210, 351 M 278, 210 P3d 688 (2009), following Edward v. Prince, 221 M 272, 719 P2d 422 (1986).

Parol Evidence of Circumstances Under Which Bid Prepared Proper in Interpreting Uncertain Contract Provisions: Bid estimates on a road building project contained vague and ambiguous project requirements, and testimony at trial regarding the height of the finished road was conflicting. Thus, the District Court, in interpreting provisions of the contract that appeared ambiguous or uncertain, properly considered parol evidence of the circumstances under which the bid was prepared. The court found more credible the contractor's testimony that there was not agreement that a subroad would be constructed of pit run gravel 6 inches above field grade, and that determination was affirmed on appeal. DeNiro v. Gasvoda, 1999 MT 129, 294 M 478, 982 P2d 1002, 56 St. Rep. 521 (1999).

Duty of Escrow Holder to Clear Title: As a matter of contract law, it was the contractual duty of the escrow holder in this case to clear title to the parcel of land involved and then distribute the balance of the funds accruing from the sale of the land to the holders of underlying mortgages. First Mont. Title Co. v. N. Point Square Ass'n, 240 M 33, 782 P2d 376, 46 St. Rep. 1920 (1989).

Termination of Lease and Royalty Interest — No Error in Summary Judgment: The District Court did not err in granting a summary judgment when several contracts relating to the same matter and made as substantially one transaction clearly showed that a lease assignment incorporating by reference the exhibit which created an overriding royalty interest in defendant included language that the assignors were owners of the overriding royalty interest of which the defendant received a one-fourth interest and which terminated with the lease. Edward v. Prince, 221 M 272, 719 P2d 422, 43 St. Rep. 805 (1986).

Contract and Bond: Subcontractor's agreement with contractor and bond covering subcontractor were construed together in suit by contractor on subcontractor's bond. Carl Weissman & Sons, Inc. v. St. Paul Fire & Marine Ins. Co., 152 M 291, 448 P2d 740 (1968).

Contract to Purchase and Quitclaim Deed: Where contract to purchase land, being in effect an option to purchase, and a quitclaim deed to the same land were made at the same time, the deed and contract constituted a single transaction and must be construed together. Ryan v. Bloom, 120 M 443, 186 P2d 879 (1947).

Note and Mortgage: Under this section, declaring that several contracts relating to the same matter and made as parts of substantially one transaction must in their interpretation be taken together, in a mortgage foreclosure suit the mortgagor's note, the mortgage, and an assignment of rents and profits derived from the property during the time the indebtedness remained unpaid were constituent parts of one transaction, to be considered together for all purposes. U.S. Bldg. & Loan Ass'n v. Burns, 90 M 402, 4 P2d 703 (1931).

Contract for Real Property Sale: Under this section all documents signed by the parties to a contract of a sale of real property, such as promissory note, mortgage, etc., are to considered as parts of one transaction and construed together. Adamczik v. McCauley, 89 M 27, 297 P 486 (1931).

No Mention of Other Document: Under this section, providing that several contracts relating to the same matter, between the same parties, and made as parts of substantially one transaction must be taken together, stipulations embodied in a mortgage become a part of the note securing which it is given even though the note contains no mention of the mortgage. Vande Veegaete v. Vande Veegaete, 75 M 52, 243 P 1082 (1925).

Same Matter — Same Transaction: Several contracts relating to the same matter and made as parts of substantially the same transaction must be taken together for all purposes. U.S. Nat'l Bank of Red Lodge v. Chappell, 71 M 553, 230 P 1084 (1924).

Note and Mortgage — Absence of Signature: The defendants obtained a loan and executed a promissory note. To secure payment, they at the same time executed a mortgage on certain personal property. After default, defendant contended a stipulation in the mortgage permitting acceleration was not part of the bargain because she had not signed the mortgage. The court held that where two or more contracts are parts of the same transaction, are known to all parties, and are delivered at the same time to accomplish an agreed purpose, the agreements are treated as one and liability cannot be avoided by not signing one of the contracts. Union Bank & Trust v. Himmelbauer, 56 M 82, 181 P 332 (1919), affirmed, 57 M 438, 188 P 940 (1920).

Last Document Referring to Others: Where different writings have relation to the same subject matter, the last referring to the others, the intention of the parties must be ascertained by construing all of the writings together as one entire contract. Lyon v. Dailey Copper Min. & Smelting Co., 46 M 108, 126 P 931 (1912).

Lease and Bond to Pay Rent: A bond given to secure the payment of rent which was signed after the lease of the property had been executed was not nudum pactum where both instruments were executed on the same day and where the bond referred to and made the latter instrument a part of it. They must be construed as having been executed contemporaneously and as amounting to one instrument. Dodd v. Vucovich, 38 M 188, 99 P 296 (1909).

Same Transaction: Where a note, deed, and defeasance were all executed at the same time, had reference to the same subject matter, and were a part of the same transaction, the deed being intended as a mortgage to secure the note, the three instruments should be construed as one as provided in this section. Bartels v. Davis, 34 M 285, 85 P 1027 (1906).

Note and Contract of Purchase: Where a note sued on was given in consideration of the written contracts of the payee, made a few days before the date of the note, that he would on or before a certain day purchase or procure a purchaser for the maker's interests in certain mines at a stated price, and that if he failed so to do the maker would be absolved from all liability to convey such interests, these contracts were admissible under this section as relating to the same matters as the note in suit between the same parties and as parts of substantially one transaction. Talbott v. Heinze, 25 M 4, 63 P 624 (1901).

CONSTRUCTION OF AGREEMENTS

Potential Access Rights Merged With Deeds and Extinguished — Applicability of Contract Law Doctrine of Merger: Prior to Gehring's consent to sell 360 acres to APS Corporation (APS) in 1970, they entered an agreement that included a provision on access rights, whereby Gehring purported to grant future purchasers access to other land owned by Gehring for certain recreational purposes. After being told by the Gehring Ranch Corporation that they would not be allowed access to Gehring's land for recreation, the successors in interest to APS sought to enforce the agreement, alleging that they had been improperly excluded from the land and that the agreement created an easement over Gehring's land. The District Court granted summary judgment for the Gehring Ranch Corporation, noting that the agreement did not identify Gehring's other lands upon which an easement was purportedly created. The court also held that any agreement prior to execution of the deeds was merged with the deeds and that because the deeds transferring title did not provide for access, any access rights promised in the agreement were lost. The decision was appealed, and the Supreme Court affirmed. The clause in the agreement was part of a larger agreement to transfer property in the future, and Gehring did not intend to create an easement, but at most intended to provide for potential access privileges if certain conditions, such as creation of a property owners' association and adoption of rules governing the use of the recreational privileges, were met. The Supreme Court cited Urquhart v. Teller, 1998 MT 119, 288 M 497, 958 P2d 714 (1998), in applying the contract law doctrine of merger, holding that the deeds contained all the rights of the parties and that because no access privileges were mentioned in the deeds, any potential access rights referred to in the agreement merged with the deeds and were lost. Richman v. Gehring Ranch Corp., 2001 MT 293, 307 M 443, 37 P3d 732 (2001).

Shareholders' Agreement Enforceable Independent of Stock Exchange — Different Intent Contained in Separate Agreements Separately Enforceable: Following his termination from employment with Bitterroot International Systems, Inc. (Bitterroot), Knutson sought to exercise his buyout rights under the shareholders' agreement. Bitterroot refused to pay, contending that an earlier merger transaction and the subsequent shareholders' agreement should be read together and citing Rumph v. Dale Edwards, Inc., 183 M 359, 600 P2d 163 (1979), for the proposition that when construing an agreement that is part of a larger transaction, the intention of the parties must be determined by examining the entirety of the larger transaction. However, Rumph was distinguishable here because all the agreements in question occurred at different times and did not reference or depend upon each other. Each agreement was clear and unambiguous. Under Gerdes v. Omaha Home for Boys, 89 NW 2d 849 (Nebr. 1958), a court may not avoid the language of a complete, unambiguous contract by consolidating it with another writing if the effect of doing so would be to avoid an essential part of the contract. The District Court properly concluded that the shareholders' agreement was enforceable independent of the stock exchange between the parties. Knutson v. Bitterroot Int'l Sys., Inc., 2000 MT 203, 300 M 511, 5 P3d 554, 57 St. Rep. 800 (2000), followed in O'Brien v. O'Brien, 2022 MT 246, 411 Mont. 101, 532 P.3d 831.

Five Agreements Constituting Integrated Sales Agreement With Condition Precedent — Overriding Previous Partnership Agreements and Providing for Attorney Fees: Daines argued that of the five agreements executed by the parties, the option agreement should have been read separately and interpreted as an option to buy conferring a privilege but not imposing an obligation and that on that basis, he could not be liable for not completing a purchase agreement. The Supreme Court held that the lower court had properly looked at the five agreements as a whole in interpreting the parties' intent and had correctly concluded that the agreements constituted an integrated sales agreement subject to conditions precedent. The Supreme Court further held that since the five agreements constituted a sales agreement, they superseded the previous partnership agreements. The respondents were not liable for capital contributions as partners, and the default provision in the option agreement providing for attorney fees did apply to the agreement created by all five of the documents executed by the parties. Daines v. Knight, 269 M 320, 888 P2d 904, 52 St. Rep. 8 (1995).

Merger of Prior Agreement Into Deed — No Presumption of Surrender of Covenants: Appellants contended that since there was no express language in deeds recorded in 1972 that the parties intended to merge the restrictive provisions of a 1971 agreement into the deeds, the commercial use restrictions in the 1971 agreement still applied, regardless of being left out of the deeds. The Supreme Court, recalling its decision in Story v. Montforton, 112 M 24, 113 P2d 507 (1941), noted that "whether or not there has been a merger depends on the intention of the parties". The court applied this principle in Thisted v. Country Club Tower Corp., 146 M 87, 405 P2d 432 (1965), quoting Reid v. Sykes, 27 Ohio St. 285: "... evidence of that intention may exist in or out of the deed. There is no presumption that a party, in giving or accepting a deed, intends to give up the covenants of which the deed is not a performance or satisfaction." In the present case, the court found strong evidence that the deeds contained all of the restrictions on the lands that were intended by the parties and that the contract had merged in the deeds. Haggerty v. Gallatin County, 221 M 109, 717 P2d 550, 43 St. Rep. 674 (1986).

Documents Construed Together — Intent Not Gleaned From Isolated Words: When there is a close relationship between two documents, they must be construed together to determine the intent of the parties. The intent is determined by reading the two documents in full rather than dissecting them to take isolated words and phrases as the intent of the parties. Rumph v. Dale Edwards, Inc., 183 M 359, 600 P2d 163 (1979), distinguished in Knutson v. Bitterroot Int'l Sys., Inc., 2000 MT 203, 300 M 511, 5 P3d 554, 57 St. Rep. 800 (2000), and followed in Richman v. Gehring Ranch Corp., 2001 MT 293, 307 M 443, 37 P3d 732 (2001).

Contrary Intention: The general rule is that where several instruments are executed at the same time by the same parties, for the same purpose, and in the course of the same transaction, they are treated as one instrument and are construed together. That is not the case where a contrary intention can be determined from the instruments. In this case neither the purchase order, a quotation, or a letter incorporated an indemnity provision, which is required to be stated in clear and definite language. Hoerner Waldorf Corp. v. Bumstead-Woolford Co., 158 M 472, 494 P2d 293 (1972).

Operation in General: This section does not in any way conflict with 28-2-905, which requires in part that outside evidence may not be used to vary the terms of a written contract, since facts relevant to the formation of the instrument, as defined in 1-4-102, may be introduced to settle ambiguities. Thisted v. Country Club Tower Corp., 146 M 87, 405 P2d 432 (1965).

Sale of Real Estate: Corporation which sold apartments in a condominium was bound by the language in the sales contract to the first purchaser, so that even though restriction requiring the premises to be used for residential purposes was not employed in subsequent contracts, such equitable servitude still attached to subsequent deeds. Thisted v. Country Club Tower Corp., 146 M 87, 405 P2d 432 (1965).

Several Writings Comprising Contract — Conditional Sale — Increase of Animals: Where a promissory note containing a conditional sale contract would not have been executed without a contemporaneous agreement relative to the animals covered by the sale contract under which the seller agreed to purchase their increase under certain conditions, the two instruments together formed the contract and were to be read together. Apple v. Edwards, 92 M 524, 16 P2d 700, 87 ALR 179 (1932).

Single Document Not Determinative of Rights: Where a contract did not in itself determine all rights, duties, and obligations of the parties but specifically referred to other contracts that would be determinative, all the writings were considered together in determining the meaning of the contract. Great W. Oil Co. v. Lewistown Oil & Ref. Co., 91 M 146, 6 P2d 863 (1931).

Application for Loan: In constructing several contracts relating to the same subject matter and constituting substantially parts of one transaction (application for loan from a building and loan association, note, and mortgage), the intention of the parties must be gathered from the writings, read together, reviewing all their terms, since one clause may modify, limit, or illuminate another. U.S. Bldg. & Loan Ass'n v. Gardiner, 87 M 586, 289 P 555 (1930).

Reference to Another Contract: A contract will not be held to incorporate stipulations embodied in another contract save insofar as the same are specifically set forth or identified by reference. St. Bank of Darby v. Pew, 59 M 144, 195 P 852 (1921).

Deed and Condition Subsequent: A deed was made upon a condition subsequently imposed by a separate writing, under the terms of which the grantee obligated herself to make a stipulated monthly payment to a third person, with reversion in favor of the grantor. The deed and written agreement were part of and constituted the same transaction, regardless of whether they were executed at the same time or not. Smith v. Hoffman, 56 M 299, 184 P 842 (1919).

Together for All Purposes: Stipulations in a mortgage are to be construed as entering into and becoming a part of the note secured thereby, and if the two are to be taken together, they must be considered together for all purposes. Union Bank & Trust Co. v. Himmelbauer, 56 M 82, 181 P 332 (1919).

PARTIES TO AGREEMENTS

Contracts Executed by Corporation and Owners of Corporation Not Construed Together: Plaintiff sold six lots to Griff and Caplan and sold seven lots to a corporation owned by Griff and Caplan. The corporation stopped making payments, after which the plaintiff refused payments offered by the individual. Plaintiff then brought suit, arguing that the two contracts were really one. The court found that the contracts speak for themselves. Neither makes the slightest reference to the other. The parties to the contract are not the same as the plaintiff contends, although there is some evidence to support the plaintiff. There is also substantial evidence to support the finding of the trial court. Wortman v. Griff, 200 M 528, 651 P2d 998, 39 St. Rep. 1916 (1982).

Issue of Fact as to Whether a Written Agreement Supersedes an Oral Agreement: Plaintiff's motion for summary judgment was properly denied where there was some question of fact as to whether one written agreement, signed by plaintiff as agent for his company, by the company vice-president and by defendant, entitling defendant to a salary advance, supersedes a prior oral agreement allegedly made between plaintiff and defendant in which plaintiff personally guaranteed a salary to defendant. Reviewing the relationship of the two agreements in the light most favorable to the defendant, the alleged oral agreement is collateral to the written contract, is distinct, involves a different party, and is able to stand independently of the other. Reaves v. Reinbold, 189 M 284, 615 P2d 896, 37 St. Rep. 1500 (1980).

Identical Parties Required: An alleged breach of employment did not constitute a breach of exclusive listing agreement when it was obvious that the two agreements were between different parties. McDonald & Co. v. Fishtail Creek Ranch, 175 M 53, 572 P2d 195 (1977).

Where Contracts Read Together Though Parties Not Same: The rule that where several instruments are made at the same time in relation to same subject matter they may be read together as one instrument and recitals in one may be limited by reference to the other may obtain even when parties are not the same, if the several instruments were known to all parties and were delivered at the same time to accomplish an agreed purpose. Doheny v. USF&G Co., 34 F. Supp. 888 (D.C. Mont. 1940), affirmed in USF&G Co. v. Doheny, 123 F2d 746 (9th Cir. 1941), certiorari denied, 62 S Ct 905, 315 US 817, 86 L Ed 1215 (1941).

Letter and Contract of Sale: Where two writings, one a contract of sale of livestock and the other a letter to the buyer, written by the agent of the seller, referring to the time of payment, were delivered at the same time, they were properly considered together in an action to recover the purchase price, irrespective of the fact that the letter was signed only by plaintiff's agent; the letter having constituted an offer with reference to the time of payment, which was accepted by defendant buyer, relied and acted upon by the latter, it constituted a part of the contract of sale. Orem v. Hansen Packing Co., 91 M 222, 7 P2d 546 (1932).

Deed to Mortgaged Property: Where preliminary agreements culminating in a deed to mortgaged property by the mortgagor to the mortgagee were made in consideration of the execution and delivery of the deed, the several transactions had at the same time must be taken together and considered as though all the promises, agreements, and obligations of the parties were contained in a single instrument signed by all the parties; hence the fact that the wife of the mortgagor did not sign one of the agreements did not render the deed invalid, she having been a party to the entire transaction, taking part therein with full knowledge of all the facts. Cooper v. Goble, 77 M 580, 252 P 362 (1926).

SEPARATE OR VOID TRANSACTIONS

Property Settlement: Agreements as to disposition of property between estranged husband and wife, which were obviously to become operative in the future when a divorce proceeding was instituted, with condition that resistance to divorce would render the property settlement nugatory, when construed together, facilitated divorce and were void as a violation of public policy. W. Life Ins. Co. v. Bower, 153 F. Supp. 25 (D.C. Mont. 1957), affirmed in Bower v. Bower, 255 F2d 618 (9th Cir. 1958).

Consideration for Separate Agreements: Provision of property settlement agreement under which husband relinquished right to change beneficiary of life insurance policy was severable from provisions facilitating divorce and was enforceable where wife presumably released certain property rights in consideration therefor. W. Life Ins. Co. v. Bower, 153 F. Supp. 25 (D.C. Mont. 1957), affirmed in Bower v. Bower, 255 F2d 618 (9th Cir. 1958).

When Construed Separately: The rule that more than one contract relating to the same subject matter between the same parties and made as parts of substantially one transaction must be construed together has no application in an action on a surety bond conditioned to pay the amount found to be due under the terms of a contract for the sale of state timber if the buyer failed to pay, the parties not being the same and the obligations thereunder being entirely separate and distinct. St. v. Am. Sur. Co. of New York, 78 M 504, 255 P 1063 (1927).

Loan Application on Life Insurance: An application to an insurance company for a loan "payable at the home office" of the company requesting interest coupons to be sent to a certain bank "and at my risk until payments made are actually received by the company at its home office" signed by the applicant was not a contract within the meaning of this section, providing that several contracts relating to the same matter are to be taken together, and therefore refusal to admit it to be considered in connection with the note and mortgage executed pursuant to the application was proper. Dehnert v. Union Cent. Life Ins. Co., 74 M 104, 239 P 773 (1925).

Special Bond: Where a contractor had obligated himself to construct a watertight basement in a building he had undertaken to erect for plaintiff by a bond separate and distinct from and without reference to the building contract or the plans and specifications furnished by plaintiff's architect, the bond being given about a month after execution of the building contract and a week later than the bond accompanying the latter contract, he was in no position, in an action on such special bond, to defend on the ground that its provisions should be construed with reference to the building contract, and that having followed the plans and specifications, he was relieved from liability thereunder. St. Bank of Darby v. Pew, 59 M 144, 195 P 852 (1921).

Conflicting Documents: Where a note is secured by a mortgage of even date the note and mortgage are parts of the same contract under this section, which must be read and construed together, thus rendering the fulfillment of the entire contract uncertain and the note nonnegotiable. Cornish v. Woolverton, 32 M 456, 81 P 4 (1905).

28-3-204. How repugnancies reconciled.

Case Notes

Total Compensation in Condemnation to Include Value of Condemned Property and Severance Damages: The city of Whitefish condemned 7,234 square feet of plaintiff's property, but conveyed to plaintiff 10,175 square feet of city property contiguous to plaintiff's lot. The conveyance was intended as severance damages to offset the harm of condemnation. The parties entered an agreement that plaintiff would grant possession of the condemned property to the city and that the city would pay plaintiff $130,000 to convey the 10,175 square foot adjacent lot. The agreement also stated that the parties were unable to agree on the value of the condemned property, the severance damages to plaintiff's remaining property, and the value of the conveyed property. Eventually plaintiff filed a complaint for inverse condemnation and breach of the agreement when the parties were unable to agree on the property values and severance damages. The

District Court held that the only issue for the jury was to determine the amount that plaintiff was entitled to for compensation, and the jury was not asked to determine any severance damages owing to plaintiff. The court also disallowed any evidence of the $130,000 payment because that money was considered for severance damages only and could not be considered by the jury in determining plaintiff's compensation for the condemned property. The court further disallowed the city from presenting any evidence regarding the conveyed property because it had not yet been deeded to plaintiff, and absent unity of ownership, the conveyed property could not be considered when determining the fair market value of plaintiff's remaining property after the condemnation. Last, the court determined that plaintiff's "cost-to-cure" damages were noncompensable because plaintiff's access remained the same after condemnation. During trial, various experts presented differing values for the condemned property. The jury ultimately found for plaintiff and held that the city owed $161,000 for the condemned property. The District Court also awarded plaintiff $94,788.23 as litigation expenses. The city appealed, and plaintiff cross-appealed. The Supreme Court held that the District Court misinterpreted the agreement and improperly limited the issues presented to the jury. The court noted that total compensation in an eminent domain case involves both the value of the condemned property and severance damages, including depreciation suffered as a result of condemnation. In order for the jury to consider all circumstances surrounding the condemnation, a new trial was required, so the case was reversed and remanded. K&R Partnership v. Whitefish, 2008 MT 228, 344 M 336, 189 P3d 593 (2008).

Interpretation of Repugnancies in Partnership Dissolution Agreement: Plaintiff claimed that one paragraph of a partnership dissolution agreement conveyed all of the first partner's 50% interest to the second partner, while a later paragraph reconveyed the 50% interest back to the first partner. This interpretation would have rendered both paragraphs meaningless and repugnant. To resolve any repugnancy and give effect to both paragraphs, the District Court properly interpreted the first paragraph as conveying a present interest and the later paragraph as an executory promise to convey a future interest. Bretz v. Ayers, 232 M 132, 756 P2d 1115, 45 St. Rep. 936 (1988).

Amount of Rent — Essential Lease Term Requiring Certainty: Appellants signed a lease with an option to renew the lease. Although the appellants properly gave notice of intent to exercise the option, the renewal provision failed for lack of certainty regarding the amount of the rent because a determination of the amount of the rent upon renewal was based on bids from third parties. In this case, there was no such bid and therefore no means of determining the amount of the rent. The renewal provision of the lease was void for lack of certainty regarding the essential term of rent. Riis v. Day, 188 M 253, 613 P2d 696, 37 St. Rep. 1093 (1980), followed in Nentwig v. United Indus., Inc., 256 M 134, 845 P2d 99, 49 St. Rep. 1172 (1992), and GRB Farm v. Christman Ranch, Inc., 2005 MT 59, 326 M 236, 108 P3d 507 (2005).

General Intent: In a real property contract a provision which could be construed to mean that title insurance was not required until sometime subsequent to final payment was construed to be subordinate to the general intent of the contract and held to be a condition precedent. Brown v. Griffin, 150 M 498, 436 P2d 695 (1968). See also Montana-Dakota Util. v. Lower Yellowstone Rural Elec., 178 M 427, 585 P2d 626 (1978).

Nature of Section: This section is a rule of interpretation rather than of construction. Butte Water Co. v. Butte, 48 M 386, 138 P 195 (1914).

28-3-205. Written or original terms to control printed terms.

Case Notes

"Payable on Death" Designation Negates Joint Tenancy Language on CD Form: The deceased's personal representative was his granddaughter, who was also the person named as the payable on death (POD) beneficiary of the deceased on several certificates of deposit (CDs). The granddaughter obtained a ruling from the District Court that she was a joint tenant with the right of survivorship with respect to the CDs, based upon the language on the CD forms specifically stating that the persons named on the CD were joint tenants. The Supreme Court held that a joint tenancy must be created by specific unambiguous language and that the POD designation on the CDs created an ambiguity negating the joint tenancy language. The Supreme Court further held that the POD language meant that the granddaughter could not have a present interest in the CDs at the time that the CDs were obtained by the deceased and that they could not pass to her under the principles of joint tenancy. The Supreme Court ruled that the POD designation acted to transfer the CDs to the granddaughter outside of the probate estate as

a nontestamentary transfer. In re Estate of Lahren, 268 M 284, 886 P2d 412, 51 St. Rep. 1311 (1994), following In re Estate of Shaw, 259 M 117, 855 P2d 105 (1993).

Indemnity Clause: Printed indemnity clause on back of purchase order was inoperative where typed portion of purchase order merely accepted offer of seller with specific reference to attached modifications and made no mention of indemnity clause. Hoerner Waldorf Corp. v. Bumstead-Woolford Co., 158 M 472, 494 P2d 293 (1972).

Insurance Policy: Stamped phrase "Double Indemnity" appearing on face of insurance policy must be interpreted in light of rider to policy to which phrase refers. Niewoehner v. W. Life Ins. Co., 149 M 57, 422 P2d 644 (1967).

Operation and Effect: Where a contract is partly written and partly printed and the two are inconsistent the former controls the latter. New Home Sewing Mach. Co. v. Songer, 91 M 127, 7 P2d 238 (1931).

Oil and Gas Lease: In an action to enforce the cancellation of an oil and gas lease and to recover damages for refusal to cancel, a written paragraph therein, providing that in the event a well was not commenced within the time limit mentioned in the lease the instrument should be null and void, was controlling as against a printed one under which, if the operations were not commenced within that time the lessor should pay $2 per acre for each additional year commencement of drilling was delayed, and demurrer to the complaint was improperly sustained. Duley v. Torrey, 69 M 599, 223 P 498 (1924).

28-3-206. Uncertainty to be resolved against party causing it.

Compiler's Comments

2013 Amendment: Chapter 31 at end deleted "except that in the case of a contract between a public officer or body, as such, and a private party, it is presumed that all uncertainty was caused by the private party"; and made minor changes in style. Amendment effective October 1, 2013.

Case Notes

General 372
Insurance Contracts 374
Real Property Contracts 377
Construction Adverse to Drafter 378

GENERAL

District Court Incorrectly Determined Plain Language of Subdivision Covenant Unambiguous — Related Documents Constituting Instrument Not Reviewed — Negative Easement — Ambiguity Interpreted Against Drafter Not Dispositive — Disputed Facts Whether County Acted Arbitrarily or Capriciously — Doctrine of Impossibility or Impracticality Not Applicable — Attorney Fees Award Reversed. Lewis & Clark County v. Wirth, 2022 MT 105, 409 Mont. 1, 510 P.3d 1206.

Port Authority Insured Under County Insurance Policy — Extrinsic Evidence Considered — Policy Construed Against Drafter — Insurer Not Immune From Suit as Reinsurer: After a port authority building was destroyed by a fire, the port claimed that it qualified as an insured under a county insurance company policy that included county members and any other county entities that receive insurance through a county joint insurance authority. The insurance company claimed that the language in the policy did not extend to county entities such as the port. Additionally, the insurance company claimed that it was a reinsurer and therefore it was improper for the port to bring a direct claim against it. The Supreme Court held that the port qualified as an insured under terms of the policy and that a direct claim was proper. In reaching a conclusion that was contrary to the language of the policy, the court gave meaning to the entire contract, considered extrinsic evidence, and construed ambiguous language in the policy against the insurer as the drafter. In determining that a direct claim was proper, the court reasoned that the port dealt directly with the insurance company, and therefore the insurer was an excess insurance carrier, rather than a reinsurer. Lincoln County Port Authority v. Allianz Global Risks US Ins. Co., 2013 MT 365, 373 Mont. 60, 315 P.3d 934.

Ambiguous Employment Contract — Question of Parties' Intent Properly Submitted to Jury: West's employment contract contained two different provisions regarding how West would be compensated in the event of termination of employment. The District Court construed the ambiguous clauses against the employer who drafted the contract and submitted the issue to the jury. On appeal by the employer, the Supreme Court examined the contract language and affirmed. The employment agreement was ambiguous on the issue of whether West would be paid trailing commissions or bonuses if West were terminated for cause, so the District Court did not err in ordering that the parties' intent on the issue be submitted to the jury. West v. The Club at Spanish Peaks, LLC, 2008 MT 183, 343 M 434, 186 P3d 1228 (2008), following Eschenbacher v. Anderson, 2001 MT 206, 306 M 321, 34 P3d 87 (2001).

Ambiguity Required Prior to Application of Construction-Against-Drafter Principle: Plaintiffs asserted that because defendants drafted a number of the easements in a utility right-of-way contract, the terms of the contract should be construed most favorably toward plaintiffs. However, plaintiffs admitted that the contract language was unambiguous, and before a contract may be construed against the drafter, some ambiguity must exist. Thus, the trial court did not err by not interpreting the contract language in a light most favorable to plaintiffs. Mary J. Baker Revocable Trust v. Cenex Harvest St., Cooperatives, Inc., 2007 MT 159, 338 M 41, 164 P3d 851 (2007).

No Contractual Definition of Cause — Discretionary Termination of Professional Sports Team Coach Related to Legitimate Business Needs Warranted: Cole was fired as a professional hockey coach because of the team's poor performance. Cole's 5-year employment agreement contained a clause, drafted by Cole, providing that if Cole was terminated without cause, he would receive 1 year's salary and a bonus. Although the contract did not contain a definition of cause, the District Court found that the termination was without cause. The Supreme Court disagreed. Applying de novo review of the District Court's summary judgment to interpret the employment contract terms in their ordinary and popular sense and construing any uncertainty in the contract language against Cole, who drafted it, the Supreme Court held that discharging the coach of a poorly performing professional sports team was a discretionary decision related to the legitimate needs of the business and constituted cause, so the employer had a legitimate business reason to terminate the coach. Thus, Cole was not entitled to recover under the contract. Cole v. Valley Ice Garden, LLC, 2005 MT 115, 327 M 99, 113 P3d 275 (2005).

Dispute Over Contract to Deliver Log Home — No Requirement That Seller Provide Name of Third Party Boom Truck Operator — Rescission Proper Remedy for Material Breach of Contract: Anderson agreed to purchase a log home from Eschenbacher. The home was designed to be constructed on Anderson's homesite. Eschenbacher drafted the purchase contract, which provided that Eschenbacher would act only as a manufacturer, not as a building contractor, and also required Anderson to coordinate and ensure availability of a boom truck to assemble the structure at the site. Anderson contacted a third party to supply a boom truck instead of using Eschenbacher's truck. Eschenbacher then refused to deliver the logs unless Anderson supplied the name of the other boom truck operator. Both parties sued for breach of contract. The District Court concluded that Anderson was under no duty to provide Eschenbacher with the name of the boom truck operator, and the Supreme Court agreed. The contract clearly placed the responsibility for acquiring a boom truck with Anderson, but did not require Eschenbacher to use it, because other language required Anderson to pay any expenses incurred by Eschenbacher for waiting once the logs were delivered, if, for instance, the boom truck that Anderson provided was inadequate. Construing the contract most strongly against the drafter, Eschenbacher, the court found that Eschenbacher could easily have inserted provisions in the contract regarding specifications of an adequate boom truck, but he did not. Eschenbacher materially breached the contract by refusing to deliver the logs until the boom truck dispute was settled. The contract did not specify a remedy; thus, the District Court did not err in granting Anderson rescission of the contract. Eschenbacher v. Anderson, 2001 MT 206, 306 M 321, 34 P3d 87 (2001).

Waiver of Homestead Allowance and Right to Exempt Property by Agreement: An agreement wherein the beneficiaries of a will ambiguously delineated how property was to be divided did not specify that a homestead allowance or exempt property was to go to the decedent's wife. The trial court properly ruled that the wife waived her right to the allowance and property by agreement, despite her contentions that there was no fair disclosure of her rights since she was not aware of the allowance or exempt property. The Supreme Court noted that neither party was aware of the allowance or exempt property and that since the wife was represented by counsel at the time of agreement, the contractual ambiguity should be interpreted against her under 28-3-206. In re Estate of Flasted, 228 M 85, 741 P2d 750, 44 St. Rep. 1362 (1987), distinguished in In re Estate of Thies, 273 M 272, 903 P2d 186, 52 St. Rep. 970 (1995).

Insurance Policy Clause Unambiguous: Home owners' insurance policy clause clearly and unambiguously covered only vehicles that met both requirements set forth in the provision. Therefore, the clause was within the general rule that when a contract is reduced to writing, the intent of the parties is ascertained from the writing alone if possible. Payne v. Safeco Ins. Co., 222 M 198, 720 P2d 1197, 43 St. Rep. 1171 (1986).

Jury Instruction Regarding Ambiguities in Product Labeling and Instructions for Use — Issue of Fact: Herbicide manufacturer contended the District Court erred in instructing the jury that ambiguities in the wording on product labels and in application instructions were to be construed against the manufacturers, claiming that this rule of construction was a rule of law for the court to apply and not a proper subject for a jury instruction. Plaintiff argued that the instruction was justified because the manufacturer presented the meaning of the application instructions as a factual issue at trial. The Supreme Court agreed, concluding that the jury instruction was a correct statement of law under the facts of the case. Vandalia Ranch, Inc. v. Farmers Union Oil & Supply Co., 221 M 253, 718 P2d 647, 43 St. Rep. 790 (1986).

Issue of Authorship of Agreement Not Precluding Summary Judgment Where Agreement Not Ambiguous: Where the plaintiffs brought an action for default of a mining lease, arguing that summary judgment for the defendants was precluded by the ambiguity of the lease and a dispute as to its authorship, the Supreme Court held that the provisions governing royalty payments were not ambiguous, that authorship was therefore irrelevant, and that summary judgment was properly granted. The plaintiffs' interpretation of the agreement was absurd because that interpretation required payment of royalties before net smelter returns were received or before the royalties themselves could be calculated. The time and method of calculation of payment by the defendants were entirely consistent with the terms of the parties' agreement. Reading the agreement as a whole, there was no factual issue to preclude summary judgment. Lewis v. St., 199 M 368, 675 P2d 107, 41 St. Rep. 9 (1984).

Interpretation of Employment Contract — No Error of Law: Claiming that ambiguities in his employment contract were interpreted incorrectly, an employee appealed the District Court's affirmance of a decision of the Labor Standards Division. Even when the contract was interpreted most strongly against the employer, the District Court order was neither clearly erroneous nor based on an error of law. Landon v. Labor Standards Div., 200 M 153, 649 P2d 1341, 39 St. Rep. 1641 (1982), followed in Travelers Ins. Co. v. Holiday Village Shopping Center Ltd. Partnership, 280 M 217, 931 P2d 1292, 53 St. Rep. 1372 (1996).

Personal Guardianship and Property Conservatorship No Bar to Trust Revocation — Construction Against Party Supplying Trust Form: A trustee appealed from a declaratory ruling of the District Court holding that a personal guardianship and a property conservatorship did not prevent the trustor from revoking the trust. The trustee, also a beneficiary, argued in effect that the trustor had been legally incapacitated from revoking the trust because she was under a personal guardianship and her property was under a conservatorship and because the trust provided that it was irrevocable upon the "incompetency" of the trustor. However, the conservatorship and guardianship did not begin before revocation of the trust. Further, a conservatorship would not affect the power to revoke under 72-5-421. The guardianship had been appointed because the trustor had become physically incapable of caring for herself, not because of mental incapacitation. Construing the term "incompetency" strictly against the trustee because it had supplied the trust form and was a beneficiary, the Supreme Court upheld the trial court's holding that the trust revocation was valid. Mont. Conference Seventh-Day Adventist Church v. Estate of Miller, 192 M 468, 628 P2d 1100, 38 St. Rep. 846 (1981), followed in In re Estate of West, 269 M 83, 887 P2d 222, 51 St. Rep. 1409 (1994).

Letter of Credit: Ambiguous letter of credit issued by bank mentioning two different amounts and stating that the bank was guaranteeing "these funds" should be interpreted most strongly against the bank. Miller v. Walter, 165 M 221, 527 P2d 240 (1974).

Acceptance of Agreement: Defendants' demurrer was properly sustained in action on a written contract where complaint did not allege a written acceptance by the plaintiff and the agreement was to be effective only when it was accepted and when defendants were notified by letter of plaintiff's acceptance. Union Interchange, Inc. v. Allen, 140 M 227, 370 P2d 492 (1962).

Contractors' Bonds: Where defendant furnished contractors with surety bond providing that contractors would faithfully perform contract with Montana State Highway Commission (now Transportation Commission) for roadwork, and contract required contractors to carry public liability insurance to indemnify public for injuries sustained by reason of work on highway, defendant was liable for satisfaction of judgments, notwithstanding exclusion clause under which use of automobiles was excluded from coverage of policy. Doheny v. USF&G Co., 34 F. Supp. 888 (D.C. Mont. 1940), affirmed in USF&G Co. v. Doheny, 123 F2d 746 (9th Cir. 1941).

INSURANCE CONTRACTS

Contradicting Clauses in Separate Contracts Construed Against Drafter — Employee Waiver — Health Insurance: The plaintiff health insurance company filed a breach of contract action against the defendant, an employer providing health insurance for its employees. The contracts between the parties required the defendant to cover 75% or more of its employees; however, a subsequent contract allowed the defendant's employees to waive coverage. The District Court granted summary judgment in favor of the defendant, finding that the two provisions in the contracts were ambiguous and the contract should be interpreted against the drafter. On appeal, the Supreme Court affirmed, holding that the contracts must be interpreted as part of the same transaction and that giving effect to both contract provisions is not reasonably practical, that the ambiguity is construed against the drafter, that the newer specific contract controlled over the older general contract, and that the waiver provision was meant to modify the minimum employee participation provision. Mont. Health Network, Inc. v. Great Falls Orthopedic Associates, 2015 MT 186, 379 Mont 513, 353 P.3d 483.

Reformation of Insurance Policy Not Permitted — Clear and Explicit Language Used — Lack of Due Diligence in Discovering Error Not Justifying Reformation: An insurer attempted to reform an insurance policy on the ground that the policy should not cover property near a structure that was specifically exempted from the policy. However, the policy specifically included property within 1,000 feet of other insured property, including property around the exempted structure. The District Court applied 33-15-302 and determined that it was prohibited from reforming insurance policies. On appeal, the Supreme Court also declined to reform the contract, as the language was clear and explicit, due diligence would have uncovered the error, and the insurer failed to establish that its insurance policy expressed something other than what the parties mutually intended. Lincoln County Port Authority v. Allianz Global Risks US Ins. Co., 2013 MT 365, 373 Mont. 60, 315 P.3d 934.

Failure to Provide Workers' Compensation Insurance — Ambiguity of Insurance Contract Not at Issue: An employee leasing company failed to provide workers' compensation insurance for its client companies. The employee leasing company argued that the Workers' Compensation Court failed to apply Montana law regarding the interpretation of insurance contracts by strictly construing any ambiguity in the insurance contract in favor of the insured and against the insurer. The Supreme Court did not disagree that this is a correct statement of insurance law; however, that contract principle did not apply here because there was no question of ambiguity regarding the insurance contracts in this case. Rather, the applicable contract principle here was that for coverage by an insurance policy to apply, there must be a named insured. The employee leasing company was not an insured under the contracts; therefore, the Workers' Compensation Court did not incorrectly apply insurance law. Total Mechanical Heating & Air Conditioning v. Employment Relations Div., 2002 MT 55, 309 M 84, 50 P3d 108 (2002).

Parked Trailers Unattached to Insured Tractors — No Coverage Under Unambiguous Policy Provisions: The District Court found an insurance policy to be ambiguous regarding coverage for trailers that had been used to haul beer but that were parked and used for storage at the time they were accidentally run into and granted summary judgment for insurer based on that ambiguity. The Supreme Court found no ambiguity in policy language that clearly covered only trailers that were attached to an insured tractor. Citing its authority in Hereford v. Hereford, 183 M 104, 598 P2d 600 (1979), the Supreme Court reversed and granted summary judgment to the nonmoving party based on the fact that the unambiguous policy language created no genuine issue of material fact. Canal Ins. Co. v. Bunday, 249 M 100, 813 P2d 974, 48 St. Rep. 597 (1991).

Ambiguous Insurance Policy Provision — Summary Judgment Reversed: An insurance policy that did not clearly state whether it provided uninsured motor vehicle coverage when the driver was insured but the ownership of the vehicle was not was held to be ambiguous; therefore, under the rationale that an ambiguous provision is construed against the insurance company, the policy was interpreted to provide coverage. The District Court grant of summary judgment holding that the policy did not provide uninsured motor vehicle coverage was reversed. St. Farm Mut. Auto. Ins. Co. v. Taylor, 223 M 215, 725 P2d 821, 43 St. Rep. 1667 (1986).

Conflict Between Contract and Certificate of Insurance: Decedent's employer provided him with group life insurance and paid the total premium. Employer kept the master policy, which stated that the benefit paid would be 300% of annual salary at the time of death, rounded to the nearest dollar. A certificate of insurance not containing this formula was issued to decedent and stated that his benefit would be $104,000. Employer paid premiums based on that amount. Decedent was not shown to have read the master policy. The certificate was issued pursuant to a statute requiring it. Decedent's salary upon his death was $14,700, and based on the policy formula, the correct benefit was $44,000. Insurer sent employer a corrected certificate showing the proper benefit 19 days before decedent died, but the certificate was not given to decedent or his wife until after his death, and neither was informed of the error and correction before death occurred. The master policy stated that the policy controlled in event of discrepancy between it and the certificate. On appeal from judgment that wife was entitled to a $104,000 benefit, the

Supreme Court ruled that: (1) the certificate was part of the contract, and in view of the conflict the construction most favorable to the insured would be adopted and the policy provision that the policy governed would be disregarded; (2) insured contracted only indirectly, through his employer, with insurer and his certificate of insurance was his primary source of information regarding the policy and thus he was entitled to rely on the certificate to correctly state the coverage; (3) if the coverage stated on the certificate is incorrect, insured and beneficiaries are deprived of the chance to supplement coverage if they find it inadequate; (4) the amount of decedent's coverage was the essence of the policy; (5) insurer was the drafter of the policy and certificate and must bear the burden of the ambiguity it created; and (6) equity did not require reformation of the contract to correct the error as the certificate was a year old and due diligence would have resulted in discovery of the error before death. Martin v. Crown Life Ins. Co., 202 M 461, 658 P2d 1099, 40 St. Rep. 216 (1983).

Construction of Automobile Insurance Contract: In construction of an automobile insurance contract an ambiguity regarding nonowned vehicles was construed in favor of the insured. Thus partial summary judgment for the insured was proper. Fitzgerald v. Aetna Ins. Co., 176 M 186, 577 P2d 370 (1978).

Ambiguous Theft Insurance Policy: Summary judgment on a claim for loss by theft of a commercial carpet cleaner was improperly granted defendant insurer when the policy of insurance was ambiguous as to exclusions from coverage. The particular exclusionary clause was subordinate to the general intent of the contract. Alpha Real Estate Dev., Inc. v. Aetna Life & Cas. Co., 174 M 301, 570 P2d 585 (1977).

Insurance Policies Generally: Where dealer's trucks were insured for "actual cash value", this term was ambiguous and when properly construed in sense most favorable to insured it was not error to permit dealer to recover the retail market value of the destroyed property rather than the wholesale market value. Johnson v. Equitable Fire & Marine Ins. Co., 142 M 128, 381 P2d 778 (1963).

Fair and Reasonable Construction: Even though an insurance contract is to be construed liberally in favor of the insured and strictly against the insurer, contracts of insurance should be given a fair and reasonable construction. James v. Prudential Ins. Co. of Am., 131 M 473, 312 P2d 125 (1957).

Construction Against Insurer: In interpreting policies of insurance the courts shall resolve uncertainties and ambiguities in the policy against the insurer since it is responsible for the form of the contract. Johnson v. Cont. Cas. Co., 127 M 281, 263 P2d 551 (1953).

Ambiguities in Contract Resolvable Against Mutual Death Benefit Associations: The rule prevailing in litigation concerning insurance policies that any ambiguity in the policy shall be resolved against the insurer since the latter is responsible for the form of the contract under this section is applicable to contracts between mutual death benefit societies and their members. McDonald v. N. Benefit Ass'n, 113 M 595, 131 P2d 479 (1942).

Health and Accident Insurance: If there is any ambiguity in an insurance policy, in the instant case a health and accident policy, the policy form of which was provided by the insurance company, it must under this section be resolved against it; the word "period" was held to mean continuous during the indemnity period of loss of time, and not a period of 1 month where an exclusion clause limited indemnity to any period during which insured was under the regular professional attendance of a physician. Scinski v. Great N. Life Ins. Co., 110 M 106, 99 P2d 218 (1940).

Fire Insurance Contract: A contract of fire insurance must be construed as any other contract. The policy must specify the parties between whom the contract is made and the interest of the insured in the property insured if he is not the absolute owner. This information must be supplied to the insurance company by the applicant for the policy. Stevens v. Steck, 101 M 569, 55 P2d 7 (1936).

Insurance Covering U.S. and Canada: Since insurance companies prepare their own contracts and the insured has no voice in their drawing any ambiguity or uncertainty in them must be construed in favor of the insured. Where an automobile was insured against fire, theft, and collision in the United States and Canada, and another company insured it, by a separate instrument attached to the policy, against confiscation "by municipal, federal, or state authorities" without limiting its liability to confiscation within the limits of the United States, and the car was confiscated in Canada, by construing the two instruments together, the latter company was liable for the loss sustained and its contention that the terms "municipal", "federal", and "state" had no application to the Canadian government was without merit. Mont. Auto Fin. Corp. v. British Fed. Fire Underwriters, 72 M 69, 232 P 198, 36 ALR 1495 (1924).

Application — Representations Not Warranties: Under this section, answers to questions in an application for life insurance as to the prior health of the applicant were representations and not warranties. Pelican v. Mut. Life Ins. Co. of New York, 44 M 277, 119 P 778 (1911). See Mut. Life Ins. Co. of New York v. Hilton-Green, 211 F 31 (9th Cir. 1914), followed in McDonald v. N. Benefit Ass'n, 113 M 595, 131 P2d 479 (1942).

REAL PROPERTY CONTRACTS

Sale of Lot Presumptively Including Access: It is a presumption, albeit disputable, that the complete use and enjoyment of a parcel of land includes access to that parcel. To overcome the presumption, the seller must offer evidence or some legal basis that would controvert the buyer's reliance on the presumption. Here, the Kester's sold the Erkers a house in Big Sky for approximately $310,000. The Kesters' attorney later discovered through the title company that a portion of the driveway, which provided sole access to the house, had not been conveyed by the deed to the lot and requested additional money for the deed to the driveway. There was no indication at the time of sale that any parcel was separate and distinct from the lot, nor did the Kesters reveal any intention to reserve the driveway from the purchase of the lot. Although the Erkers were charged with constructive notice of the contents of properly recorded instruments describing prior conveyances of the property, under Montana subdivision laws, the driveway was not an individual parcel of land at the time of purchase, so the Erkers could be charged only with knowledge that the purchase of the lot described in the common metes and bounds description included the driveway. Absent evidence to the contrary, the Erkers were entitled to the presumption that purchase of the lot included access to it and to summary judgment as a matter of law. Erker v. Kester, 1999 MT 231, 296 M 123, 988 P2d 1221, 56 St. Rep. 912 (1999), following Yellowstone Valley Co. v. Assoc. Mtg. Investors, Inc., 88 M 73, 290 P 255, 70 ALR 1002 (1930).

Contract Construed as Right of First Refusal and Not Option Contract — Ambiguity Resolved Against Lessee Drafters of Agreement: Lessor signed two documents giving the lessees certain rights in lessor's 800-acre ranch. The first document, granting a "first option" to purchase, required other offers to be in writing and gave the lessees 45 days from the day of notification of intent to sell to make payment. The Supreme Court held that this document created a right of first refusal. The second document granted a "first option to purchase [my] property . . . upon or before my passing . . ." and also granted 45 days for payment "[u]pon notification of intent to sell". The Supreme Court found that while some of the language in the second document was consistent with a true option, the insertion of the last sentence granting 45 days for payment upon notification of intent to sell indicated a right of first refusal. Because the lessees had drafted the second document, the Supreme Court construed the ambiguity against the lessees and held that the document created a right of first refusal and not an option contract. Because notice of intent to sell had never been given by lessor's estate, the right of first refusal did not come into effect. Lee v. Shaw, 251 M 118, 822 P2d 1061, 48 St. Rep. 1110 (1991). See also a subsequent appeal addressing waiver of the right of first refusal in In re Estate of Pelzman, 261 M 461, 863 P2d 1019, 50 St. Rep. 1408 (1993).

Subjective Standard Applicable to Term "Satisfactory": A real estate listing contract contained the following clause, typed in by the realtor: "This listing is subject to Fultz being able to satisfactory [sic] trade the above lands for lands in Big Horn Co. on a tax free exchange." The realtor argued that an objective standard for a satisfactory trade should be used. The District Court found that because the realtor drafted the contract, any ambiguities should be construed against him. The term "satisfactory" was found to be a subjective standard rather than a reasonable man standard. Because the trade arrangement set up by the realtor did not meet the requirement of a tax-free exchange, the arrangement was properly found to be unsatisfactory under the contract terms. Watson v. Fultz, 239 M 364, 782 P2d 361, 46 St. Rep. 1751 (1989).

Obligation to Veracity of Warrant by Party Drafting It: Real estate was conveyed to plaintiff by "special warranty deed", drafted by defendant, which warrant defendant claimed limited liability to defendant's own acts. It was argued that because defendant did not cause latent defects, liability did not attach. However, by warranting the house, defendant contractually obligated itself to the veracity of the warrant. Because plaintiff relied on defendant's misrepresentations to her detriment, defendant was held liable for the latent defects. Wagner v. Cutler, 232 M 332, 757 P2d 779, 45 St. Rep. 1092 (1988).

Lack of Ambiguity — Rule Inapplicable to Commission Contract: Where the plaintiff and defendant made a commission contract upon which the plaintiff brought an action to collect a commission for the sale of real property, the Supreme Court held that inasmuch as the District

Court properly found no ambiguity in the contract, the rule requiring the construction of the contract against its drafter was inapplicable, as under the rationale of Parkhill v. Fuselier, 194 M 415, 632 P2d 1132, 38 St. Rep. 1424 (1981), the drafter must cause an uncertainty. Martin v. Community Gas & Oil Co., 205 M 394, 668 P2d 243, 40 St. Rep. 1385 (1983).

Specific Performance — Failure to Tender Purchase Price — Excuse: Plaintiff and defendants entered into a buy-sell agreement for a parcel of land. The agreement was prepared by defendants' real estate agent. The agreement failed to note a 60-foot roadway and utility easement. Defendants in the meantime sold an adjoining parcel of land, including an interest in the 60-foot easement. Plaintiff sued for specific performance of the buy-sell agreement. Plaintiff was excused from tendering the purchase price because defendants by selling the adjoining parcel subject to the easement indicated their refusal and inability to perform the agreement. Plaintiff is entitled to specific performance of that part of the agreement defendants are now able to convey, notwithstanding that it is the very same title plaintiff refused to accept in the first instance. Chadwick v. Giberson, 190 M 88, 618 P2d 1213, 37 St. Rep. 1723 (1980).

Grazing Permit: A real property sale included some grazing land owned by the United States on which sellers held grazing permits. The contract was ambiguous as to whether sellers were required to transfer the permit or merely execute a waiver on a forest service form. The ambiguity was construed against the promisor. Dooling v. Bright-Holland Co., 152 M 267, 448 P2d 749 (1969).

Option in Lease: Agricultural tenant was not entitled to exercise option to buy contained in lease of land after expiration of lease, even though holding over, in light of statute providing that uncertainties in contract be interpreted against plaintiff-promisor, causing uncertainty to exist. Miller v. Meredith, 149 M 125, 423 P2d 595 (1967).

Sale Agreement: If any uncertainty exists in the sale agreement and the deeds, it must be construed most strongly against the person causing the uncertainty. This was true in the case of a realtor, who in turn was vendor's agent. Voyta v. Clonts, 134 M 156, 328 P2d 655 (1958).

Lease — Improvements by Lessee: Where there is an uncertainty in a contract it is to be interpreted most strongly against the person who caused the uncertainty to exist. Thus where there was a question as to what were intended to be improvements as contemplated by the $1200 rent provisions of the lease and both the lessor and the lessee gave testimony, it was error for the court to disregard such testimony. Consideration of the improvements made by the lessee should be given by the lower court and the value of these items offset against the rents contemplated. Hempstead v. Allen, 126 M 578, 255 P2d 342 (1953).

CONSTRUCTION ADVERSE TO DRAFTER

Requirement to Pay Additional Tax Liability in Prepayment Clause Ambiguous — Ambiguity to Be Construed Most Strongly Against Drafter: In a real estate contract, the prepayment clause included a requirement that the buyer had to pay for additional taxes incurred by the sellers as a result of the prepayment. The District Court determined that the language in the prepayment clause was ambiguous as to whether the buyer owed the tax liability in the year the prepayment occurred or over the entire term of the contract, and the court looked to extrinsic evidence to determine that the parties' intent was to include the tax liability for the year the prepayment was made. On appeal, the Supreme Court overruled the District Court, noting that the ambiguous language had been drafted entirely by the sellers, therefore requiring the ambiguous language to be construed most strongly against them as the drafter. The case was remanded to the District Court to recalculate the sellers' damages based on total additional tax liability as calculated over the term of the contract. First Nat'l Properties, LLC v. Hillstead Trust, 2020 MT 211, 401 Mont. 59, 472 P.3d 134.

Ambiguity in Plea Agreement in Defendant's Favor — Improper Denial of Motion to Withdraw Plea: The defendant entered into a plea agreement that expressly referenced 46-12-211(1)(b), which allows a defendant to withdraw the plea if the court rejects the plea agreement. However, the agreement also incorporated other statutory language that does not allow withdrawal of a plea. The District Court denied the motion to withdraw the plea agreement and sentenced the defendant. On appeal, the defendant claimed that his sentence was illegal because he should have been allowed to withdraw his plea given that the agreement expressly referenced law that would permit him to do so. The state argued that the plea agreement was ambiguous because the express language of the agreement conflicted with the citation to 46-12-211(1)(b) and that, under 28-3-206, the ambiguity should be construed against the defendant because defense counsel had drafted the agreement. The Supreme Court rejected the state's argument and, in a matter of first impression and relying on federal case law, held that an ambiguity in a plea agreement should be construed in favor of the defendant. Accordingly, the Supreme Court reversed and remanded with instructions to conduct another sentencing hearing. St. v. Langley, 2016 MT 67, 383 Mont. 39, 369 P.3d 1005.

Ambiguous Decline of Comparable Position Exclusion in Retirement Plan Construed Against Employer — Control Determinative of Independent Contractor Status: Eldredge brought suit against ASARCO for failure to pay him a retirement benefit; the company claimed no benefit was due because Eldgidge had earlier declined a comparable position. The Supreme Court found that the retirement plan stated no timeframe within which the decline of a comparable position would exclude an employee from a retirement benefit and, construing the plan against the company as the drafter of the plan, refused to apply the limitation to the much earlier offer to Eldredge. The court also found that despite ASARCO's attempt to paint Eldredge as an independent contractor, Eldredge was an employee and for that reason, all of his time working for ASARCO counted toward his years of employment for the purposes of the company's retirement plan. Eldredge v. ASARCO, Inc., 2011 MT 80, 360 Mont. 112, 252 P.3d 182.

Contract to Arbitrate Not Formed by Employee Handbook and Employee's Acknowledgment — Ambiguous Arbitration Provisions: When Hubner began working for defendant communications company, she signed an acknowledgment in an employee handbook that contained an arbitration provision. The arbitration clause provided that all controversies would be subject to binding arbitration, but the clauses in the handbook specified that the handbook did not constitute a contract of employment or create any relationship other than an employment-at-will relationship. When Hubner's employment was subsequently terminated, she brought a state claim for wrongful discharge, and defendant moved for a summary disposition compelling arbitration pursuant to 27-5-115. The District Court agreed with Hubner that there was no agreement to arbitrate and denied the motion, so defendant appealed. Defendant argued that because the arbitration clause was separable, it could be independently enforced. A state contract law defense that goes to the entire contract rather than specifically to an arbitration clause does not defeat a motion to compel arbitration; however, when a defense is aimed directly at the arbitration provision rather than the entire contract, state law contract defenses may be applied to hold that no enforceable agreement to arbitrate was made. Further, acceptance or consent by the party against whom a contract is sought to be enforced is required before a contract is enforceable. The language in the handbook was ambiguous and construed against the drafter. The ambiguity prevented Hubner from knowing and accepting that she was agreeing to binding arbitration by signing the handbook. Thus, no contract to arbitrate was formed by virtue of the handbook and Hubner's acknowledgment, even when the arbitration provision was considered separately from the rest of the handbook. The District Court was affirmed. Hubner v. Cutthroat Communications, Inc., 2003 MT 333, 318 M 421, 80 P3d 1256 (2003).

Arbitration Clauses Subject to Principles of Contract Interpretation: The Supreme Court affirmed the lower court's holding that the defendant, by not stating what law would govern the arbitration clause, had created an ambiguity subject to the general rules of contract interpretation and that the ambiguity would be construed strictly against the defendant. Mueske v. Piper, Jaffray & Hopwood, Inc., 260 M 207, 859 P2d 444, 50 St. Rep. 1009 (1993), followed in Topco, Inc. v. St., 275 M 352, 912 P2d 805, 53 St. Rep. 175 (1996).

Ambiguity — Conformity to General Principles: Kevin Cumiskey leased a restaurant from Elizabeth Bradley. The lease provided that Cumiskey could make improvements and alterations to the premises that were to remain Cumiskey's property. Fixtures were also to be Cumiskey's. Cumiskey was to insure Bradley's interest, which he failed to do. The restaurant was severely damaged through suspected arson. The insurer brought a declaratory judgment action, and Bradley counterclaimed for damages or loss on the basis of the failure to insure. Damages were an issue at trial, but the trial court granted summary judgment for Bradley on the issue of liability. The Supreme Court, on appeal, held that the District Court had properly found the terms on fixtures and improvements in the lease ambiguous and used an appropriate rule of construction to interpret these clauses. The lease was prepared by an attorney for Cumiskey. Cumiskey testified he intended to use the lease to coerce Bradley into selling him the property. The court properly construed the ambiguity against Cumiskey, the person causing it, and found that the specific provision controlled the general provision and that such interpretation was in conformance with general landlord and tenant law in Montana. St. Paul Fire & Marine Ins. Co. v. Cumiskey, 204 M 350, 665 P2d 223, 40 St. Rep. 891 (1983), followed in Wyman v. DuBray Land Realty, 231 M 294, 752 P2d 196, 45 St. Rep. 621 (1988), and Nimmick v. St. Farm Mut. Auto. Ins. Co., 270 M 315, 891 P2d 1154, 52 St. Rep. 208 (1995). See also Frates v. Edward D. Jones & Co., 233 M 377, 760 P2d 748, 45 St. Rep. 1567 (1988).

Exception for Jointly Drawn Document:
Shortly after entering into a land purchase agreement, the parties changed the agreement into a tax-free land exchange agreement. The new agreement gave buyer 3½ years to acquire like-kind property to be exchanged for seller's ranch. The like-kind property was to be purchased with funds placed periodically by buyer in an escrow account. Several years later a dispute arose concerning the nature and timing of the payments. Buyer submitted the questions to the District Court in a declaratory judgment action. The District Court interpreted the contract in a manner generally favorable to seller, and buyer appealed, claiming that the District Court's decision was unreasonable, contrary to the parties' intentions, and improper under the rules of construction of contracts. The Supreme Court affirmed, ruling that the District Court's interpretation had not been unreasonable since: (1) its decision on the timing of the rental payments was reflective of the parties' intentions as shown by their past performance; (2) its decision on the timing of the amortization payments was consistent with the rule of construction requiring that a contract be construed in such a way as to give effect to all of its provisions; and (3) its decision on the intention of the parties was supported by the evidence. Finally, this section did not entitle buyer to have ambiguities construed in his favor; even though buyer claimed that the nature of the agreement was changed solely for seller's benefit, the agreement was prepared by an attorney for both parties, not by one party alone. Lewis v. Murphy, 199 M 368, 649 P2d 740, 39 St. Rep. 1459 (1982).

The general rule is that a contract containing ambiguous language is construed most strongly against the party causing it. The general rule does not apply where both parties jointly draw up the terms and a transcription of the agreement prepared by only one of the parties is reviewed by the other party to confirm that it corresponds to their agreement since any ambiguity is jointly created. Rumph v. Dale Edwards, Inc., 183 M 359, 600 P2d 163 (1979).

Resolution of Uncertainty: Any uncertainty in a contract must be resolved against the person drafting it. Shanahan v. Universal Tavern Corp., 179 M 36, 585 P2d 1314 (1978).

Ambiguity in Partnership Dissolution Agreement: Since appellant drafted a partnership dissolution agreement that was held ambiguous the terms were construed most strongly against him. Lauterjung v. Johnson, 175 M 74, 572 P2d 511 (1977).

Party Drafting Agreement: If the provisions of contracts (promissory note and mortgage securing it) prepared by plaintiff in a foreclosure suit are uncertain, they must be most strongly construed against him under this section, he having caused the uncertainty to exist. U.S. Bldg. & Loan Ass'n v. Gardiner, 87 M 586, 289 P 555 (1930).

Burden of Proof: The language of an undertaking on appeal must be interpreted most strongly against the sureties, and upon them rests the burden of explaining or removing whatever uncertainty exists therein. Kasun v. Todevich, 71 M 315, 229 P 714 (1924).

Employment Contract: Where defendant, in offering employment to plaintiff by letter and subsequently in employing him, stated orally that he would give him work "the year round" at a compensation of $75 a month, the burden of removing any uncertainty as to the meaning of the term "the year round" was upon defendant as the party who by its use caused the uncertainty to exist, and his failure to do so warranted the jury in finding that the employment was to be from the beginning to the end of the contract year. Weir v. Ryan, 68 M 336, 218 P 947 (1923).

Teacher Contract: When a school board had provided in its rules that in case a teacher resigns or is dismissed before the end of the school year her compensation shall be "for only the actual time in service", the language being that of the board, any uncertainty in it must be construed most strongly against the board in a controversy with it by a teacher on a claim for compensation. Finley v. School District, 51 M 411, 153 P 1010 (1915), distinguished in State ex rel. Priestly v. Croff, 95 M 498, 27 P2d 540 (1933).

Attorney as Drafter: Where after applying the ordinary rules of construction any uncertainty remains in the terms and expressions employed in a contract, they must be construed most strongly against the party who drew it up—in this instance an attorney at law. Lyon v. Dailey Copper Min. & Smelting Co., 46 M 108, 126 P 931 (1912).

Evidence to Support: Where the evidence tends to prove that the promisee wrote the agreement and selected the terms thereof, the presumption under this section gives way to the contrary one that the latter caused the uncertainty and the burden rests on him to remove it. Blankenship v. Decker, 34 M 292, 85 P 1035 (1906).

Part 3
Intention of the Parties

Part Case Notes

Complaint Failed to Allege Bodily Injury — Self-Serving Affidavits in Response to Motion for Summary Judgment Insufficient Evidence of Physical Manifestations of Injury to Trigger Coverage Under Bodily Injury Clause. Farmers Ins. Exch. v. Minemyer, 2023 MT 138, 413 Mont. 60, 532 P.3d 837.

No Duty to Defend Under Property Damage Clause — "Property Damage" Defined as Loss of Use of Tangible Property Not Physically Injured — Allegation of Economic Loss Does Not Constitute Loss of Use. Farmers Ins. Exch. v. Minemyer, 2023 MT 138, 413 Mont. 60, 532 P.3d 837.

Misrepresentation Based on Mistake — Coverage Not Excluded Under Policy: The plaintiff sued the defendant, the insurer of the homeowner from whom she purchased a home. After closing on the home, the plaintiff had found the basement of the home flooded and later learned the homeowner had not disclosed that the basement had previously flooded. The defendant denied coverage to the previous homeowner, claiming that the homeowner had intentionally misled the plaintiff and that intentional misrepresentations were not covered by either the homeowner's home policy or rental policy. The District Court agreed and granted the defendant summary judgment. On appeal, the Supreme Court agreed that the home policy expressly excluded coverage; however, it reversed and remanded the case to the District Court based on its conclusion that the renter's policy did provide coverage because the homeowner had stated that his misrepresentation to the plaintiff was based on mistake. Huckins v. United Serv. Auto Ass'n, 2017 MT 143, 387 Mont. 514, 396 P.3d 121.

Ambiguous Decline of Comparable Position Exclusion in Retirement Plan Construed Against Employer — Control Determinative of Independent Contractor Status: Eldredge brought suit against ASARCO for failure to pay him a retirement benefit; the company claimed no benefit was due because Eldgidge had earlier declined a comparable position. The Supreme Court found that the retirement plan stated no timeframe within which the decline of a comparable position would exclude an employee from a retirement benefit and, construing the plan against the company as the drafter of the plan, refused to apply the limitation to the much earlier offer to Eldredge. The court also found that despite ASARCO's attempt to paint Eldredge as an independent contractor, Eldredge was an employee and for that reason, all of his time working for ASARCO counted toward his years of employment for the purposes of the company's retirement plan. Eldredge v. ASARCO, Inc., 2011 MT 80, 360 Mont. 112, 252 P.3d 182.

No Duty to Defend Property Damage or Fraud Claim When No Property Damage or Fraud Asserted: Defendant contended that plaintiff insurer had a duty to defend and provide coverage under defendant's commercial general liability policy, which provided coverage for property damages. However, the claim did not seek compensation for property damages for physical injury to tangible property, but rather for sums fraudulently paid to defendant based on a breach of contract. Because allegations in the complaint did not set forth facts that brought the event within the policy provisions and specifically excluded coverage for a fraud claim, the insurer had no duty to defend the claim. Generali-U.S. Branch v. Alexander, 2004 MT 81, 320 M 450, 87 P3d 1000 (2004), following Graber v. St. Farm Fire & Cas. Co., 244 M 265, 797 P2d 214 (1990). See also Farmers Ins. Exch. v. Minemyer, 2023 MT 138, 413 Mont. 60, 532 P.3d 837, holding that claims for purely economic loss do not create a duty to defend against property damage when no direct physical injury occurred.

Real Estate Listing — Vagueness to Be Raised at Trial Level: Plaintiff and defendant entered into a real estate listing agreement. Defendant was a cotenant with her husband. Defendant contended that the listing contained an erroneous asking price, did not adequately describe the property, and was signed only by the defendant. Defendant contended the contract should be declared void due to vagueness. Defendant participated in the contract throughout its entire existence without any objection of vagueness and did not raise the issue at trial. The surrounding circumstances and positions of the parties clearly indicate their intent to enter into and perform an agreement. When reviewing a conflict in testimony regarding ambiguity, the trier of fact is entitled to determine the meaning of the contract in its own right. The reviewing court looks only to determine whether there is substantial credible evidence supporting the verdict. The vagueness issue was not raised in the District Court, thus it could not be considered on appeal. Barrett v. Ballard, 191 M 39, 622 P2d 180, 37 St. Rep. 2038 (1980).

Interpretation of Contract — Time of Performance: On appeal, the seller of a log cabin urged that the agreement required the buyer to remove the logs from the seller's property as soon as possible. The Supreme Court found that the negotiations were quick and informal and that nothing specific was said about the time in which the cabin was to be removed. Noting the seller's testimony that he was in the process of refurbishing his motel and wanted the cabin removed as soon as possible so that he could take advantage of the good building weather to expand the motel and that the cabin was old and had not been used for years and contributed nothing to the value or appearance of the property and little value to the motel, the Supreme Court held that there was substantial evidence to support the trial court's finding that a condition of the sale was that the logs were to be removed as soon as possible. Jeffery v. Neville, 190 M 300, 620 P2d 1218, 37 St. Rep. 1983 (1980).

Contract for Sale of Timber After Severance Not Interest in Real Property — No Breach for Sale of Land to Third Party: A contract under which appellant had a right of first refusal to purchase timber if and when appellee decided to sell timber did not convey an interest in real property and was not breached by appellee's sale of the land to third party without notice to the appellant. Yellowstone Pine Co. v. Big Sky of Mont., 185 M 176, 605 P2d 172 (1980).

28-3-301. Interpretation to give effect to mutual intention.

Case Notes

General 382
Insurance Contracts 391
Real Estate Contracts 396

GENERAL

Surrogacy Contract — Express Written Contract Limited to Clear and Unambiguous Terms — Contract Did Not Preclude Subsequent Establishment of Parental Interest Under Montana Law Not Based on Fact of Surrogacy. Sayler v. Yan Sun, 2023 MT 175, 413 Mont. 303, 536 P.3d 399.

District Court Incorrectly Determined Plain Language of Subdivision Covenant Unambiguous — Related Documents Constituting Instrument Not Reviewed — Negative Easement — Ambiguity Interpreted Against Drafter Not Dispositive — Disputed Facts Whether County Acted Arbitrarily or Capriciously — Doctrine of Impossibility or Impracticality Not Applicable — Attorney Fees Award Reversed. Lewis & Clark County v. Wirth, 2022 MT 105, 409 Mont. 1, 510 P.3d 1206.

No Breach by Defendant When Lawsuit Commenced — Still Sufficient Time to Remedy Issue but for Plaintiff's Interference: The District Court did not err in concluding that when a lawsuit commenced, the defendant had not breached the parties' agreement concerning a pivot irrigation system. It was undisputed that, at the time the parties entered into an agreement concerning the pivot irrigation system, it was the intention of the parties to provide the plaintiff with green fields on which to hunt. The record reflected that the plaintiffs sole purpose in acquiring land from the defendant in the first place was to enjoy the hunting that he thought the area could be manicured to offer. The Supreme Court upheld the District Court's finding that the defendant had not breached the parties' agreement as of the time that the plaintiff directed that a contractor not undertake any more work on the pivots, because there was still sufficient time for the defendant to repair the pivot irrigation system and cultivate green fields for hunting prior to the start of hunting season but for the plaintiffs interference. Welu v. Twin Hearts Smiling Horses, Inc., 2016 MT 347, 386 Mont. 98, 386 P.3d 937.

Parties' Failure to Follow Arbitration Agreement — Procedural Arbitrability: Alleging wrongful discharge, the plaintiff employee association sought declaratory judgment requiring the city of Bozeman to submit to arbitration. Each party argued that the other failed to follow arbitration procedures. On appeal, the Supreme Court held that the dispute should be determined by an arbitrator because time limits and conditions precedent invoke procedural arbitrability. Mont. Pub. Employees Ass'n v. Bozeman, 2015 MT 69, 378 Mont. 337, 343 P.3d 1233.

Port Authority Insured Under County Insurance Policy — Extrinsic Evidence Considered — Policy Construed Against Drafter — Insurer Not Immune From Suit as Reinsurer: After a port authority building was destroyed by a fire, the port claimed that it qualified as an insured under a county insurance company policy that included county members and any other county entities that receive insurance through a county joint insurance authority. The insurance company claimed that the language in the policy did not extend to county entities such as the port. Additionally, the insurance company claimed that it was a reinsurer and therefore it was improper for the port to bring a direct claim against it. The Supreme Court held that the port qualified as an insured under terms of the policy and that a direct claim was proper. In reaching a conclusion that was contrary to the language of the policy, the court gave meaning to the entire contract, considered extrinsic evidence, and construed ambiguous language in the policy against the insurer as the drafter. In determining that a direct claim was proper, the court reasoned that the port dealt directly with the insurance company, and therefore the insurer was an excess insurance carrier, rather than a reinsurer. Lincoln County Port Authority v. Allianz Global Risks US Ins. Co., 2013 MT 365, 373 Mont. 60, 315 P.3d 934.

No Modification of Original Construction Agreement: In a construction contract dispute, the general contractor submitted a Subcontract Agreement (Agreement) to the subcontractor 2 weeks after the subcontractor had begun work. The Agreement expanded the scope of the work the subcontractor had agreed to perform without additional compensation. The general contractor argued the Agreement modified any contract with the subcontractor because the subcontractor: (1) orally agreed to the Agreement; (2) submitted a payment application in compliance with the Agreement; and (3) admitted to having signed the Agreement. The Supreme Court concluded no modification occurred. The parties had not fully executed the alleged oral agreement; therefore, it could not operate as a modification. Compliance with the payment process did not rise to the requisite level of assent to modification. Pursuant to 28-2-906, a written contract must be delivered before it becomes effective. Since the subcontractor never returned the Agreement to the general contractor, no modification occurred. AAA Constr. of Missoula, LLC v. Choice Land Corp., 2011 MT 262, 362 Mont. 264, 264 P.3d 709.

Covenants Intended to Remain in Effect Until Rejected by Property Owners — Failure of Sufficient Tract Owners to Vote to Amend Covenants: Subdivision property owners entered covenants that would automatically extend for "successive period" of 10 years. The covenants could also be amended by a two-thirds vote of the owners of the original tracts. Some of the owners contended that the covenant extension language was ambiguous because it was not clear if the covenants would be renewed only for a single 10-year period or for successive 10-year periods. The District Court held that the language was not ambiguous, but rather contained a typographical error, and that successive 10-year periods applied. Plaintiffs appealed, but the Supreme Court affirmed. Taken as a whole the covenant language intended that the covenants remain in effect until affirmatively rejected by the property owners. In this case, five of the eight original tract owners voted to amend the covenants, so without the required two-thirds vote, the covenants remained unamended. Brewer v. Hawkinson, 2009 MT 346, 353 M 154, 221 P3d 643 (2009). See also Creveling v. Ingold, 2006 MT 57, 331 M 322, 132 P3d 531 (2006).

Genuine Issue of Material Fact Whether Dam Operation Damaged Lakeshore Properties — Summary Judgment Improper — Class Action Vacated: Flathead Lake landowners brought a class action suit against defendant operators of Kerr Dam for operating outside the scope of their easements in a manner that continuously eroded and damaged plaintiffs' lakeshore properties. The District Court rejected plaintiffs' argument that the dam operator was not allowed to affect plaintiffs' properties above an elevation of 2,893 feet, concluding instead that defendants' easements covered entire parcels. The court concluded that erosion, including wave action erosion, was within the scope of the easements and held that any duty defendants had to not cause unreasonable damage to plaintiffs' properties applied only to damage unrelated to use of the easement. Therefore, summary judgment was granted to defendants, and plaintiffs appealed. The Supreme Court first agreed that the District Court's contour line theory was correct. The "2,893 feet" clause did not establish the vertical limit argued by plaintiffs because although the dam operators' right to flood, subirrigate, drain, or otherwise affect the shoreline was not unlimited, it was not restricted to a maximum elevation of 2,893 feet at each parcel, but rather extended to whatever part of each parcel was affected when the lake was held at 2,893 feet above mean sea level as measured at the dam. The court also agreed that the right to cause some erosion was necessary to the enjoyment of the right to perpetually flood, subirrigate, and drain and was thus included by implication in the easements. However, further factual development and trial were necessary to address the question of whether the erosion was reasonable, necessary, and within the scope of the easements, which could not be resolved by summary judgment. Additionally, the question of whether defendants breached their obligation to not cause unreasonable damage to the shoreline properties and to not unreasonably interfere with plaintiffs' enjoyment also required further factual development and possibly trial. Therefore, the order certifying the case as a class action was vacated and the case was remanded for further consideration. Mattson v. Mont. Power Co., 2009 MT 286, 352 M 212, 215 P3d 675 (2009).

On remand, the District Court decertified the class as to one defendant and denied the plaintiffs' motion for certification as to another defendant on the basis that the question of whether the erosion caused unreasonable damage to or unreasonably interfered with the plaintiffs' properties required an individual, property-by-property analysis that was improper for class certification. On appeal, the Supreme Court reversed, concluding that class certification to both defendants was proper because the reasonableness of the erosion presents a common question that is incapable of being resolved on a property-by-property basis since an aggregate of the benefits and burdens imposed on all of the shoreline properties must be considered together to determine reasonableness. Mattson v. Mont. Power Co., 2012 MT 318, 368 Mont. 1, 291 P.3d 1209.

No Ambiguity in Complete, Final Sales Agreement — Parol Evidence Inadmissible: The parties entered a sale agreement for a ready-mix concrete plant. Plaintiff subsequently filed an action alleging that defendant violated the agreement by breaching the covenant to not compete and the covenant of good faith and fair dealing, which constituted malice resulting in lost profits, sales, and goodwill. The District Court granted summary judgment to defendant and plaintiff appealed, but the Supreme Court affirmed. The District Court correctly concluded that the sales agreement constituted a complete, final agreement and unambiguously did not include a noncompetition provision, but in fact provided that plaintiff would sell concrete to defendant for use in the area. The intention of the parties was ascertainable from the writing alone, and the agreement was presumed to represent all transactions regarding elements extrinsic to the agreement and was thus considered complete and final, so parol evidence was inadmissible. Richards v. JTL Group, Inc., 2009 MT 173, 350 M 516, 212 P3d 264 (2009). See also Lindey's, Inc. v. Professional Consultants, Inc., 244 M 238, 797 P2d 920 (1990), and Mary J. Baker Revocable Trust v. Cenex Harvest States, Cooperatives, Inc., 2007 MT 159, 338 M 41, 164 P3d 851 (2007).

Ambiguity of Contract Raising Genuine Issues of Fact — Summary Judgment Improper: In a dispute over the sale of aircraft, the District Court considered summary judgment motions from both parties, granted summary judgment for plaintiff on claims of breach of contract and express warranty, and denied defendant's summary judgment counterclaim of breach of contract and express warranty. The Supreme Court examined the contract and found ambiguities regarding whether defendant accepted the aircraft "as is" at signing or maintained the right to inspect and reject the aircraft prior to closing, as well as the parties' extension of the closing date. The ambiguities raised genuine issues of material fact regarding breach of contract and express warranty that were not appropriate for summary judgment, and the Supreme Court reversed for trial on the issues. Corporate Air v. Edwards Jet Center, Mont., Inc., 2008 MT 283, 345 M 336, 190 P3d 1111 (2008).

Tort Claims Not Precluded by Contract Claims Arising From Same Event: In a dispute over the sale of aircraft, the District Court considered summary judgment motions from both parties and granted defendant summary judgment on plaintiff's tort claims on grounds that plaintiff had relied on a contract theory of relief and thus elected to be made whole under the contract. Plaintiff appealed on grounds that tort liability can exist with contract liability and that recovery on a contract theory does not necessarily preclude recovery on tort theories such as fraud. Defendant responded that summary dismissal of the tort claims was proper because plaintiff should not be allowed to make a double recovery and that because plaintiff's claims were commercial, tort damages are not available except in rare cases when a separate tort claim arises from the contractual relationship. Without ruling on the validity of the tort claims, the Supreme Court held that consideration of plaintiff's fraud-based claims was not precluded by the fact that plaintiff also made separate contract claims arising out of the same event. The tort claims were required to be considered individually and could not be dismissed under a blanket rationale that the tort claims and contract claims were mutually exclusive. The District Court's summary judgment was reversed, and the issue was remanded for further consideration. Corporate Air v. Edwards Jet Center, Mont., Inc., 2008 MT 283, 345 M 336, 190 P3d 1111 (2008).

Unambiguous Release of Claims Against Attorney for Malpractice — Parties Bound by Terms of Release: Rich was injured in two automobile accidents and retained attorney Ellingson to represent her in claims against her insurer. The first claim was dismissed when Ellingson failed to serve a timely summons on the insurer after filing the claim. Rich sued Ellingson for malpractice and received a settlement of $175,000 from Ellingson's malpractice insurer. As part of the settlement, Rich signed a release providing that Ellingson was released from any future malpractice claims arising from representation of Rich. Rich's second accident claim was subsequently dismissed when the statute of limitations had run, and Rich again sued Ellingson for malpractice. Ellingson contended that the suit was barred by the release. The District Court agreed and dismissed the claim, and Rich appealed. Considering the document as a whole, the Supreme Court held that the release clearly and unambiguously barred future claims arising from Ellingson's representation of Rich in the multiple actions against Rich's insurer. Rich's latent discontent with the release, without more, was an insufficient basis upon which to premise an alteration of the express, unambiguous agreement. The District Court was affirmed. Rich v. Ellingson, 2007 MT 346, 340 M 285, 174 P3d 491 (2007). See also Hanson v. Oljar, 231 M 272, 752 P2d 187 (1988).

Easement Limited to Historical Size and Location of Grant: In 1949, plaintiffs' predecessor in interest granted an easement to defendant's predecessor in interest to allow the construction of radio towers on a portion of a 160-acre parcel, conditioned on location and maintenance of the property. Defendant subsequently notified plaintiffs that he intended to expand the radio facilities beyond the original construction site. Plaintiffs sued, asserting that the expansion would encompass property not included in the original grant, while defendant contended that the easement encompassed the entire 160 acres described in the grant, so the facilities could be expanded onto other portions of the parcel or relocated elsewhere within the parcel. The District Court found for plaintiffs, and on appeal, the Supreme Court affirmed. Under the rules of contract construction, the grant language clearly limited placement of the radio facilities on a portion of the 160-acre parcel to be chosen by defendant's predecessor in interest. Thus, the easement did not encumber the full 160-acre parcel, but rather was limited in size and location to the historical location of the radio facilities. The original grant also required that wires, ground radial antennas, conduits, and transmission lines be buried to a minimum depth of 12 inches, and the District Court did not err in ordering defendant to bury the equipment pursuant to the maintenance portion of the grant. Anderson v. Stokes, 2007 MT 166, 338 M 118, 163 P3d 1273 (2007).

Ambiguity Required Prior to Application of Construction-Against-Drafter Principle: Plaintiffs asserted that because defendants drafted a number of the easements in a utility right-of-way contract, the terms of the contract should be construed most favorably toward plaintiffs. However, plaintiffs admitted that the contract language was unambiguous, and before a contract may be construed against the drafter, some ambiguity must exist. Thus, the trial court did not err by not interpreting the contract language in a light most favorable to plaintiffs. Mary J. Baker Revocable Trust v. Cenex Harvest St., Cooperatives, Inc., 2007 MT 159, 338 M 41, 164 P3d 851 (2007).

Evidence of Circumstances Under Which Instrument Made Admissible for Determining Ambiguity: As a general rule, evidence of the circumstances under which an instrument was made may not be considered when the language of the instrument is clear and certain in its terms. However, objective evidence of those circumstances, including the situation of the subject of the instrument and the parties to it, may be shown and considered to aid the court in determining, as a preliminary matter, whether the instrument contains an ambiguity. If the court determines that no ambiguity exists, then the extrinsic evidence may not be considered further, but if the court determines that an ambiguity is present in the instrument, then the extrinsic evidence may be introduced at trial to allow the trier of fact to determine the intent of the parties in entering into the contract. In the present case, both parties agreed that language in a right-of-way contract was unambiguous, so the trial court did not err in refusing to consider the circumstances under which the contract was made. Mary J. Baker Revocable Trust v. Cenex Harvest St., Cooperatives, Inc., 2007 MT 159, 338 M 41, 164 P3d 851 (2007). See 11 Williston on Contracts, 33:39 (4th Ed. 1999).

Objective Determination of Whether Ambiguity Exists in Contract — Ambiguity Not Created by Disagreement Over Interpretation of Contract Language: The determination whether an ambiguity exists in a contract is made on an objective basis. A conclusion of ambiguity is not compelled by the fact that parties to a document, or their attorneys, have or suggest opposing interpretations of a contract or even disagree as to whether the contract is reasonably open to just one interpretation, nor does ambiguity exist just because a claimant says so. Rather, an ambiguity exists only if the language is susceptible to at least two reasonable but conflicting meanings. In the present case, plaintiffs' backup position was that language in a right-of-way contract was ambiguous, but the three circumstances proffered by plaintiffs, even when considered collectively, did not demonstrate that the contract language was susceptible to at least two reasonable but conflicting meanings. Thus, the trial court did not err in concluding that the language was unambiguous, which was in fact plaintiffs' primary position. Mary J. Baker Revocable Trust v. Cenex Harvest St., Cooperatives, Inc., 2007 MT 159, 338 M 41, 164 P3d 851 (2007), followed in Wills Cattle Co. v. Shaw, 2007 MT 191, 338 M 351, 167 P3d 397 (2007).

Validity of Forum Selection Language in Employment Contract: A clause in an employment contract provided that in case of disputes, venue for enforcement of the contract would be in the state District Courts of Lewis and Clark County, Montana, or in the district of choice set by the independent contractor. A dispute arose, and plaintiff independent contractor sought to enforce the contract in Lewis and Clark County. Defendant moved to dismiss for lack of personal jurisdiction, and the motion was granted on grounds that the contract's forum clause did not give the court personal jurisdiction over defendant, a resident of Illinois. Plaintiff appealed, and the Supreme Court reversed. As held in May v. Figgins, 186 M 383, 607 P2d 1132 (1980), parties to a contract may agree in advance to submit to the jurisdiction of a given court, and as such, forum selection clauses are prima facie valid and should be enforced unless the resisting party shows that the agreement was not deliberately and understandably made and that the contractual language did not clearly, unequivocally, and unambiguously express a waiver of personal jurisdiction. In this case, the parties knowingly consented to personal jurisdiction in Montana and the forum selection clause was clear and unambiguous. The case was remanded for further proceedings in the Montana court. Milanovich v. Schnibben, 2007 MT 128, 337 M 334, 160 P3d 562 (2007).

Contract Interpretation Applicable to Restrictive Covenants — How Ambiguity Resolved — Restrictive Covenants Strictly Construed: General rules of contract interpretation apply to restrictive covenants, and any person having an interest under a restrictive covenant may seek declaratory relief concerning any question of construction arising under the covenant. When a restrictive covenant has been reduced to writing, the intent of the parties is to be ascertained, when possible, from the writing alone, and when the language of a covenant is clear, a court must apply the language as written. Restrictive covenants are strictly construed, and ambiguities in covenants are resolved to allow free use of property. The determination of whether an ambiguity exists in a restrictive covenant is a question of law for a court to decide, but mere disagreement between the parties as to interpretation of a restrictive covenant does not automatically create an ambiguity. Creveling v. Ingold, 2006 MT 57, 331 M 322, 132 P3d 531 (2006). See also Newman v. Wittmer, 277 M 1, 917 P2d 926 (1996), and Toavs v. Sayre, 281 M 243, 934 P2d 165 (1997).

No Ambiguity in Restrictive Covenant Prohibiting Placement of Trailers and Mobile Homes Upon Property — Development of Recreational Vehicle Park Precluded: A restrictive covenant provided that no trailers or mobile homes were to be placed upon the property conveyed by a deed. The District Court held that the term "placed upon" contemplated permanent placement, and that temporary placement was therefore not precluded. The court also held that the covenant disallowed only trailer houses or mobile homes used for residences. The court thus concluded that the covenant did not disallow development of the property as a campground for recreational vehicles and travel trailers. On appeal, the Supreme Court noted that language in a restrictive covenant should be understood in its ordinary and popular sense. It is not the role of a court to insert modifying language into clearly written and unambiguous written instruments, and the unambiguous language in the covenant contained no words to indicate the parties' intent to allow temporary trailers or mobile homes not used as residences. The District Court erred in modifying the covenant language to allow trailers to be placed on the property, so the conclusion that a campground for recreational vehicles and travel trailers was allowable was reversed. Creveling v. Ingold, 2006 MT 57, 331 M 322, 132 P3d 531 (2006).

Ambiguous Settlement Agreement Language Regarding Maintenance Calculation — Gross Disposable Income Interpreted as Pretax Income: A settlement agreement provided that monthly maintenance payments be 15% of the husband's gross disposable income. In direct opposition to the husband's interpretation, the wife and her expert contended that the amount should be based on pretax rather than after-tax income, and the District Court agreed. The court found that the term gross disposable income was ambiguous because "gross" and "disposable" had mutually exclusive meanings in this context, so the court looked beyond the agreement language to the parties' intent. Because the term was ambiguous, the parties' proposed interpretations were equally proper, so under 28-3-306, the ambiguity was construed in the wife's favor because the maintenance provision was for her benefit. The court's allowance of testimony from the wife's expert was also within the court's discretion. In re Marriage of Mease, 2004 MT 59, 320 M 229, 92 P3d 1148 (2004).

Interest Owed on State Highway Right-of-Way Condemnation Agreement Pursuant to Clear Language of Stipulation: The Department of Transportation filed a condemnation action against defendants in connection with a highway construction project. As part of the action, the parties entered a stipulation granting the Department possession of the right-of-way in exchange for $35,780, $11,000 payable immediately and $24,780 still owing, plus interest, at 10% a year, on the final award or settlement from the date of service of summons until the date of withdrawal by defendants. A dispute arose over the amount of interest owed. The District Court applied 70-30-302 and determined that the Department owed interest on $7,187 of the total remainder, the amount of land-leveling costs, which the Department paid. Defendants appealed the order, contending that interest was actually owed on the entire $24,780 remaining settlement. The Supreme Court agreed. The language in the stipulation was clear and unambiguous and required the Department to pay interest on the excess of the final settlement award, which was $24,780.

The District Court erred in applying the statute to the exclusion of the actual stipulation language to which the parties agreed. The clear language of the stipulation and the intent of the parties controlled. The case was remanded with instructions to order the Department to pay interest on the entire final settlement, with credit for amounts already paid. St. v. Asbeck, 2003 MT 337, 318 M 431, 80 P3d 1272 (2003).

Ambiguity Regarding Whether Settlement Contingent on Alternate Financing — Summary Judgment Improper: Plaintiff sought to foreclose on a loan made to defendant, alleging that defendant's liabilities exceeded the value of the collateral, resulting in default pursuant to the terms of the note. The parties made several attempts to settle the issue, resulting in defendant's payoff to plaintiff, but in an amount that the plaintiff claimed was insufficient. The District Court granted summary judgment to plaintiff and ordered enforcement of the settlement agreement. However, a letter memorializing the settlement agreement, when considered with the parties' other correspondence, created an ambiguity regarding whether the settlement was contingent on alternate financing. Because there was more than one reasonable interpretation regarding the parties' intention, the parties' affidavits and testimony were admissible to determine intention and raised an issue of fact that precluded summary judgment. The case was remanded for further proceedings. Stockman Bank v. Potts, 2002 MT 178, 311 M 12, 52 P3d 920 (2002).

Fundamental Right to Choose Independent Contractor Status — Presumption of Employee Status Not Violative of Right to Contract: The Department of Revenue classified a worker as an employee, despite the worker's contention that he was an independent contractor. The worker contended that he had a fundamental right to choose independent contractor status and that the Department's classification deprived him of the right to contract. The District Court cited Phoenix Physical Therapy v. Unemployment Ins. Div., 284 M 95, 943 P2d 523 (1997), for the proposition that the ability to contract is not absolute and that a party's intent does not control whether the party is classified as an employee or independent contractor, but rather that the status must be proved as a matter of fact. Although the worker in question had a fundamental right to choose employment status, the worker was nevertheless required to prove that he was an independent contractor as a matter of fact, and the fact that he failed to do so was supported by substantial evidence in the record. Thus, the Department did not exceed its statutory authority in classifying the worker as an employee. Spain v. Dept. of Revenue, 2002 MT 146, 310 M 282, 49 P3d 615 (2002).

Potential Access Rights Merged With Deeds and Extinguished — Applicability of Contract Law Doctrine of Merger: Prior to Gehring's consent to sell 360 acres to APS Corporation (APS) in 1970, they entered an agreement that included a provision on access rights, whereby Gehring purported to grant future purchasers access to other land owned by Gehring for certain recreational purposes. After being told by the Gehring Ranch Corporation that they would not be allowed access to Gehring's land for recreation, the successors in interest to APS sought to enforce the agreement, alleging that they had been improperly excluded from the land and that the agreement created an easement over Gehring's land. The District Court granted summary judgment for the Gehring Ranch Corporation, noting that the agreement did not identify Gehring's other lands upon which an easement was purportedly created. The court also held that any agreement prior to execution of the deeds was merged with the deeds and that because the deeds transferring title did not provide for access, any access rights promised in the agreement were lost. The decision was appealed, and the Supreme Court affirmed. The clause in the agreement was part of a larger agreement to transfer property in the future, and Gehring did not intend to create an easement, but at most intended to provide for potential access privileges if certain conditions, such as creation of a property owners' association and adoption of rules governing the use of the recreational privileges, were met. The Supreme Court cited Urquhart v. Teller, 1998 MT 119, 288 M 497, 958 P2d 714 (1998), in applying the contract law doctrine of merger, holding that the deeds contained all the rights of the parties and that because no access privileges were mentioned in the deeds, any potential access rights referred to in the agreement merged with the deeds and were lost. Richman v. Gehring Ranch Corp., 2001 MT 293, 307 M 443, 37 P3d 732 (2001).

Shareholders' Agreement Enforceable Independent of Stock Exchange — Different Intent Contained in Separate Agreements Separately Enforceable: Following his termination from employment with Bitterroot International Systems, Inc. (Bitterroot), Knutson sought to exercise his buyout rights under the shareholders' agreement. Bitterroot refused to pay, contending that an earlier merger transaction and the subsequent shareholders' agreement should be read together and citing Rumph v. Dale Edwards, Inc., 183 M 359, 600 P2d 163 (1979), for the proposition that when construing an agreement that is part of a larger transaction, the intention of the parties must be determined by examining the entirety of the larger transaction. However, Rumph was distinguishable here because all the agreements in question occurred at different times and did not reference or depend upon each other. Each agreement was clear and unambiguous. Under Gerdes v. Omaha Home for Boys, 89 NW 2d 849 (Nebr. 1958), a court may not avoid the language of a complete, unambiguous contract by consolidating it with another writing if the effect of doing so would be to avoid an essential part of the contract. The District Court properly concluded that the shareholders' agreement was enforceable independent of the stock exchange between the parties. Knutson v. Bitterroot Int'l Sys., Inc., 2000 MT 203, 300 M 511, 5 P3d 554, 57 St. Rep. 800 (2000), followed in O'Brien v. O'Brien, 2022 MT 246, 411 Mont. 101, 532 P.3d 831.

Interpretation of Latent Ambiguity in Marital Property Settlement Agreement — Wife Entitled to Value of Improvements to Real Property Made Between Time of Dissolution and Time of Sale: A property settlement agreement provided that the wife would receive the family home subject to the debt owed upon it (although no debt was owing) and that when she sold it, she would return one-half of the proceeds of the sale of the house to the husband. The wife's subsequent improvements to the home increased its value from $55,500 at the time of dissolution to $75,000 at the time of sale. The wife requested an interpretation of the settlement agreement to address the division of proceeds in light of her substantial improvements to the property, as well as her payment of all property taxes since the date of dissolution. The District Court concluded that the property settlement agreement created a latent ambiguity by failing to address what would happen to the expenditures of one party that were for neither maintenance nor repairs. The court concluded that the agreement contemplated that the wife would maintain the value of the home at the time of dissolution and divide that value when the house was sold and that the property taxes were an item of maintenance that the wife was responsible for pursuant to the agreement. The Supreme Court affirmed. In light of the latent ambiguity in the agreement, the District Court did not introduce an additional provision to the agreement that deprived the husband of his contractual rights, but merely interpreted the agreement to clarify what was meant by "one-half of the proceeds of the sale of the house" in the context of nonmaintenance expenditures. Upon finding a latent ambiguity, the District Court properly admitted parol evidence to interpret the agreement and correctly allowed the wife to retain the proceeds from the sale of the house attributable to her expenditures for improvements beyond maintenance and repairs. In re Marriage of Holloway, 2000 MT 104, 299 M 291, 999 P2d 980, 57 St. Rep. 418 (2000).

Assignment of Retail Installment Contract — Breach of Warranty — Abrogation of Waiver of Recourse: Arcadia Financial, Ltd. (Arcadia), is a Minnesota corporation that purchases retail installment contracts from automobile dealers, including Prestige Toyota (Prestige) in Billings, after the dealers have entered into installment contracts with automobile buyers. Knight purchased a Toyota from Prestige, and Knight's contract contained a provision assigning the contract to Arcadia under one of four options. The same day that Knight purchased the automobile, Prestige assigned the contract to Arcadia "without recourse", which meant that only the contract warranties applied, one of which was that Prestige had a valid certificate of title and would send it to the appropriate officials within 10 days of sale to ensure Arcadia's interest in the vehicle. The contract also provided that Prestige unconditionally guaranteed full performance of the contract in the event that it breached any of the warranties. Prestige failed to send a valid certificate of title as required. Knight later defaulted and filed for bankruptcy protection. Arcadia demanded that Prestige repurchase the Knight contract. Prestige admitted breaching the warranty but claimed that it was not required to repurchase the contract and refused to do so, asserting that Arcadia's damages were limited to the amount that the bankruptcy trustee received from sale of the automobile. The District Court awarded Arcadia the principal amount due on the Knight contract, plus interest, attorney fees, and costs, concluding that under the clear language of the contract assignment provisions, Prestige had guaranteed payment of all sums due when it failed to deliver the valid title within the time required. The Supreme Court agreed, noting that the contract was converted into a full recourse contract when Prestige failed to deliver the valid title, so Prestige was required to repurchase the contract for the amount of principal remaining due. The detriment proximately caused by Prestige's failure to repurchase the contract was the principal amount owing on the contract. Further, the District Court properly awarded attorney fees to Arcadia as the prevailing party pursuant to 28-3-704. Arcadia Financial, Ltd. v. Prestige Toyota, 1999 MT 273, 296 M 494, 989 P2d 831, 56 St. Rep. 1111 (1999).

Ability to Contract Not Absolute — Public Policy Legislation May Not Be Avoided: Phoenix Physical Therapy argued that the intent of the contract for services entered into with an individual was to create an independent contractor relationship and that therefore it was not liable to pay unemployment insurance premiums. The Supreme Court ruled that the right to contract is not absolute, the purpose of the Unemployment Insurance Law is to protect the general welfare of the citizens of the state, and parties may not privately contract to waive public protection statutes. Phoenix Physical Therapy v. Unemployment Ins. Div., 284 M 95, 943 P2d 523, 54 St. Rep. 791 (1997).

Five Agreements Constituting Integrated Sales Agreement With Condition Precedent — Overriding Previous Partnership Agreements and Providing for Attorney Fees: Daines argued that of the five agreements executed by the parties, the option agreement should have been read separately and interpreted as an option to buy conferring a privilege but not imposing an obligation and that on that basis, he could not be liable for not completing a purchase agreement. The Supreme Court held that the lower court had properly looked at the five agreements as a whole in interpreting the parties' intent and had correctly concluded that the agreements constituted an integrated sales agreement subject to conditions precedent. The Supreme Court further held that since the five agreements constituted a sales agreement, they superseded the previous partnership agreements. The respondents were not liable for capital contributions as partners, and the default provision in the option agreement providing for attorney fees did apply to the agreement created by all five of the documents executed by the parties. Daines v. Knight, 269 M 320, 888 P2d 904, 52 St. Rep. 8 (1995).

Consideration of Nature of Dealings Between Attorney and Client: When the determination of duties owed to an insurance company by its attorney involved a question of fact, the District Court did not err in examining past legal dealings between the parties or in ascertaining the exact duties expected of the attorney from an examination of the parties' conduct. Based on that conduct, the court properly concluded that the attorney had fulfilled his required advisory duties and was not liable for any negligence or breach of contract. Aetna Fin. Co. v. Ball, 237 M 535, 774 P2d 992, 46 St. Rep. 1031 (1989).

Adjusting Appraised Value to Enforce Agreement Proper: On appeal of an order granting specific performance of a settlement agreement between the parties to a dispute over operation of a family farm, Hass claimed that the District Court had erred in finding the value of the farm corporations to be higher than that agreed upon by the appraisers appointed by the parties. The Supreme Court affirmed, ruling that since a court has a duty to enforce an agreement that is clear, as this one is, it was proper for the District Court to increase the appraised value by the value of debts owed to the corporations by the parties. Hass v. Hass Land Co., 217 M 246, 704 P2d 63, 42 St. Rep. 1170 (1985).

Error to Deny Jury Trial on Plaintiffs' Claims for Breach of Contract — Interpretation: Appellants, as developers, entered into subdivision improvement agreement with respondent city. The court held that it was error for trial court to deny appellants a jury trial on their claims for breach of contract based on allegations that the parties either failed to attach like meanings to the word "crossing" (to be installed over a city drain) or, alternatively, that the crossing to be constructed under SID is not comparable to the one contemplated by the parties at time of entering agreement. If, as here, contract term is ambiguous, intention of parties is left to jury. A claim of differing uses of the word "crossing" puts the existence, as well as meaning, of the present contract at issue for a jury determination. Gray v. Billings, 213 M 6, 689 P2d 268, 41 St. Rep. 1910 (1984), followed in Klawitter v. Dettmann, 268 M 275, 886 P2d 416, 51 St. Rep. 1296 (1994). See also Johnson v. Nyhart, 269 M 379, 889 P2d 1170, 52 St. Rep. 37 (1995).

Repurchase at Reduced Price — Not Mitigation of Damages: The parties entered into an agreement for the lease of a truck. The lease agreement contained a noncancellation provision and provided alternative remedies to the lessor in the event of a default. Lessee returned the truck with current payments to lessor prior to the termination date of the lease. Lessor had to make repairs to the truck. Lessor held a public sale pursuant to the lease and repurchased the truck. He then leased it to another party. The lessor had full title to the truck before and after the sale. There was no payment from buyer to seller to offset damages resulting from lessee's default. Since there was mitigating effect in plaintiff purchasing his own truck, it was error for the District Court to consider the sale in awarding damages. The value of the re-lease rather than the sale price of the truck was the proper method of determining mitigation of damages. Diede v. Davis, 203 M 205, 661 P2d 838, 40 St. Rep. 394 (1983).

Ambiguous Phrase — Entire Contract to Determine Intent: A coal contract was entered on March 31, 1974. In 1976, the Montana Department of State Lands (functions now transferred to Department of Environmental Quality) determined that Decker was precluded under Title 82, ch. 4, part 2, from disturbing a certain portion of land within the mine area contemplated by the contract. It was conceded this would increase mining costs. The contract contained a price adjustment provision that allowed for price adjustments due to new government regulation.

Decker contended the nondisturbance determination was a "new regulation" even though the statute under which the Department acted was enacted in 1973. The court in construing "new regulation" looked to the entire contract to determine mutual intent. The court determined, in light of adjustment provisions for all other cost increases, that "new regulation" meant increases required by government action taken after the effective date of the contract. Austin v. Decker Coal Co., 701 F2d 420 (5th Cir. 1983).

Landfill Operator to Be Licensed: The appellant had contracted with the refuse board of his county to operate a sanitary landfill. The trial court found that the appellant was required by his contract to obtain a license to operate the landfill. The Supreme Court on review said that when read together, it is apparent that under 75-10-203 and 75-10-221, the County Commissioners, the refuse board, or the appellant could be proper applicants for the landfill license. Finding no exemption from the obligation to seek the required license, it was a question of the parties' contract requirements. The Supreme Court declined to find that 75-10-112 requires all local governments to obtain the requisite license for operation of a disposal site when the operations by contract are to be performed by another individual. Citing this section and 28-3-303 and noting that the language in the contract here was clear and unambiguous, the Supreme Court found its duty to enforce the contract as made. The license requirement imposed by 75-1-221 was clearly applicable to the operation of the disposal site. Therefore, the appellant was required by the terms of the contract to obtain the operator's license. Ryan v. Bd. of County Comm'rs, 190 M 273, 620 P2d 1203, 37 St. Rep. 1965 (1980).

Documents Construed Together — Intent Not Gleaned From Isolated Words: When there is a close relationship between two documents they must be construed together to determine the intent of the parties. The intent is determined by reading the two documents in full rather than dissecting them to take isolated words and phrases as the intent of the parties. Rumph v. Dale Edwards, Inc., 183 M 359, 600 P2d 163 (1979), distinguished in Knutson v. Bitterroot Int'l Sys., Inc., 2000 MT 203, 300 M 511, 5 P3d 554, 57 St. Rep. 800 (2000), and followed in Richman v. Gehring Ranch Corp., 2001 MT 293, 307 M 443, 37 P3d 732 (2001).

Clear Language — Rules of Construction Inapplicable: When the language is clear and unambiguous, the contract does not require the application of rules of construction and it is the court's duty to enforce the contract as made by the parties. Schulz v. Peake, 178 M 261, 583 P2d 425 (1978).

Third-Party Materialmen — Action Against Surety: A third-party materialman was not entitled to recover on a cause of action against a surety on its surety bond that named the general contractor as the sole obligee and when the general contractor, subcontractor, and surety did not intend to benefit or protect any third-party materialmen by the execution of the bond. Treasure St. Indus., Inc. v. Welch, 173 M 403, 567 P2d 947 (1977).

Output Contract: Extrinsic evidence is admissible to explain the true intentions of the parties to an output contract, since the terms of the contract are ambiguous and such contracts must be interpreted in light of circumstances surrounding the parties and prior business dealings. McNussen v. Graybeal, 146 M 173, 405 P2d 447 (1965).

Where Ambiguous: Where there is ambiguity in a contract, it is open under this section and 28-3-402 to interpretation by the aid of evidence aliunde, so as to give effect to the mutual intention of the parties to it at the time it was made. McNussen v. Graybeal, 146 M 173, 405 P2d 447 (1965); Butte Water Co. v. Butte, 48 M 386, 138 P 195 (1914).

Intention Determined as of Time of Contracting — Look to Entire Agreement: Contracts must be so interpreted as to give effect to the mutual intention of the parties as it existed at the time of contracting, so far as the same is ascertainable and lawful, the intention to be gathered from the entire agreement, not from particular words or phrases or disjointed parts of it. Snider v. Carmichael, 102 M 387, 58 P2d 1004 (1936).

Interpretation of Parties: Where parties to a contract (deed) of doubtful or ambiguous meaning have placed a particular interpretation upon it, such interpretation is one of the best indications of their true intent. Musselshell Valley Farming & Livestock Co. v. Cooley, 86 M 276, 283 P 213 (1929).

Duty of Courts to Enforce Entire Contract as Made:

Courts must give effect to every part of a contract so as to make its terms operative; they may not make a new contract for the parties, nor read language into or eliminate lawful terms therefrom unless the words employed are meaningless or involve an absurdity. Union Cent. Life Ins. Co. v. Jensen, 74 M 70, 237 P 518 (1925).

It is a well-settled rule of law that the circumstances under which a contract is made or the intent of the parties existing at that time are only material when the contract is ambiguous in some of its terms. If it is plain and unambiguous it needs no construction, and it is the duty of the court to enforce it as made by the parties. Bullard v. Smith, 28 M 387, 72 P 761 (1909). See also Frank v. Butte & Boulder Min. & Lumber Co., 48 M 83, 135 P 904 (1913), distinguished in Howard v. Hancock Oil Co., 68 F2d 694 (9th Cir. 1934).

Valid Though Burdensome and Unwise: Where no legal impediment is shown which would have prevented parties to a contract from entering into it or from expressing it in language of their own, courts must give effect to the meaning and intention of the parties as expressed in the language employed and may not make a new contract for them. The mere fact that as made the contract may appear unreasonable, burdensome, or unwise to one of them is insufficient to avoid it, where the latter party was of legal age, had all the facts clearly before him long prior to its execution, and his alleged damage was due to his own inattention and carelessness. Hinerman v. Baldwin, 67 M 417, 215 P 1103 (1923).

Substance Over Form: In interpreting a contract so as to give effect to the mutual intentions of the parties at the time the contract was entered, the substance rather than the form of the contract is controlling. Ferry & Co. v. Forquer, 61 M 336, 202 P 193 (1921). See also State ex rel. Priestly v. Croff, 95 M 498, 27 P2d 540 (1933); Winkelmann v. Minn. Mut. Life Ins. Co., 66 M 451, 213 P 1104 (1923).

Escrow Agreement: The intention of the parties to a contract such as an escrow agreement is to be ascertained from the language used in the instrument, and this section, together with 28-3-202, 28-3-302, and 28-3-303, furnishes the guide for its interpretation. Knapp v. Andrus, 56 M 37, 180 P 908 (1919).

Clear Language Given Ordinary Meaning: This section simply means that the intention of the parties shall be ascertained in the first instance by reference to the language employed by them. Where the words used are clear, certain, and unambiguous, interpretation may not be resorted to. The language employed must be given its ordinary meaning. Quirk v. Rich, 40 M 552, 107 P 821 (1910). See also Frank v. Butte & Boulder Min. & Lumber Co., 48 M 83, 135 P 904 (1913), distinguished in Howard v. Hancock Oil Co., 68 F2d 694 (9th Cir. 1934).

INSURANCE CONTRACTS

Declaratory Judgment Action — Duty of Insurer to Defend and Indemnify — District Court Error as Matter of Law: The plaintiff, an insurance company, filed an action for declaratory judgment that it did not have a duty to defend or indemnify the defendants in a wrongful death lawsuit. The District Court denied the motion for summary judgment and held that the plaintiff had a duty to defend one of the defendants as an additional insurer under the policy. On appeal, the Supreme Court reversed, holding that the District Court erred as a matter of law and that the defendant did not meet the contractual requirement to be an automatic additional insured under the policy. Employers Mut. Cas. Co. v. Estate of Buckles, 2019 MT 136, 396 Mont. 153, 443 P.3d 534.

Qualification of Vehicle as Temporary Substitute — Use of Vehicle Determinative: The plaintiff, who worked as a cook for an outfitting company, was injured at camp when her personal truck, which was attached to the trailer in which she was sleeping, was stolen. In the days preceding the accident, the truck had been used to transport clients and their luggage to camp because the company's vehicle, a Suburban, that usually hauled clients and luggage was being repaired. The plaintiff claimed that she was entitled to uninsured motorist coverage under her employer's policy on the Suburban because her truck was being used as a "temporary substitute vehicle". The insurer refused coverage, countering that her truck could not be considered a "temporary substitute vehicle" because the plaintiff would have still been driving her truck even if the Suburban had been available. After the District Court granted the insurer summary judgment, the plaintiff appealed. In a matter of first impression, the Supreme Court clarified that the proper test for what constitutes a temporary substitute vehicle is the use to which it is put. Given that the undisputed facts showed that the plaintiff had used her truck to do the work the Suburban would have done had it not been in the shop for repairs, she was entitled to coverage. Accordingly, the Supreme Court reversed the order granting summary judgment and directed the District Court to enter judgment in favor of the plaintiff. Stonehocker v. Gulf. Ins. Co., 2016 MT 78, 383 Mont. 140, 368 P.3d 1187.

Injured Neither Named Insured Nor Occupant of Covered Vehicle at Time of Accident — No Coverage Under Commercial Policy: The defendants' daughter was injured when she was riding a bicycle out of state. The defendants owned a business that had a commercial policy for its fleet of company vehicles; however, the daughter was neither an employee of the business nor occupying a company vehicle at the time of the accident. The defendants sought benefits from the commercial policy on their daughter's behalf. The plaintiff insurance company sought declaratory judgment that the policy did not cover the daughter for her injuries. The District Court granted summary judgment in favor of the plaintiff, and the defendants appealed. The Supreme Court affirmed, agreeing that because the daughter was not a named insured or occupying a car covered by the policy at the time of the accident, the plaintiff was entitled to judgment as a matter of law. Am. St. Ins. Co. v. Flathead Janitorial & Rug Services Inc., 2015 MT 239, 380 Mont. 308, 355 P.3d 735.

Farmowners Policy Construed to Cover Individuals, Not Partnership: Modroo's daughter was killed in an auto accident, and Modroo sought coverage under a farmowners policy that listed Modroo (and by definition Modroo's family members) as insureds. The insurer asserted that the policy was for the family farming partnership and covered only insureds who were driving a vehicle insured under the policy, which the daughter was not. The District Court agreed and held that the policy did not cover Modroo individually or family members. On appeal, the Supreme Court determined that the insurer's interpretation was reasonable but was not the only interpretation. Another reasonable interpretation was that the policy granted Modroo coverage as an individual because the named insured block on the form listed Modroo, not the partnership. If the insurer intended to cover only the partnership, that entity could have been listed as the named insured, but no reason existed for the insurer to list individuals as insureds unless it intended coverage to apply to them. Construing the ambiguity against the insurer, the policy was held to cover Modroo individually, and the daughter as a family member as well. Modroo was entitled to medical payments under the farmowners policy and the District Court decision was reversed. Modroo v. Nationwide Mut. Fire Ins. Co., 2008 MT 275, 345 M 262, 191 P3d 389 (2008). See also Mitchell v. St. Farm Ins. Co., 2003 MT 102, 315 M 281, 68 P3d 703 (2003).

Ohio Law Applied to Disallow Stacking of Coverages — Offsets Allowed: The District Court conducted a conflict of law analysis and concluded that Ohio law governed Modroo's entitlement to damages for an accident that occurred in Montana under a personal auto policy that Modroo obtained in Ohio. Under Ohio law, stacking of policy coverages is disallowed and offsets are allowed. Citing Csulik v. Nationwide Mut. Ins. Co., 723 NE 2d 90 (Ohio 2000), Modroo contended that the policy's multiple choice-of-law provisions resulted in ambiguity and that Montana law should have applied because it is more favorable to the insured. The Supreme Court disagreed and noted that although the policy provided for payment of compensatory damages under Montana tort law while also providing that Ohio law governed interpretation of the contract, the presence of two choice-of-law provisions did not necessarily create an ambiguity. The issue of stacking policies was a question of contract law rather than tort law, so the Ohio law applied. Likewise, the provisions in the policy that any amounts available under uninsured motorist coverage would be offset by any amounts available for payment by or on behalf of any liable parties also presented a question of contract law, so Ohio law applied to that issue as well. The Supreme Court declined to overrule its choice of law principles. The District Court did not err in applying Ohio law to the stacking and offset issues. Modroo v. Nationwide Mut. Fire Ins. Co., 2008 MT 275, 345 M 262, 191 P3d 389 (2008). The Modroo choice of law rationale was also applied in Tucker v. Farmers Ins. Exch., 2009 MT 247, 351 M 448, 215 P3d 1 (2009). In Tidyman's Management Serv. v. Davis, 2014 MT 201, 376 Mont. 72, 330 P.3d 1135, the Supreme Court overruled Tucker to the extent it suggested that the "materially greater interest" factors supplant the rule from Mitchell v. St. Farm Ins. Co., 2003 MT 102, 315 Mont. 281, 68 P.3d 703, when an insurance contract does not contain a choice-of-law provision.

Insurance Policy Provisions Excluding Coverage for Medical Payments Paid by Workers' Compensation Not Ambiguous or Against Public Policy: Newbury's auto insurance policies provided medical coverage for bodily injury sustained through being struck as a pedestrian by a motor vehicle or trailer, except to the extent that workers' compensation benefits were required to be payable. Newbury was struck by a vehicle while on the job, and workers' compensation paid all but $1,175.80 of Newbury's medical expenses. Newbury then submitted an insurance claim seeking the full $10,000 in medical benefits from the insurance policies, but the insurer paid only the remaining $1,175.80 not paid by workers' compensation. Newbury asserted that the workers' compensation provisions in the policies were ambiguous and against public policy. The District Court granted summary judgment for the insurer, and Newbury appealed. The Supreme Court held that the policy, taken as a whole, was not ambiguous because it clearly demonstrated an intent to exclude coverage and did not defeat coverage or render policy coverage illusory. Moreover, the workers' compensation provisions were not violative of public policy. Newbury's expectations were not objectively reasonable, and Newbury received exactly the coverage for which he paid. Allowing Newbury to receive more than the total amount of medical expenses would have resulted in a windfall to Newbury. The District Court was affirmed. Newbury v. St. Farm Fire & Cas. Ins. Co., 2008 MT 156, 343 M 279, 184 P3d 1021 (2008), distinguishing Sullivan v. Doe, 159 M 50, 495 P2d 193 (1972), Hardy v. Progressive Specialty Ins. Co., 2003 MT 85, 315 M 107, 67 P3d 892 (2003), and Mitchell v. St. Farm Ins. Co., 2003 MT 102, 315 M 281, 68 P3d 703 (2003), and followed in Conway v. Benefis Health Sys., Inc., 2013 MT 73, 369 Mont. 309, 297 P.3d 1200.

Diesel Fuel Properly Considered Pollutant for Purposes of Commercial Liability Insurance Policy Exclusion: A petroleum company held commercial liability and property insurance policies that contained a standard absolute pollution exclusion clause disclaiming coverage for spills resulting from pollutants, which were defined to include liquid irritants or contaminants. The company also held a coverage extension that provided coverage for expenses to extract pollutants from land or water. When a diesel fuel spill occurred on the company's property, the company sought insurance reimbursement under the policies and also submitted claims to the Montana Petroleum Tank Release Compensation Board for reimbursement for corrective action costs. The insurer denied the claim, and after the company subrogated the claim to the Board, the Board sought reimbursement from the insurer, but the insurer denied all reimbursement requests, so the Board sued to recover corrective costs from the insurer. The District Court concluded that diesel fuel was a pollutant and that coverage was therefore excluded under the commercial general liability portion of the policy. On appeal, the Board asserted that the court erred in denying coverage, but the Supreme Court affirmed. The terms of the pollution exclusion clause were not ambiguous, and when viewed from the objective perspective of the average consumer, diesel fuel was properly included in the definition of pollutant. The District Court correctly denied coverage under the commercial general liability portion of the policy disclaiming coverage for spills resulting from pollutants. Mont. Petroleum Tank Release Comp. Bd. v. Crumleys, Inc., 2008 MT 2, 341 M 33, 174 P3d 948 (2008), distinguished in High Country Paving, Inc. v. United Fire & Cas. Co., 2022 MT 72, 408 Mont. 202, 507 P.3d 1165, holding that a technical violation of the Property and Casualty Insurance Policy Language Simplification Act, 33-15-333 through 33-15-340, may not be used to invalidate unambiguous policy exclusions that would result in an increase of the risk assumed.

Y2K Computer Problems Considered Faulty Design and Inherent Vice — Insurance Coverage Precluded by Policy Exclusions: The state filed insurance claims related to remediation of problems associated with the Y2K transition. The claims were denied, and the state sued. The District Court held that the claims were precluded from coverage by policy language that excluded coverage for damage caused by faulty design and inherent vice. On appeal, the Supreme Court affirmed. An inherent vice is an existing defect, disease, or decay or the inherent nature of a commodity that will cause it to deteriorate over time and also means a loss not covered by a policy that is not related to an extraneous cause but to a loss entirely from internal decomposition or some quality that brings about its own injury or destruction and that must be inherent in the property for which recovery is sought. The state's Y2K problem was an excluded inherent vice because the date field was an inherent problem that brought about its own problem. The faulty design and inherent vice policy exclusions were not ambiguous and clearly excluded the claimed losses. Even though the state did not receive copies of the policies, the policies were renewals of existing policies that contained identical coverage provisions and exclusions, so the state could not reasonably claim that it was unaware of the relevant policy terms and exclusions, and the insurer could rely on valid exclusions in the policy when the state had notice of the exclusions. St. v. Allendale Mut. Ins. Co., 2007 MT 83, 337 M 49, 154 P3d 1233 (2007), following Port of Seattle v. Lexington Ins. Co., 48 P3d 334 (Wash. App. 2002), and GTE Corp. v. Allendale Mut. Ins. Co., 372 F3d 598 (3rd Cir. 2004).

Retroactive Applicability of Decision Prohibiting Antistacking of Insurance Provisions to Pending Cases: In Hardy v. Progressive Specialty Ins. Co., 2003 MT 85, 315 M 107, 67 P3d 892 (2003), the Supreme Court decided that antistacking provisions in an underinsured motorist policy were unconstitutional. Plaintiffs brought a class action in federal court claiming that Hardy entitled them to additional payments from past insurance claims that were not previously allowed because their policies did not allow for stacking. The federal court certified the question to the Supreme Court as to whether Hardy applied prospectively only or retroactively to qualified claims arising before the Hardy decision. The Supreme Court agreed with the decision in Harper v. Va. Dept. of Taxation, 509 US 86 (1993), that limiting a rule of law to its prospective application creates an arbitrary distinction between litigants based merely on the timing of their claims and that in the interests of fairness and finality, the line should be drawn between claims that are final and claims that are not. The Supreme Court then decided that the retroactivity test in

Chevron Oil Co. v. Huson, 404 US 97 (1971), still applies to Montana civil decisions if all three Chevron factors are met: (1) the decision to be applied nonretroactively must establish a new principle of law, either by overruling clear past precedent on which litigants may have relied or by deciding an issue of first impression whose resolution was not clearly foreshadowed; (2) the court must weigh the merits and demerits in each case by looking at the prior history of the rule in question, its purpose and effect, and whether retroactive application will further or retard its operation; and (3) the inequity imposed by retroactive application has been weighed. However, the retroactive effect of a decision does not apply to cases that became final or that were settled prior to a decision's issuance. Thus, Hardy applies retroactively in qualifying circumstances on open claims arising before its issuance and is limited to cases pending on direct appeal or not yet final. Dempsey v. Allstate Ins. Co., 2004 MT 391, 325 M 207, 104 P3d 483 (2004). See also LaMere v. Farmers Ins. Exch., 2011 MT 272, 362 Mont. 379, 265 P.3d 617, holding that under Dempsey, a settled case is considered final.

Underinsured Motorist Coverage Included With Uninsured Motorist Coverage — Reasonable Consumer Expectation of Additional Coverage: Rather than paying a separate premium for independent underinsured motorist coverage, Mitchell's underinsured motorist coverage was part of the uninsured motorist coverage, no separate premium was paid for the underinsured coverage, and the declarations pages did not list underinsured motorist coverage separately. Nevertheless, Mitchell was still entitled to a reasonable expectation that the underinsured motorist coverage provided additional coverage. As in Hardy v. Progressive Specialty Ins. Co., 2003 MT 85, 315 M 107, 67 P3d 892 (2003), the underinsured motorist definition in Mitchell's policy contravened that expectation and thus violated Montana's public policy. Mitchell v. St. Farm Ins. Co., 2003 MT 102, 315 M 281, 68 P3d 703 (2003).

Failure of Insurer to Pay Within Sixty-Day Period Specified in Insurance Contract — No Error in Interpretation of Contract: An insurance contract required the insurer to pay for a loss within 60 days after the insurer received proof of loss and: (1) the parties reached an agreement; (2) there was a final judgment; or (3) the insured filed an appraisal with the insurer. The insured sought money damages because the claim was not paid within the 60-day period following the joint appraisal, which resulted in plaintiffs' alleged mental anguish and emotional distress. However, given a lengthy dispute over the amount of damages, the significant disparity between estimates, and plaintiffs' rejection of the joint appraisal, the District Court found that the agreement contemplated by the contract that would trigger the 60-day payment period was never reached. Plaintiffs appealed on grounds that the District Court misinterpreted the contract. The Supreme Court affirmed. The rejected joint appraisal did not constitute an agreement. Because the contractual requirements for the 60-day payment period were not met, the District Court did not err when it declined to conclude that the insurer should have made payment within 60 days of the joint appraisal. Nelson v. Farmers Union Mut. Ins. Co., 2003 MT 101, 315 M 268, 68 P3d 689 (2003).

Offset Provision in Underinsured Motorist Policy Violative of State Policy — Antistacking Provisions Unconstitutional: Hardy paid separate premiums for underinsured motorist (UIM) coverage of $50,000 a person and $100,000 an accident for each of three vehicles. Hardy was injured when the vehicle that he was riding in was negligently struck by another car. Hardy recovered $50,000 from the other driver's liability insurer, but that amount was insufficient to cover Hardy's injuries, so Hardy sought compensation pursuant to the UIM coverage on his vehicles. Hardy believed that the policies could be stacked to aggregate $150,000 of UIM coverage. Defendant insurance company denied coverage, and Hardy sued in federal District Court. The insurer raised three arguments in its defense, contending that: (1) the tortfeasor's vehicle was not underinsured, as defined in the policy, because the total liability coverage for the tortfeasor's vehicle was equal to the highest single UIM coverage limit in Hardy's policy; (2) the policy required Hardy's UIM coverage for one vehicle to be offset by all amounts recovered from the tortfeasor; and (3) Hardy's UIM coverages could not be stacked or aggregated for purposes of either comparing limits or affording $150,000 of UIM coverage. The federal District Court certified the three questions to the Montana Supreme Court, which determined that the UIM definition and offset clause in Hardy's policy violated Hardy's reasonable expectation of coverage when a tortfeasor's insurance provided inadequate indemnity. The policy declarations page suggested coverage in an amount that was actually not available; therefore, the terms of the UIM coverage were ambiguous in violation of Montana public policy and rendered the coverage that the insurer promised to provide illusory. Further, the provisions of 33-23-203 that allow insurers to charge premiums for nonexistent coverage are not rationally related to the objective of maintaining affordable insurance in Montana and constitute an arbitrary and capricious legislative action that is unconstitutionally violative of due process. A Montanan should reasonably expect coverage up to the aggregate limits of separate policies when a separate premium for UIM coverage was charged for each policy. Antistacking provisions that allow an insurer to receive valuable consideration for coverage that is not provided are against public policy. Hardy v. Progressive Specialty Ins. Co., 2003 MT 85, 315 M 107, 67 P3d 892 (2003), followed in Mitchell v. St. Farm Ins. Co., 2003 MT 102, 315 M 281, 68 P3d 703 (2003), and distinguished in Parish v. Morris, 2012 MT 116, 365 Mont. 171, 278 P.3d 1015. The Hardy decision was applied retroactively to open claims arising before its issuance and was limited to cases pending on direct appeal or not yet final in Dempsey v. Allstate Ins. Co., 2004 MT 391, 325 M 207, 104 P3d 483 (2004), which was followed in LaMere v. Farmers Ins. Exch., 2011 MT 272, 362 Mont. 379, 265 P.3d 617, holding that under Dempsey, a settled case is considered final. See also Chaffee v. USF&G Co., 181 M 1, 591 P2d 1102 (1979), and Bennett v. St. Farm Mut. Auto. Ins. Co., 261 M 386, 862 P2d 1146 (1993).

Doctrine of Reasonable Expectations Inapplicable When Policy Language Excludes Coverage — Liability Coverage on Borrowed Horse Trailer Limited to Policy Terms: Babcock borrowed a horse trailer from her neighbor, and even though the trailer ball on Babcock's truck was too small for the trailer hitch, she attempted to tow the trailer anyway. The trailer came unhooked, left the road, and struck a fence. Farmers Insurance Exchange (Farmers) paid Babcock the full cost of the fence repair. Babcock requested that Farmers also pay for damages to the trailer. Farmers paid $500 toward the trailer, which constituted Babcock's policy limit for collision and comprehensive coverage. Babcock sued, claiming that Farmers was required to pay for the trailer damage under the liability coverage. The District Court granted summary judgment for Farmers, concluding that the plain policy language limited coverage to $500. Babcock appealed, asserting that the policy language was ambiguous but nevertheless created a reasonable expectation that a trailer was covered and that the exclusion for damage "to property owned or being transported by an insured person" did not apply because the trailer was not being "transported" when it was damaged, having separated from the truck. Farmers argued that, under Babcock's interpretation, a passenger ejected from a car would have no claim for medical payments because the passenger did not "occupy" the vehicle at the time of injury. The Supreme Court agreed. The doctrine of reasonable expectations does not apply to create coverage when the terms of the policy clearly demonstrate an intent to exclude particular coverage. In this case, the policy language clearly excluded liability coverage for the borrowed trailer because it was in Babcock's charge and she was transporting it at the time of the accident. Babcock v. Farmers Ins. Exch., 2000 MT 114, 299 M 407, 999 P2d 347, 57 St. Rep. 479 (2000).

Invalidity of No-Consent-to-Settlement Clause: A no-consent-to-settlement clause in an insurance policy, disallowing coverage if the insured settled with any person or organization who may have been liable for the bodily injury without obtaining written consent of the insurance company, was held to be void because enforcement of the clause would result in a backing away from the mandatory offering requirement of 33-23-201 and would place control of efforts to collect from the responsible party in the hands of the insurer. While not denying the insurer's right to subrogation, the court would not allow the right to subrogation to negate the required offering of uninsured motor vehicle coverage. St. Farm Mut. Auto. Ins. Co. v. Taylor, 223 M 215, 725 P2d 821, 43 St. Rep. 1667 (1986).

Primary Insurance Company Solely Responsible for Liability: While making a delivery for his employer, Roach and Smith Distributors, Guiberson parked a delivery truck outside the Warm Springs store, leaving the keys in the ignition. Tintinger, a patient at Warm Springs state hospital, and another patient got in the truck and began to drive it away. Guiberson jumped in the truck and unsuccessfully attempted to persuade Tintinger to stop the truck. Eventually the truck overturned and Guiberson was injured. Guiberson sued Hartford Casualty Insurance, his personal insurer, under an uninsured motorist provision. Hartford joined, as third-party defendants, State Farm, Roach and Smith Distributors' insurer, and the state of Montana. State Farm's policy also contained uninsured motorist coverage. The jury returned a verdict in favor of Guiberson for $600,000, finding Tintinger and the state equally responsible for Guiberson's injuries. Based on the insurance policies, the court apportioned Tintinger's portion of the judgment between Hartford and State Farm. The Supreme Court reversed, ruling that the insurance policies indicated that Hartford contracted to be an excess insurer only, that State Farm was a primary insurer, and that under a "stacking" approach (now abolished, 33-23-203) State Farm's insurance adequately covered Tintinger's liability. Guiberson v. Hartford Cas. Ins. Co., 217 M 279, 704 P2d 68, 42 St. Rep. 1196 (1985). See also Farmers Alliance Mut. Ins. Co. v. Holeman, 1998 MT 155, 289 M 312, 961 P2d 114, 55 St. Rep. 601 (1998).

Restrictions on Uninsured Motorist Coverage Strictly Construed in Favor of Insured: The Supreme Court does not support provisions placed on uninsured motorist coverage that restrict or thwart available liability coverage which the insured would be entitled to in an accident. The language of an uninsured motorist provision is nullified where it gives less coverage for acts of the uninsured than it would to the insured, thus defeating the purpose of providing such coverage. Guiberson v. Hartford Cas. Ins. Co., 217 M 279, 704 P2d 68, 42 St. Rep. 1196 (1985). See also St. Farm Mut. Auto. Ins. Co. v. Taylor, 223 M 215, 725 P2d 821, 43 St. Rep. 1667 (1986), and Nimmick v. St. Farm Mut. Auto. Ins. Co., 270 M 315, 891 P2d 1154, 52 St. Rep. 208 (1995).

Contracts of Insurance: Contracts of insurance, like all others, must be construed with a view to carrying out the intention of the parties. McAuley v. Cas. Co. of Am., 39 M 185, 102 P 586 (1909).

REAL ESTATE CONTRACTS

Real Estate Contract Prepayment Clause Ambiguous — Payment of Additional Tax Liability Not Fully Performed: A contract for the sale of real estate contained a prepayment clause that required the plaintiff purchaser to pay any additional taxes incurred by the defendant sellers because of the prepayment. The plaintiff tendered payment of the balance due 2 years in advance of the final due date but did not include payment for additional tax liability. The District Court held that the tendered payment of the balance due under the contract without inclusion of the additional tax liability did not constitute full performance of the plaintiff's obligations under the contract. On appeal, the Supreme Court upheld the District Court's ruling. First Nat'l Properties, LLC v. Hillstead Trust, 2020 MT 211, 401 Mont. 59, 472 P.3d 134.

Existence of Express Easement Governed by Rules of Contract Interpretation: Neighbors each asserted having an express easement over the other's property and denied being burdened by an express easement. The District Court looked to their predecessor's easement agreement and the incorporation of that agreement into their conveyances, ruling that each neighbor enjoyed and was burdened by an easement. When both parties appealed, the Supreme Court affirmed the District Court's decision. The Supreme Court explained that the existence of an express easement is governed by the rules of contract interpretation and engaged in extensive discussion of the case, concluding that the District Court was correct. Wiegele v. W. Dry Creek Ranch, LLC, 2019 MT 254, 397 Mont. 414, 450 P.3d 879.

Extrinsic Evidence Permissible Based on Parties' Intent — Intent Defeated by Mistakes in Vital Facts: The District Court did not err by considering extrinsic evidence to interpret and reform the parties' contract. Generally, when the terms of an agreement are reduced to writing by the parties, the writing is considered as containing all those terms and there can be no evidence of the terms of the agreement other than the contents of the writing. However, an exception to this rule permits extrinsic evidence to be admitted when a mistake or other imperfection of the writing is put at issue. The District Court correctly concluded that the recorded agreement did not reflect the parties' intent. The mistakes in the agreement constituted "vital facts" that defeated the parties' contractual intentions. It was therefore appropriate for the District Court to consider extrinsic evidence and to reform the contract to reflect the parties' true intent. In re Platt, 2018 MT 43, 390 Mont. 338, 413 P.3d 818.

Writings Granting Interest in Real Property Governed by Rules of Contract Interpretation: Landowners sued for access to an airstrip on neighboring property on a theory that their land was benefited by an easement. The District Court ruled against the landowners, finding that their property was not benefited by an easement because a previous subdivider failed to reserve an easement. On appeal, the Supreme Court affirmed, but for the different reason that contract interpretation governs the construction of a writing granting an interest in real property and that the original easement allowed access to the airstrip for one airplane; finding an easement in favor of the landowners would permit more than one airplane to use the airstrip. Hudson v. Irwin, 2018 MT 8, 390 Mont. 138, 408 P.3d 1283.

No Improper Reliance on Extrinsic Evidence in Finding of Valid and Enforceable Express 60-Foot Easement for Subdivision: Defendant acquired certain property after an express easement across the property was created by the former owner. Defendant refused to allow the building of an access road across the property, contending that the easement agreement was invalid on several grounds. The District Court examined the agreement and concluded that the easement was valid and enforceable and granted summary judgment for plaintiffs. On appeal, defendant asserted that the District Court erroneously relied on facts outside the agreement, making summary judgment inappropriate, but the Supreme Court affirmed. For purposes of interpreting a writing granting an interest in real property, evidence of the surrounding circumstances, including the situation of the property and the context of the parties' agreement, may be shown so that the judge is placed in the position of those whose language the judge is to interpret. However, to comply with the statute of frauds and the recording system, the writing itself must ultimately stand on its own and meet the formal requirements for granting a property interest. In this case, the District Court was allowed to consider various facts not contained in the easement agreement for purposes of understanding the situation, but the court's analysis of the easement's validity apparently was limited to the face of the agreement, so the court did not erroneously rely on extrinsic facts. The easement agreement satisfied the formal requirements for expressly granting an easement and created a valid 60-foot emergency public access and utility easement that was enforceable against defendant. Additionally, the District Court properly concluded that because there was no dominant tenement, the easement was in gross and could be used by members of the public to travel between the subdivision and the public highway for emergency purposes and to provide utility services. There being no questions of material fact, summary judgment was proper. Broadwater Dev., LLC v. Nelson, 2009 MT 317, 352 M 401, 219 P3d 492 (2009), distinguishing Blazer v. Wall, 2008 MT 145, 343 M 173, 183 P3d 84 (2008). See also Kuhlman v. Rivera, 216 M 353, 701 P2d 982 (1985).

Lack of Express Utility Easements Not Condition Adversely Affecting Title: The buyer of condominium units refused to close on the sale because the sale agreement did not expressly state the existence of utility easements for each parcel. The District Court determined that the lack of express utility easements was not a condition that adversely affected title and held that the buyer breached the contract by refusing to close the sale. On appeal, the Supreme Court affirmed. The entire property was part of the sale, including all units and appurtenances. If the buyer wanted each unit to have a stated right to access the utility areas, the buyer could affirmatively grant that right to each unit after acquiring the property. Also, the buyer could have required the express establishment of the easements in a written addendum to the contract to be a condition precedent to closing, but the buyer did not do so. The buyer failed to establish that the absence of individual unit easements was an adverse condition of title that allowed the buyer to refuse to close the sale. Apple Park, L.L.C. v. Apple Park Condominiums, L.L.C., 2008 MT 284, 345 M 359, 192 P3d 232 (2008).

Buy-Sell Agreement Not Subject to Financing Contingency Absent Specific Contractual Funding Language: A buy-sell agreement stated that the buyer had sufficient funds to close the sale of a ranch and was not relying upon any contingent source of funds unless otherwise stated in the agreement, but there was no third-party financing specified in the agreement. Nevertheless, when the buyer was not able to close the sale for lack of funds, both parties sought to recover the earnest money, and the buyer asserted that the contract language was clear and unambiguous in conditioning the sale on financing. The District Court disagreed, and on appeal, the Supreme Court concurred. The buyer represented that it had sufficient funds, and nowhere in the agreement or in an addendum extending the closing date was it specified that completing financing meant that the buyer had to obtain a loan from a third party. The District Court's award of the earnest money to the seller was affirmed. Sec. Abstract & Title Co. v. Smith Livestock, Inc., 2006 MT 265, 334 M 172, 146 P3d 732 (2006).

Payment of Actual Costs and Discretionary Attorney Fees Under Contract: A real estate contract provided that the award of reasonable attorney fees to the prevailing party was discretionary with the court and also provided that the prevailing party was entitled to actual costs. The District Court deducted fees and costs related to actions in which plaintiff did not prevail, resulting in a reduction of both attorney fees and costs. On appeal, the Supreme Court affirmed the attorney fee award as an appropriate exercise of the District Court's discretion, but reversed the reduced award of costs because plaintiff was entitled to actual costs under the contract. Gullett v. Van Dyke Constr. Co., 2005 MT 105, 327 M 30, 111 P3d 220 (2005).

No Factual Issue of Waiver Under Contractual Consent to Assignment Clause — Summary Judgment Proper: The Nicholsons entered a contract option with J.G.L. Distributing (JGL) that gave JGL 5 years to purchase the Nicholsons' property. The option contained a consent to assignment clause that required JGL to obtain the Nicholsons' written consent before assignment to a third party. JGL subsequently assigned an interest in the property to plaintiff but did not notify the Nicholsons. Plaintiff spent money improving the property but missed a payment. The Nicholsons then notified JGL that the option expired and that they intended to sell the property to someone else. Plaintiff sued JGL and the Nicholsons, JGL counterclaimed against plaintiff and filed cross-claims against the Nicholsons, the Nicholsons counterclaimed against JGL, and all three parties moved for summary judgment. The District Court dismissed plaintiff's claim because plaintiff was not a party to the contract. The court also held that the consent to assignment clause was valid and enforceable, but that even though JGL breached the agreement by not notifying the Nicholsons of the assignment and by missing a payment, the breach was not material and did not serve to terminate JGL's right to exercise the option. The court then concluded that forfeiture would be too harsh a remedy, excused the forfeiture, and granted JGL 20 days to pay the Nicholsons the full purchase price. On appeal, the Supreme Court affirmed. Plaintiff failed to show a genuine issue of material fact that the Nicholsons waived their rights under the consent to assignment clause. The breach of contract by JGL was incidental rather than material, so the District Court's holding that forfeiture would be too harsh was not erroneous. Thus, the District Court correctly applied the antiforfeiture statute when it granted JGL equitable relief under 28-1-104 because JGL's breach was not grossly negligent, willful, or fraudulent. It was only when the Nicholsons discovered that they could sell the property at a greater profit that they acted to strictly enforce the timely payment provision of the contract, so application of the antiforfeiture statute was appropriate to avoid an unjust result. R.C. Hobbs Enterprises, LLC v. J.G.L. Distrib., Inc., 2004 MT 396, 325 M 277, 104 P3d 503 (2004). See also Erban v. Monforton, 227 M 531, 740 P2d 677 (1987), Norwood v. Serv. Distrib., Inc., 2000 MT 4, 297 M 473, 994 P2d 25 (2000), and VanDyke Constr. Co., Inc. v. Stillwater Min. Co., 2003 MT 279, 317 M 519, 78 P3d 844 (2003).

Default Notice in Compliance With Contract for Deed — No Mention of Fees and Costs: A provision in a contract for deed set out additional fees to be paid to the escrow agent in case of default, but when the default notice was sent, there was no mention of the additional fees. Plaintiffs contended that failure to mention the fees rendered the default notice defective. The Supreme Court disagreed. The notice sufficiently complied with the provisions of the contract. Defendants properly followed the default procedure set out in the contract, and excluding the fee information did not render the default notice defective. Danelson v. Robinson, 2003 MT 271, 317 M 462, 77 P3d 1010 (2003).

Attempted Sale of Parcel in Violation of Contract — Plantiff Allowed to Block Sale: Defendants contracted to purchase several parcels of property from plaintiff. When defendants ended up in default, defendants decided to sell one of the parcels to pay off part of the contract balance. Plaintiff attempted to block the sale, and the District Court confirmed plaintiff's ability to do so under the terms of the contract. Defendants appealed, but the Supreme Court affirmed. A provision of the contract allowed the subsequent sale of the parcels by defendants, but only after the principal balance was paid. Because defendants were in default when the attempted sale was made, sale of the tract was not permitted by the terms of the contract. The District Court did not err in holding that plaintiff had a contractual right to block the sale. Weter v. Archambault, 2002 MT 336, 313 M 284, 61 P3d 771 (2002).

Sale of Property Contingent on Financing — Financing Contingent on Grant of Contract — Oral Agreement to Purchase Additional Property Contingent on Initial Sale — Summary Judgment Proper Absent Genuine Issue of Fact: Community, Counseling, and Correctional Services, Inc. (Community), agreed to purchase Albright's property for a prerelease center. An additional oral agreement provided that Community would also purchase furnishings on the property when the sale was completed. The sale was contingent on Community's ability to obtain financing, and financing was contingent upon a grant for the prerelease center to Community from the Department of Corrections. Ultimately, the Department declined to issue the contract for prerelease services, Community was unable to obtain financing, and Albright was unable to sell the property or furnishings. Albright sued Community for breach of contract. The District Court granted summary judgment to Community, holding that under the plain language of the contract, the offer terminated when the Department did not issue the contract. Albright appealed, but the Supreme Court affirmed. No question of fact existed with respect to the conditions for the agreement because the agreement conditioned formation of any contract to buy the real property on Community's ability to obtain financing and Community could not obtain financing without the Department contract. Further, Albright's own affidavit stated that the oral agreement to purchase the furnishings was contingent on purchase of the property, so no issue of fact existed regarding the sale of the furnishings either, and that issue was also properly disposed of by summary judgment. Albright v. Community, Counseling, & Correctional Serv., Inc., 2001 MT 272, 307 M 289, 37 P3d 675 (2001).

Reservation of Single Right-of-Way Over Existing Private Road — No Ambiguity or Conflict With Intended Access: The District Court determined that a reservation of rights in a 1965 deed was ambiguous because the reservation of rights over a single roadway conflicted with the grantors' intent to reserve as many means as possible to their remaining property in a mountainous area. Ambiguities in a reservation of rights in any grant of property are to be construed in favor of the grantor; however, the breadth and scope of an easement are determined upon the actual terms of the contract. The easement in this case was described as "a right of way" over "an existing private road which extends across" the servient tenement "for the use and benefit of Section 3 and [parts] of Section 34". That language indicated the use to which the easement would be put, not the scope of the easement itself. The Supreme Court found that the reservation of rights was not ambiguous; rather, the language restricting the easement to a single right-of-way over an existing private road did not conflict with the intended use of the easement to benefit the grantors' remaining properties, nor did the grantors' intent override any limitation of the singular use of the word "road" in the reservation. Van Hook v. Jennings, 1999 MT 198, 295 M 409, 983 P2d 995, 56 St. Rep. 767 (1999).

Property Description of "2 Acres, More or Less" Not Ambiguous: A property agreement provided that Tract 1 be "2 acres, more or less". Although the phrase "more or less" may not be particularly precise, it is a phrase commonly understood by its plain and ordinary meaning and is not subject to two interpretations. More or less means "approximately", regardless of whether one party would prefer "less", while the other party "more". The property agreement was clear, unambiguous, and enforceable. Schwend v. Schwend, 1999 MT 194, 295 M 384, 983 P2d 988, 56 St. Rep. 754 (1999).

Contract Term Precludes Sellers From Pursuing Remedy of Specific Performance: The sellers under a real estate contract for deed are not entitled to specific performance of the contract because extrinsic evidence, admissible because the contract forfeiture clause is ambiguous, shows that it was the mutual intent of the parties that specific performance is not a possible remedy under the contract. Holman v. Hansen, 237 M 198, 773 P2d 1200, 46 St. Rep. 734 (1989).

Lease Language Unambiguous: Lessee argued that lessor breached agreement by not placing the controls to the clock on the leased sign inside lessee's office. The Supreme Court ruled that the lower court erred in allowing lessee's parole testimony as to where he understood the controls would be placed when the lease between the parties stated that the controls would "remain as installed". Empire Dev. Co. v. Johnson, 236 M 433, 770 P2d 525, 46 St. Rep. 487 (1989).

Parol Evidence Necessary to Determine Intention When Latent Ambiguity Exists: A party transferred property back to sellers in lieu of foreclosure. The transfer arguably constituted a technical conveyance. "Conveyance" had different meanings for the parties and therefore was to be interpreted in accord with the manifest intent of the parties. Parol evidence was necessarily admissible to demonstrate and explain this latent ambiguity, and summary judgment on the issue was improper. Ellingson Agency, Inc. v. Baltrusch, 228 M 360, 742 P2d 1009, 44 St. Rep. 1598 (1987), followed in Fox Grain & Cattle Co. v. Maxwell, 267 M 528, 885 P2d 432, 51 St. Rep. 1136 (1994).

Tenant's Estate in Land — Tenant's Share in PIK Benefits: An oral lease granted two-thirds of crops grown to the tenant Popp. The land was later included in the federal payment in kind program (PIK), but in the absence of a written lease, the payments were made to landlords Frank and Gountanis rather than to Popp. The District Court awarded two-thirds of the PIK benefits to Popp. On appeal, Frank questioned whether a lease which required a percentage of crops to go to the tenant but which did not contemplate later federal benefits required the tenant to share in those benefits when the fruits of his labor did not create any entitlements under the federal program. The Supreme Court, in affirming the award, held that Popp had an estate interest in the land for the duration of his tenancy and that the award to Frank and Gountanis was in derogation of Popp's interest. Popp v. Gountanis, 221 M 267, 718 P2d 340, 43 St. Rep. 801 (1986).

Contracts Executed by Corporation and Owners of Corporation Not Construed Together: Plaintiff sold six lots to Griff and Caplan and sold seven lots to a corporation owned by Griff and Caplan. The corporation stopped making payments, after which the plaintiff refused payments offered by the individual. Plaintiff then brought suit, arguing that the two contracts were really one. The court found that the contracts speak for themselves. Neither makes the slightest reference to the other. The parties to the contract are not the same as the plaintiff contends, although there is some evidence to support the plaintiff. There is also substantial evidence to support the finding of the trial court. Wortman v. Griff, 200 M 528, 651 P2d 998, 39 St. Rep. 1916 (1982).

Construction of Agricultural Lease: Where provision in agricultural lease regarding removal of improvements to the land or payment therefor at end of the lease was unclear, the court applied extrinsic evidence to determine that the parties did not intend payment for nonremovable improvements to be required. The fact of lessee's careless documentation of his expenses and his attempt to claim as improvements items that were included in a required maintenance clause were held to support the finding. Overcast v. Akra, 197 M 276, 642 P2d 1058, 39 St. Rep. 558 (1982).

Real Estate Listing Agreement — Attempt of Broker to Find Purchaser on Owner's Terms as Creating Mutuality: Buechler entered into a contract with Payne, granting him the right to sell Buechler's property. Payne attempted to sell the property and expended time and money to attract purchasers. Buechler canceled the contract before its term expired and sold the property herself. Buechler argued that the contract lacked mutuality. The court found that mutuality of obligation was created by the efforts of the broker to find a purchaser for the property on the owner's terms and the broker's expenditures of time and money in this effort. Payne v. Buechler, 192 M 311, 628 P2d 646, 38 St. Rep. 799 (1981).

Mutual Assent on Elements of Contract — Raising at Trial Level: Plaintiff and defendants entered a buy-sell agreement for a parcel of land owned by defendants. From the filing of the complaint to eventual trial, both parties contended that the buy-sell was valid and enforceable against the other. The issue at trial was not the validity of the contract but whether it included certain alleged easements. Plaintiff was granted specific performance. On appeal, defendants contended that the parties had never agreed on the same terms, that there was no mutual assent or meeting of the minds, and therefore no enforceable contract. Because this contention had not been raised at the trial level, it could not be considered on appeal. Chadwick v. Giberson, 190 M 88, 618 P2d 1213, 37 St. Rep. 1723 (1980).

Contract for Joint Purchase of Property — Construction of Contract as a Whole: Where the appellant and respondent entered into an agreement whereby the respondent agreed to loan appellant the downpayment for the purchase of real property on a contract for deed, the District Court correctly looked to the clear language of the instrument as a whole to determine the intentions of the parties, and phrases relied on by the appellant would not be taken out of context to reach the result urged by the appellant. Downs v. Smyk, 185 M 16, 604 P2d 307 (1979).

Right of First Refusal in Lease: Contract was interpreted as sustaining lessees' right of first refusal of purchase. Tribble v. Reely, 171 M 201, 557 P2d 813 (1976), distinguished in Wymo Land Co. v. Luggie, 1998 MT 50, 288 M 21, 955 P2d 171, 55 St. Rep. 208 (1998).

Restrictive Covenant: Restrictive covenant giving lessee exclusive right to operate drugstore did not extend to property beyond the plot described in the lease, and summary judgment for lessor was properly granted because the intent of the parties at the time they entered into the agreement was reduced to writing and expressed in clear and explicit language that the exclusive covenant applied to "the entire premises covered by the plans and specifications". Matteucci's Super Save Drug v. Hustad Corp., 158 M 311, 491 P2d 705 (1971).

28-3-302. How intention ascertained.

Case Notes

No Breach by Defendant When Lawsuit Commenced — Still Sufficient Time to Remedy Issue but for Plaintiff's Interference: The District Court did not err in concluding that when a lawsuit commenced, the defendant had not breached the parties' agreement concerning a pivot irrigation system. It was undisputed that, at the time the parties entered into an agreement concerning the pivot irrigation system, it was the intention of the parties to provide the plaintiff with green fields on which to hunt. The record reflected that the plaintiff's sole purpose in acquiring land from the defendant in the first place was to enjoy the hunting that he thought the area could be manicured to offer. The Supreme Court upheld the District Court's finding that the defendant had not breached the parties' agreement as of the time that the plaintiff directed that a contractor not undertake any more work on the pivots, because there was still sufficient time for the defendant to repair the pivot irrigation system and cultivate green fields for hunting prior to the start of hunting season but for the plaintiff's interference. Welu v. Twin Hearts Smiling Horses, Inc., 2016 MT 347, 386 Mont. 98, 386 P.3d 937.

No Ambiguity in Complete, Final Sales Agreement — Parol Evidence Inadmissible: The parties entered a sale agreement for a ready-mix concrete plant. Plaintiff subsequently filed an action alleging that defendant violated the agreement by breaching the covenant to not compete and the covenant of good faith and fair dealing, which constituted malice resulting in lost profits, sales, and goodwill. The District Court granted summary judgment to defendant and plaintiff appealed, but the Supreme Court affirmed. The District Court correctly concluded that the sales agreement constituted a complete, final agreement and unambiguously did not include a noncompetition provision, but in fact provided that plaintiff would sell concrete to defendant for use in the area. The intention of the parties was ascertainable from the writing alone, and the agreement was presumed to represent all transactions regarding elements extrinsic to the agreement and was thus considered complete and final, so parol evidence was inadmissible. Richards v. JTL Group, Inc., 2009 MT 173, 350 M 516, 212 P3d 264 (2009). See also Lindey's, Inc.

v. Professional Consultants, Inc., 244 M 238, 797 P2d 920 (1990), and Mary J. Baker Revocable Trust v. Cenex Harvest States, Cooperatives, Inc., 2007 MT 159, 338 M 41, 164 P3d 851 (2007).

Intent Ascertained From Conduct: In the construction of contracts such as a teacher's contract of employment, courts may look not only to the language employed, but to the subject matter and the surrounding circumstances and may avail themselves of the same light which the parties possessed when the contract was made. To ascertain the intention of the parties to a contract, regard must be had to the nature of the instrument, the condition of the parties executing it, the objects which they had in view, and the words employed. If the words are capable of more than one meaning, they are to be given that meaning which it is apparent the parties intended them to have. The practical interpretation of a contract which the parties placed upon it by their course of conduct over a period of years is entitled to great, if not controlling, influence in ascertaining what they understood by its terms. Smith v. School District, 115 M 102, 139 P2d 518 (1943).

Where Automobile Liability Policy Held to Cover Use of Automobile Excluded Thereunder: Defendant, in the business of writing surety bonds and public liability policies, furnishing performance bonds for contractors in construction of bridges and public liability insurance to indemnify public for injuries sustained by reason of work on highway, required under contract with the state, fully advised of the broad requirements contained therein, the performance of which it had guaranteed, will not be heard to say that the policy it actually wrote was less comprehensive than the requirement, and is liable for judgments against contractors for negligence of employees although the use was excluded from coverage. USF&G Co. v. Doheny, 123 F2d 746 (9th Cir. 1941), affirming Doheny v. USF&G Co., 34 F. Supp. 888 (D.C. Mont. 1940).

Recitals Key to Intention: Where the operative parts of an agreement are ambiguous, the recitals may be referred to as a key to the intention of the parties and for the purpose of ascertaining their situation. In re Oppenheimer's Estate, 73 M 560, 238 P 599 (1925).

28-3-303. Writing generally to determine intention.

Case Notes

Parol Evidence Inadmissible 401
Parol Evidence Admissible 402
Intent of Parties 403
Miscellaneous 411

PAROL EVIDENCE INADMISSIBLE

Breach of Contract Claim — Contract Clear and Unambiguous — Judgment on Pleadings Proper: The parties entered into a contract for the defendants to purchase an airplane from the plaintiff. The contract provided that the defendants would conduct an inspection of the plane; however, they withdrew their offer without inspecting the plane. The plaintiff filed suit alleging breach of contract, and the District Court granted the plaintiff judgment on the pleadings. The defendants appealed, arguing that the language in the contract was ambiguous and that extrinsic evidence should be allowed. The Supreme Court affirmed the judgment on the pleadings, holding that the language in the contract was clear and unambiguous and that the District Court had been correct to exclude extrinsic evidence. Kalispell Aircraft Co., LLC v. Patterson, 2019 MT 142, 396 Mont. 182, 443 P.3d 1100.

No Ambiguity in Complete, Final Sales Agreement — Parol Evidence Inadmissible: The parties entered a sale agreement for a ready-mix concrete plant. Plaintiff subsequently filed an action alleging that defendant violated the agreement by breaching the covenant to not compete and the covenant of good faith and fair dealing, which constituted malice resulting in lost profits, sales, and goodwill. The District Court granted summary judgment to defendant and plaintiff appealed, but the Supreme Court affirmed. The District Court correctly concluded that the sales agreement constituted a complete, final agreement and unambiguously did not include a noncompetition provision, but in fact provided that plaintiff would sell concrete to defendant for use in the area. The intention of the parties was ascertainable from the writing alone, and the agreement was presumed to represent all transactions regarding elements extrinsic to the agreement and was thus considered complete and final, so parol evidence was inadmissible. Richards v. JTL Group, Inc., 2009 MT 173, 350 M 516, 212 P3d 264 (2009). See also Lindey's, Inc. v. Professional Consultants, Inc., 244 M 238, 797 P2d 920 (1990), and Mary J. Baker Revocable Trust v. Cenex Harvest States, Cooperatives, Inc., 2007 MT 159, 338 M 41, 164 P3d 851 (2007).

Lease Language Unambiguous: Lessee argued that lessor breached agreement by not placing the controls to the clock on the leased sign inside lessee's office. The Supreme Court ruled that the lower court erred in allowing lessee's parole testimony as to where he understood the controls would be placed when the lease between the parties stated that the controls would "remain as installed". Empire Dev. Co. v. Johnson, 236 M 433, 770 P2d 525, 46 St. Rep. 487 (1989).

Employment Contract Controls: There was no need for further interpretation or parol evidence of an employment contract which expressly exempted appellant from recovering overtime compensation. There was no need for construction of any implied contract since there can be no express and implied contract for the same thing existing at the same time. Thus, summary judgment was appropriate. Weston v. Mont. Highway Comm'n, 186 M 46, 606 P2d 150 (1980).

Husband and Wife: Contract between husband and wife for payment of $10,000 in purchase of partnership interest which stated that the parties released each other from any further liability was not an ambiguous contract and could not be varied by parol evidence. Merritt v. Merritt, 165 M 172, 526 P2d 1375 (1974).

Reservation in Deed: A contract to sell real property provided that oil, gas, and mineral rights would be divided equally between grantor and grantees. A warranty deed and a correction deed issued later contained the same provision. The clause was clear and unambiguous. Plaintiff's attempt to show through the use of parol evidence that the provision referred to royalties only was disallowed. Amundson v. Gordan, 134 M 142, 328 P2d 630 (1958).

Variance of Terms: Parol evidence which tended to vary or alter the terms of a written chattel mortgage will be disregarded where the chattel mortgage was plain and unambiguous and needed no construction. First Nat'l Bank of Plains v. Green Mtn. Soil Conserv. Dist., 130 M 1, 293 P2d 289 (1956).

Employment Contract: The clear meaning of a provision of a contract of employment of defendants as managers of ranch property to the effect that their compensation for a year's services should be one-half of the total receipts from the sales of produce, the increase of livestock, etc., less certain deductions, in the light of other provisions, was that their one-half interest in the total receipts was chargeable with the total operating expenses in computing their compensations, and therefore oral testimony as to prior or contemporaneous negotiations, merged in the contract, was properly excluded. Hill Cattle Corp. v. Killorn, 79 M 327, 256 P 497 (1927).

Purchase Contract: In the absence of fraud, an unconditional written contract of purchase of building material presumably embraced the whole agreement of the parties, and therefore evidence of an oral understanding to the effect that it should not become binding until the architect in charge had approved the materials was inadmissible. Wheeler v. James, 70 M 37, 223 P 900 (1924).

Breach of Sale Contract: In an action for damages for breach of a clause of a written contract of sale of a threshing machine warranting it as being as well made, of good material, and that with proper use and management it would do as good work as any other machine of the same size manufactured for the like purpose, evidence of statements made by defendant's agent in making the sale that it would thresh and clean alfalfa as well as any other machine of the same size, etc., was properly rejected as an attempt to vary the terms of the written instrument by parol. Rowe v. Emerson-Brantingham Implement Co., 61 M 73, 201 P 316 (1921).

Custom Not to Vary Writing: Where the terms of a contract of shipment of livestock were clear and explicit as to where stops should be made for feeding and resting, parol testimony to the effect that it was customary for shippers to have them stop for those purposes at another point was inadmissible. Cook v. N. Pac. Ry., 61 M 573, 203 P 512 (1921).

PAROL EVIDENCE ADMISSIBLE

Evidence of Circumstances Under Which Instrument Made Admissible for Determining Ambiguity: As a general rule, evidence of the circumstances under which an instrument was made may not be considered when the language of the instrument is clear and certain in its terms. However, objective evidence of those circumstances, including the situation of the subject of the instrument and the parties to it, may be shown and considered to aid the court in determining, as a preliminary matter, whether the instrument contains an ambiguity. If the court determines that no ambiguity exists, then the extrinsic evidence may not be considered further, but if the court determines that an ambiguity is present in the instrument, then the extrinsic evidence may be introduced at trial to allow the trier of fact to determine the intent of the parties in entering into the contract. In the present case, both parties agreed that language in a right-of-way contract was unambiguous, so the trial court did not err in refusing to consider the circumstances under which the contract was made. Mary J. Baker Revocable Trust v. Cenex Harvest St., Cooperatives, Inc., 2007 MT 159, 338 M 41, 164 P3d 851 (2007). See 11 Williston on Contracts, 33:39 (4th Ed. 1999).

Termination of Lease — Removal of Holdover Tenant — Agricultural Exception to Landlord-Tenant: Defendant sold plaintiff her property. The instrument contained a lease back to defendant of the buildings and 6 acres. Plaintiff gave notice that the lease was to terminate. Defendant refused to vacate. Plaintiff brought an action under the unlawful detainer statutes which provide for an award of treble damages. Defendant contended the dispute was governed by the Montana Residential Landlord and Tenant Act of 1977. Plaintiff contended the lease was within the "agricultural" exclusion contained in 70-24-104(8). The lease provisions gave no indication of the nature of the buildings or of the intended use of the 6 acres. The trial court allowed the introduction of photographs and oral testimony regarding the lease, which established that the use of the land was for maintenance of defendant's livestock. The trial court properly allowed parol evidence to resolve an ambiguity in the lease. The Supreme Court determined that the legislative intent of 70-24-104 was for a comprehensive coverage of all agricultural operations, whether they are large-scale operations for profit or small-scale operations secondary to the use of the residence. The unlawful detainer provisions were properly applied. Dussault v. Hjelm, 192 M 282, 627 P2d 1237, 38 St. Rep. 738 (1981).

Real Estate Sale Contract: Provisions in real estate sale contract that time was of the essence and that payments could be made on or before January 15 of each year created ambiguity sufficient that when vendee accelerated payment and made full payment to escrow agent, vendor's action for breach of contract could not be dismissed without hearing parol evidence to determine intention of the parties. Kielmann v. Mogan, 156 M 230, 478 P2d 275 (1970).

Grazing Permit: Where a contract was unambiguous and clear in all respects except for the seller's obligation concerning a grazing permit for national forest land, it was proper to admit extrinsic evidence on both sides of the issue. Where the extrinsic evidence was conflicting, the Supreme Court looked to determine if there was substantial credible evidence to uphold the District Court's decision. Dooling v. Bright-Holland Co., 152 M 267, 448 P2d 749 (1969).

Automobile Sale: Where a brief memorandum of sale of an automobile did not contain all the terms of the agreement between the buyer and seller and was uncertain and ambiguous, parol evidence in aid of its interpretation was admissible. Sutton v. Masterson, 86 M 530, 284 P 264 (1930).

Where One Party Is Allowed to Introduce Parol Evidence, Other May Also on Same Subject: Where one party to an action on a written contract is permitted to introduce evidence of preceding oral negotiations leading up to the making of the writing, thus varying its terms, his opponent may properly give oral testimony as to the same matter, over an objection that the testimony offered tends to contradict the writing. Peterson v. Nelson, 77 M 539, 252 P 368 (1926).

INTENT OF PARTIES

Indemnification Proper Under Terms of Subcontract: The state contracted with the plaintiff on a highway paving project. The state and the plaintiff insured the project, and the contractor subcontracted parts of the job to the defendant. On the day after the defendant applied sand and oil to the road, a thunderstorm caused the oil to emulsify in the rainwater and therefore damage passing vehicles. The vehicle owners brought claims against the state, which the state paid. The plaintiff reimbursed the state for what the state paid to the vehicle owners and then sued the defendant, seeking indemnification pursuant to the subcontract. The District Court granted the defendant's motion for summary judgment. On appeal, however, the Supreme Court reversed, holding that under the express terms of the subcontract, indemnification was proper because, but for the defendant's action in applying the oil, the damage would not have occurred. The Supreme Court therefore remanded the matter for the District Court to enter judgment in favor of the plaintiff. A.M. Welles, Inc. v. Montana Materials, Inc., 2015 MT 38, 378 Mont. 173, 342 P.3d 987.

Contract Terms Requiring Payment of Depreciation Unambiguous: The language of a signed contract, in which the contract terms specified that depreciation payments would be made beginning on a specific date provided for in the contract, was clear and unambiguous. When the language of a contract is unambiguous, the court ascertains and declares the terms of the contract. Boyne USA, Inc. v. Lone Moose Meadows, LLC, 2010 MT 133, 356 Mont. 408, 235 P.3d 1269.

Covenants Intended to Remain in Effect Until Rejected by Property Owners — Failure of Sufficient Tract Owners to Vote to Amend Covenants: Subdivision property owners entered covenants that would automatically extend for "successive period" of 10 years. The covenants could also be amended by a two-thirds vote of the owners of the original tracts. Some of the owners contended that the covenant extension language was ambiguous because it was not clear if the covenants would be renewed only for a single 10-year period or for successive 10-year periods. The District Court held that the language was not ambiguous, but rather contained a typographical error, and that successive 10-year periods applied. Plaintiffs appealed, but the Supreme Court affirmed. Taken as a whole the covenant language intended that the covenants remain in effect until affirmatively rejected by the property owners. In this case, five of the eight original tract owners voted to amend the covenants, so without the required two-thirds vote, the covenants remained unamended. Brewer v. Hawkinson, 2009 MT 346, 353 M 154, 221 P3d 643 (2009). See also Creveling v. Ingold, 2006 MT 57, 331 M 322, 132 P3d 531 (2006).

Expectation of Arbitration Unreasonable Under Contract of Adhesion: Plaintiff signed a contract to purchase a used motor home and subsequently discovered that it needed $17,000 in mitigation damages. Defendant moved to compel arbitration and the motion was granted, so plaintiff appealed. The Supreme Court held that because plaintiff's options were to accept or reject the contract without an opportunity to negotiate the preprinted terms, the contract was one of adhesion. The arbitration clause in the contract by which plaintiff waived various constitutional and procedural rights was not within plaintiff's reasonable expectations, so the arbitration clause was determined to be unenforceable. The District Court was reversed. Woodruff v. Bretz, Inc., 2009 MT 329, 353 M 6, 218 P3d 486 (2009), following Kloss v. Edward D. Jones & Co., 2002 MT 129, 310 M 123, 54 P3d 1 (2002), distinguishing Denton v. First Interstate Bank of Commerce, 2006 MT 193, 333 M 169, 142 P3d 797 (2006). However, see Graziano v. Stock Farm Homeowners Ass'n, Inc., 2011 MT 194, 361 Mont. 332, 258 P.3d 999, which held that an arbitration provision contained in covenants, conditions, and restrictions (CCRs) was within a sophisticated businessman's reasonable expectations since the businessman, a former chief executive officer of Apple Computer, Inc., had prior experience with arbitration provisions and had notice of the CCRs.

No Improper Reliance on Extrinsic Evidence in Finding of Valid and Enforceable Express 60-Foot Easement for Subdivision: Defendant acquired certain property after an express easement across the property was created by the former owner. Defendant refused to allow the building of an access road across the property, contending that the easement agreement was invalid on several grounds. The District Court examined the agreement and concluded that the easement was valid and enforceable and granted summary judgment for plaintiffs. On appeal, defendant asserted that the District Court erroneously relied on facts outside the agreement, making summary judgment inappropriate, but the Supreme Court affirmed. For purposes of interpreting a writing granting an interest in real property, evidence of the surrounding circumstances, including the situation of the property and the context of the parties' agreement, may be shown so that the judge is placed in the position of those whose language the judge is to interpret. However, to comply with the statute of frauds and the recording system, the writing itself must ultimately stand on its own and meet the formal requirements for granting a property interest. In this case, the District Court was allowed to consider various facts not contained in the easement agreement for purposes of understanding the situation, but the court's analysis of the easement's validity apparently was limited to the face of the agreement, so the court did not erroneously rely on extrinsic facts. The easement agreement satisfied the formal requirements for expressly granting an easement and created a valid 60-foot emergency public access and utility easement that was enforceable against defendant. Additionally, the District Court properly concluded that because there was no dominant tenement, the easement was in gross and could be used by members of the public to travel between the subdivision and the public highway for emergency purposes and to provide utility services. There being no questions of material fact, summary judgment was proper. Broadwater Dev., LLC v. Nelson, 2009 MT 317, 352 M 401, 219 P3d 492 (2009), distinguishing Blazer v. Wall, 2008 MT 145, 343 M 173, 183 P3d 84 (2008). See also Kuhlman v. Rivera, 216 M 353, 701 P2d 982 (1985).

Ambiguous Employment Contract — Question of Parties' Intent Properly Submitted to Jury: West's employment contract contained two different provisions regarding how West would be compensated in the event of termination of employment. The District Court construed the ambiguous clauses against the employer who drafted the contract and submitted the issue to the jury. On appeal by the employer, the Supreme Court examined the contract language and affirmed. The employment agreement was ambiguous on the issue of whether West would be paid trailing commissions or bonuses if West were terminated for cause, so the District Court did not err in ordering that the parties' intent on the issue be submitted to the jury. West v. The Club at Spanish Peaks, LLC, 2008 MT 183, 343 M 434, 186 P3d 1228 (2008), following Eschenbacher v. Anderson, 2001 MT 206, 306 M 321, 34 P3d 87 (2001).

Question Whether Condition Precedent Satisfied and Contract Formed — Remand: The parties negotiated for the purchase of a new vehicle, and the terms of the contract documents set the interest rate at 3.9%. The plain language of the contract was clear that there was no binding contract until the contract terms were accepted by a bank or finance company. A week after negotiations when the bank would not accept the 3.9% rate, the car dealer notified the buyers that they would have to sign new finance papers with a higher annual percentage rate of 4.9%, but the buyers refused. The buyers then sued the dealer, but the District Court compelled arbitration and stayed the proceedings. On appeal, the car dealer asserted that the contract language was not binding to the dealer unless financing was obtained and that the condition precedent applied only to the dealer and not the buyers. The Supreme Court disagreed. The totality of the contract language demonstrated that the condition precedent also applied to the buyers, even though that was not expressly stated. The total sales price and the corresponding finance charge agreed to by the buyers were based on financing at 3.9%, and a change in rate required renegotiation by both parties, so the condition precedent applied to both parties. Because there were questions of disputed fact whether the condition precedent was satisfied and a contract formed, the case was remanded to District Court for further factfinding and discovery. Thompson v. Lithia Chrysler Jeep Dodge of Great Falls, 2008 MT 175, 343 M 392, 185 P3d 332 (2008).

No Wrongful Discharge Claim When Employment for Specific Term: Plaintiff physician signed a 1-year employment contract with defendant medical center that provided that the employment terms could be extended or renewed by mutual agreement in writing. Although the initial contract expired, plaintiff continued to work by oral agreement for 2 more years. The parties then signed an addendum to the initial contract that set an employment expiration date 6 months later. Plaintiff received a letter 5 days before the expiration date, terminating the employment on the expiration date. Plaintiff filed a wrongful discharge suit, alleging that the termination was unlawful. Defendant moved for summary judgment on grounds that because the addendum provided a specific term of employment, plaintiff had no wrongful discharge claim. The District Court granted summary judgment for defendant, and plaintiff appealed, but the Supreme Court affirmed. A claim for relief that is predicated on discharge from employment is barred if the employment is for a specific term under a written contract and that term has expired. In this case, the addendum constituted a ratification of the original agreement that constituted a contract for a specific term of employment, and by executing the addendum, the parties ratified the original agreement calling for employment for a specific term. The fact that the termination date was stated in the contract recitals did not void the date, because the recitals were consideration for the agreement and the parties intended that the recitals be part of the agreement. Plaintiff's argument that because he did not read the addendum he should not be held to its terms was also without merit because one who executes a contract is presumed to know its contents. Stowers v. Community Medical Center, Inc., 2007 MT 309, 340 M 116, 172 P3d 1252 (2007).

Lessor Fully Compensated for Loss of Truck Under Rental Agreement — Agreed Value of Truck Inapplicable to Damage Claim: Plaintiff leased a truck to defendant for construction work. The truck had an agreed value of $250,000 and a rental rate of $12,000 a month. While in defendant's possession, the truck was heavily damaged. Plaintiff initially sought to repair the truck, but eventually it was stripped of usable parts, and the remaining shell was sold for $15,000. Plaintiff received $114,500 from its insurer, based on the insurer's calculation that the truck had a $126,000 cash replacement value minus the $2,500 policy deductible owed to plaintiff by defendant and minus a $9,000 salvage value. Plaintiff then sued defendant for the unpaid balance of the agreed value, including the monthly payments because the agreed value had not been paid. The District Court noted that even though the parties did not have a signed, enforceable, written contract, defendant had properly insured the truck pursuant to a reasonable lease term, identifying plaintiff as beneficiary, and held that defendant had no independent obligation to pay damages beyond the deductible. Because plaintiff had recovered all damages to which it was entitled, judgment was entered for defendant, and plaintiff appealed. The Supreme Court found that the language of the rental agreement did not require the lessee to pay the agreed value if the truck was damaged or destroyed, so defendant was not liable for the agreed value. Plaintiff failed to show the actual replacement cost of the truck and failed to establish that the District Court's finding was clearly erroneous, so the court did not err in holding that plaintiff was not entitled to additional compensation for replacing the truck. Additionally, plaintiff did not demonstrate what additional rental payments were owed, so defendant had no further obligation to pay damages for loss of use. The District Court did not err in holding that plaintiff was fully compensated under the rental agreement, and judgment was affirmed. Performance Mach. Co., Inc. v. Yellowstone Mtn. Club, LLC, 2007 MT 250, 339 M 259, 169 P3d 394 (2007).

Promissory Note Not Considered Contract of Adhesion: Plaintiff read and signed a promissory note to secure a loan for a friend who subsequently went bankrupt. The promissory note provided that plaintiff waived the right to rely on the defense of impairment. Nevertheless, after defendant bank foreclosed on the property that plaintiff used to secure the loan, plaintiff claimed impairment, arguing that the waiver constituted a contract of adhesion that was unenforceable. The District Court disagreed, and plaintiff appealed. The Supreme Court noted that a contract of adhesion is a contract whose terms are dictated by one party to another who has no voice in the contract's formulation and that the contract is unenforceable if it is not within the expectations of the weaker party or if the contract terms are unduly oppressive, unconscionable, or against public policy. Plaintiff was a sophisticated businessman who did not attempt to negotiate the contract terms and who studied the contract prior to signing and thus could not later claim that he was unaware of the waiver provision and that it was not within his reasonable expectations. Although the bank prepared the contract, the transaction was entered solely at plaintiff's behest, and plaintiff voluntarily waived the defense of collateral impairment under 30-3-607. Therefore, the Supreme Court concluded that the promissory note was not a contract of adhesion, nor were the contract's general provisions outside of plaintiff's reasonable expectations. The District Court was affirmed. Denton v. First Interstate Bank of Commerce, 2006 MT 193, 333 M 169, 142 P3d 797 (2006), following Kloss v. Edward D. Jones & Co., 2002 MT 129, 310 M 123, 54 P3d 1 (2002).

Contract Interpretation Applicable to Restrictive Covenants — How Ambiguity Resolved — Restrictive Covenants Strictly Construed: General rules of contract interpretation apply to restrictive covenants, and any person having an interest under a restrictive covenant may seek declaratory relief concerning any question of construction arising under the covenant. When a restrictive covenant has been reduced to writing, the intent of the parties is to be ascertained, when possible, from the writing alone, and when the language of a covenant is clear, a court must apply the language as written. Restrictive covenants are strictly construed, and ambiguities in covenants are resolved to allow free use of property. The determination of whether an ambiguity exists in a restrictive covenant is a question of law for a court to decide, but mere disagreement between the parties as to interpretation of a restrictive covenant does not automatically create an ambiguity. Creveling v. Ingold, 2006 MT 57, 331 M 322, 132 P3d 531 (2006). See also Newman v. Wittmer, 277 M 1, 917 P2d 926 (1996), and Toavs v. Sayre, 281 M 243, 934 P2d 165 (1997).

No Ambiguity in Restrictive Covenant Prohibiting Placement of Trailers and Mobile Homes Upon Property — Development of Recreational Vehicle Park Precluded: A restrictive covenant provided that no trailers or mobile homes were to be placed upon the property conveyed by a deed. The District Court held that the term "placed upon" contemplated permanent placement, and that temporary placement was therefore not precluded. The court also held that the covenant disallowed only trailer houses or mobile homes used for residences. The court thus concluded that the covenant did not disallow development of the property as a campground for recreational vehicles and travel trailers. On appeal, the Supreme Court noted that language in a restrictive covenant should be understood in its ordinary and popular sense. It is not the role of a court to insert modifying language into clearly written and unambiguous written instruments, and the unambiguous language in the covenant contained no words to indicate the parties' intent to allow temporary trailers or mobile homes not used as residences. The District Court erred in modifying the covenant language to allow trailers to be placed on the property, so the conclusion that a campground for recreational vehicles and travel trailers was allowable was reversed. Creveling v. Ingold, 2006 MT 57, 331 M 322, 132 P3d 531 (2006).

Investment Agreement Containing Arbitration Clause Considered Contract of Adhesion — Remand for Consideration of Investor's Reasonable Expectations and Potential Contract Formation Defenses: Zigrang entered an investment agreement with defendant investment company. The agreement contained an arbitration provision. When Zigrang learned that defendant frequently traded securities in Zigrang's account without permission, Zigrang filed a complaint, which was one of 23 suits filed by investors alleging defendant's mismanagement of accounts. Defendant moved to compel arbitration pursuant to the agreement. A panel of three judges sat en banc to hear evidence common to all 23 cases. Defendant's motion to compel arbitration was denied, but the order contained common findings of fact that did not apply to Zigrang, including a mischaracterization of Zigrang's investment agreement. Defendant appealed. The Supreme Court noted that the agreement constituted a contract of adhesion that supported other contract formation defenses, but did not in itself constitute a sufficient basis for invalidating the agreement. The Supreme Court was unable to completely examine Zigrang's contract formation defenses, including unconscionability, waiver, and reasonable expectations, because the District Court's order relied on the mistaken finding of fact. Thus, the court remanded for further findings of fact related to Zigrang's investment agreement, noting that an inquiry into Zigrang's expectations should consist only of an analysis of Zigrang's objectively reasonable expectations regarding the agreement from Zigrang's perspective and that Zigrang's expectations might negate the arbitration provisions. Zigrang v. U.S. Bancorp Piper Jaffray, Inc., 2005 MT 282, 329 M 239, 123 P3d 237 (2005). See also Iwen v. U.S. W. Direct, 1999 MT 63, 293 M 512, 977 P2d 989 (1999), and Kloss v. Edward D. Jones & Co., 2002 MT 129, 310 M 123, 54 P3d 1 (2002).

Interest Owed on State Highway Right-of-Way Condemnation Agreement Pursuant to Clear Language of Stipulation: The Department of Transportation filed a condemnation action against defendants in connection with a highway construction project. As part of the action, the parties entered a stipulation granting the Department possession of the right-of-way in exchange for $35,780, $11,000 payable immediately and $24,780 still owing, plus interest, at 10% a year, on the final award or settlement from the date of service of summons until the date of withdrawal by defendants. A dispute arose over the amount of interest owed. The District Court applied 70-30-302 and determined that the Department owed interest on $7,187 of the total remainder, the amount of land-leveling costs, which the Department paid. Defendants appealed the order, contending that interest was actually owed on the entire $24,780 remaining settlement. The Supreme Court agreed. The language in the stipulation was clear and unambiguous and required the Department to pay interest on the excess of the final settlement award, which was $24,780. The District Court erred in applying the statute to the exclusion of the actual stipulation language to which the parties agreed. The clear language of the stipulation and the intent of the parties controlled. The case was remanded with instructions to order the Department to pay interest on the entire final settlement, with credit for amounts already paid. St. v. Asbeck, 2003 MT 337, 318 M 431, 80 P3d 1272 (2003).

Security Brokerage Contracts — Contract of Adhesion Rendering Arbitration Clause Unenforceable: Kloss opened a full-service brokerage account with defendant, which permitted Kloss to purchase securities and maintain a money market account and which included a living trust account. The account did well, and Kloss decided to set up a charitable trust with the bond proceeds. The initial account and the living trust agreement contained a mandatory arbitration clause, and the charitable trust incorporated the arbitration clause by reference. Kloss then had second thoughts about the charitable trust and petitioned to revoke it. Defendant moved to compel arbitration, and the District Court granted the motion, citing Chor v. Piper, Jaffray & Hopwood, 261 M 143, 862 P2d 26 (1993), and Iwen v. U.S. W. Direct, 1999 MT 63, 293 M 512, 977 P2d 989 (1999), for the holding that defendant had no obligation to explain the terms of the contract because it was within Kloss's reasonable expectations and that even if the contract was considered a contract of adhesion, it was not unenforceable because it was not unconscionable. Kloss appealed, arguing that the arbitration clause was part of a contract of adhesion and that waiver of the constitutional right to jury trial should not be presumed from the signing of a contract of adhesion. Defendant maintained that form contracts prepared by securities brokers are not contracts of adhesion dictated by one party to another who has no voice in its formulation, and that arbitration clauses contained in the contracts are not unconscionable. The Supreme Court examined Passage v. Prudential-Bache Sec., Inc., 223 M 60, 727 P2d 1298 (1986), for an explanation of contracts of adhesion in the securities context and the circumstances under which they are unenforceable. The court distinguished both Chor and Passage, finding that the contracts in this case were clearly contracts of adhesion because they were standardized forms containing terms that Kloss had no opportunity to negotiate if wishing to invest with defendant. Further, the arbitration clause by which Kloss waived the right to access to state courts, the right to jury trial, the right to reasonable discovery, the right to findings of fact based on the evidence, and the right to enforce the law by way of appeal was clearly not within Kloss's reasonable expectations. The arbitration clause was never explained by defendant, and Kloss was not aware of the arbitration provision in the contract. Thus, the District Court committed reversible error when it concluded that the arbitration clause was enforceable. Kloss v. Edward D. Jones & Co., 2002 MT 129, 310 M 123, 54 P3d 1 (2002), followed in Larsen v. W. St. Ins. Agency, Inc., 2007 MT 270, 339 M 407, 170 P3d 956 (2007), with regard to factors to be applied in determining a contract of adhesion.

Dispute Over Contract to Deliver Log Home — No Requirement That Seller Provide Name of Third Party Boom Truck Operator — Rescission Proper Remedy for Material Breach of Contract: Anderson agreed to purchase a log home from Eschenbacher. The home was designed to be constructed on Anderson's homesite. Eschenbacher drafted the purchase contract, which provided that Eschenbacher would act only as a manufacturer, not as a building contractor, and also required Anderson to coordinate and ensure availability of a boom truck to assemble the structure at the site. Anderson contacted a third party to supply a boom truck instead of using Eschenbacher's truck. Eschenbacher then refused to deliver the logs unless Anderson supplied the name of the other boom truck operator. Both parties sued for breach of contract. The District Court concluded that Anderson was under no duty to provide Eschenbacher with the name of the boom truck operator, and the Supreme Court agreed. The contract clearly placed the responsibility for acquiring a boom truck with Anderson, but did not require Eschenbacher to use it, because other language required Anderson to pay any expenses incurred by Eschenbacher for waiting once the logs were delivered, if, for instance, the boom truck that Anderson provided was inadequate. Construing the contract most strongly against the drafter, Eschenbacher, the court found that Eschenbacher could easily have inserted provisions in the contract regarding specifications of an adequate boom truck, but he did not. Eschenbacher materially breached the contract by refusing to deliver the logs until the boom truck dispute was settled. The contract did not specify a remedy; thus, the District Court did not err in granting Anderson rescission of the contract. Eschenbacher v. Anderson, 2001 MT 206, 306 M 321, 34 P3d 87 (2001).

Shareholders' Agreement Enforceable Independent of Stock Exchange — Different Intent Contained in Separate Agreements Separately Enforceable: Following his termination from employment with Bitterroot International Systems, Inc. (Bitterroot), Knutson sought to exercise his buyout rights under the shareholders' agreement. Bitterroot refused to pay, contending that an earlier merger transaction and the subsequent shareholders' agreement should be read together and citing Rumph v. Dale Edwards, Inc., 183 M 359, 600 P2d 163 (1979), for the proposition that when construing an agreement that is part of a larger transaction, the intention of the parties must be determined by examining the entirety of the larger transaction. However, Rumph was distinguishable here because all the agreements in question occurred at different times and did not reference or depend upon each other. Each agreement was clear and unambiguous. Under Gerdes v. Omaha Home for Boys, 89 NW 2d 849 (Nebr. 1958), a court may not avoid the language of a complete, unambiguous contract by consolidating it with another writing if the effect of doing so would be to avoid an essential part of the contract. The District Court properly concluded that the shareholders' agreement was enforceable independent of the stock exchange between the parties. Knutson v. Bitterroot Int'l Sys., Inc., 2000 MT 203, 300 M 511, 5 P3d 554, 57 St. Rep. 800 (2000), followed in O'Brien v. O'Brien, 2022 MT 246, 411 Mont. 101, 532 P.3d 831.

Assignment of Retail Installment Contract — Breach of Warranty — Abrogation of Waiver of Recourse: Arcadia Financial, Ltd. (Arcadia), is a Minnesota corporation that purchases retail installment contracts from automobile dealers, including Prestige Toyota (Prestige) in Billings, after the dealers have entered into installment contracts with automobile buyers. Knight purchased a Toyota from Prestige, and Knight's contract contained a provision assigning the contract to Arcadia under one of four options. The same day that Knight purchased the automobile, Prestige assigned the contract to Arcadia "without recourse", which meant that only the contract warranties applied, one of which was that Prestige had a valid certificate of title and would send it to the appropriate officials within 10 days of sale to ensure Arcadia's interest in the vehicle. The contract also provided that Prestige unconditionally guaranteed full performance of the contract in the event that it breached any of the warranties. Prestige failed to send a valid certificate of title as required. Knight later defaulted and filed for bankruptcy protection. Arcadia demanded that Prestige repurchase the Knight contract. Prestige admitted breaching the warranty but claimed that it was not required to repurchase the contract and refused to do so, asserting that Arcadia's damages were limited to the amount that the bankruptcy trustee received from sale of the automobile. The District Court awarded Arcadia the principal amount due on the Knight contract, plus interest, attorney fees, and costs, concluding that under the clear language of the contract assignment provisions, Prestige had guaranteed payment of all sums due when it failed to deliver the valid title within the time required. The Supreme Court agreed, noting that the contract was converted into a full recourse contract when Prestige failed to deliver the valid title, so Prestige was required to repurchase the contract for the amount of principal remaining due. The detriment proximately caused by Prestige's failure to repurchase the contract was the principal amount owing on the contract. Further, the District Court properly awarded attorney fees to Arcadia as the prevailing party pursuant to 28-3-704. Arcadia Financial, Ltd. v. Prestige Toyota, 1999 MT 273, 296 M 494, 989 P2d 831, 56 St. Rep. 1111 (1999).

Property Description of "2 Acres, More or Less" Not Ambiguous: A property agreement provided that Tract 1 be "2 acres, more or less". Although the phrase "more or less" may not be particularly precise, it is a phrase commonly understood by its plain and ordinary meaning and is not subject to two interpretations. More or less means "approximately", regardless of whether one party would prefer "less", while the other party "more". The property agreement was clear, unambiguous, and enforceable. Schwend v. Schwend, 1999 MT 194, 295 M 384, 983 P2d 988, 56 St. Rep. 754 (1999).

Error in Reliance on Intent Not to Be Bound by Contractual Arbitration Clause: In ruling that arbitration clauses included in securities contracts were invalid, the District Court concluded that one of the parties did not intend that the arbitration clauses would be used in the event that the party was defrauded. Under this section, the intention of the parties is to be ascertained from the writing alone, if possible. The court was in error in relying upon one party's subjective intent not to be bound by the legal consequences of the arbitration clauses contained in the agreement that the party signed. Chor v. Piper, Jaffray & Hopwood, 261 M 143, 862 P2d 26, 50 St. Rep. 1234 (1993).

Improper Modification of Maintenance Awarded "For Life": The District Court modified a property settlement agreement, which provided that the wife receive $300 a month "as maintenance for life" in lieu of property for which she was to receive income, after husband unilaterally discontinued maintenance when wife began receiving social security payments. The maintenance agreement was a plain and unambiguous contract between the parties that was not subject to later interpretation or construction by a court. The agreement was drawn up by husband, a practicing attorney, who clearly understood the meaning of the term "for life". The District Court erred in modifying the agreement, absent a showing of substantial credible evidence that modification was warranted, without considering all necessary information in the original settlement agreement. In re Marriage of McKeon, 252 M 15, 826 P2d 537, 49 St. Rep. 127 (1992), followed in In re Marriage of Woodford, 254 M 501, 839 P2d 574, 49 St. Rep. 887 (1992).

Subordination Agreement — Terms Unambiguous: The District Court did not err in granting summary judgment when it determined that the parties' subordination agreement did not constitute a novation that extinguished the original agreement between the parties. The parties had submitted conflicting affidavits regarding what they intended by the subordination agreement. In this case, it was possible for the District Court to determine the intention of the parties from the terms of the subordination agreement itself, which revealed no genuine issue of material fact and entitled Waite to judgment as a matter of law. Waite v. Andreassi, 249 M 149, 813 P2d 987, 48 St. Rep. 647 (1991).

Enforceability of Clear and Unambiguous Contract Language: When the language of a contract is clear and unambiguous, the contract does not require application of the rules of construction and it is a court's duty to enforce the contract as made by the parties. Keller v. Dooling, 248 M 535, 813 P2d 437, 48 St. Rep. 554 (1991), followed in Consolidated Minerals Corp. v. Madison Gold Mines, Inc., 263 M 6, 865 P2d 1138, 50 St. Rep. 1678 (1993), in which the court erred in terminating the mining contract rather than enforcing valid default provisions.

Policy Unambiguous as to Bodily Injury Coverage: The lower court granted the insurer's motion for summary judgment, stating that the policy only covered bodily injury liability coverage for persons injured by the plaintiff and did not include coverage for his own injuries. The plaintiff contended that he had marked the box indicating he wanted "Full Package", and therefore the policy was ambiguous and should be construed against the insurance company. The Supreme Court affirmed the lower court and held that the policy terms were clear when read as a whole in limiting coverage to those persons injured as a result of the plaintiff's negligence. Erickson v. Dairyland Ins. Co., 241 M 119, 785 P2d 705, 47 St. Rep. 130 (1990).

Contract Provision Unambiguous: A contract among tenants in common stated unambiguously that all decisions regarding the property were to be determined by a majority vote, unless otherwise specified. By signing the agreement, defendant expressly agreed to be bound by a majority vote to sell the property, even though he was not available when the other owners voted to sell and abstained from signing the sale documents. Felska v. Goulding, 238 M 224, 776 P2d 530, 46 St. Rep. 1222 (1989).

Remand of Issue of Legality of Retroactive Designation of Funds as Business Loan: In an action concerning the sale of business property owned by tenants in common, the trial court, acting in equity, awarded each owner a portion of the sale proceeds in proportion to his initial capital investment. The issue of division of the sale proceeds was remanded to the court to make specific findings concerning the designation of certain advancements to the business as loans. Felska v. Goulding, 238 M 224, 776 P2d 530, 46 St. Rep. 1222 (1989).

Assignment of Estate Rights — Certificate of Deposit Held by Surviving Joint Tenant Not Transferred: A $10,000 certificate of deposit (C.D.) held by a surviving joint tenant was properly not included as an asset of the estate; therefore, a transfer and assignment of the tenant's right, title, and interest in the estate did not affect the C.D., of which tenant was sole owner upon the death of the nonsurviving joint tenant. Yellowstone Bank of Absarokee v. Morse, 226 M 126, 733 P2d 1310, 44 St. Rep. 524 (1987).

Insurance Policy Clause Unambiguous: Home owners' insurance policy clause clearly and unambiguously covered only vehicles that met both requirements set forth in the provision. Therefore, the clause was within the general rule that when a contract is reduced to writing, the intent of the parties is ascertained from the writing alone if possible. Payne v. Safeco Ins. Co., 222 M 198, 720 P2d 1197, 43 St. Rep. 1171 (1986).

Issue of Authorship of Agreement Not Precluding Summary Judgment Where Agreement Not Ambiguous: Where the plaintiffs brought an action for default of a mining lease, arguing that summary judgment for the defendants was precluded by the ambiguity of the lease and a dispute as to its authorship, the Supreme Court held that the provisions governing royalty payments were not ambiguous, that authorship was therefore irrelevant, and that summary judgment was properly granted. The plaintiffs' interpretation of the agreement was absurd because that interpretation required payment of royalties before net smelter returns were received or before the royalties themselves could be calculated. The time and method of calculation of payment by the defendants were entirely consistent with the terms of the parties' agreement. Reading the agreement as a whole, there was no factual issue to preclude summary judgment. Lewis v. St., 207 M 361, 675 P2d 107, 41 St. Rep. 9 (1984).

Ambiguous Phrase — Entire Contract to Determine Intent: A coal contract was entered on March 31, 1974. In 1976, the Montana Department of State Lands (functions now transferred to Department of Environmental Quality) determined that Decker was precluded under Title 82, ch. 4, part 2, from disturbing a certain portion of land within the mine area contemplated by the contract. It was conceded this would increase mining costs. The contract contained a price adjustment provision that allowed for price adjustments due to new government regulation. Decker contended the nondisturbance determination was a "new regulation" even though the statute under which the Department acted was enacted in 1973. The court in construing "new regulation" looked to the entire contract to determine mutual intent. The court determined, in light of adjustment provisions for all other cost increases, that "new regulation" meant increases required by government action taken after the effective date of the contract. Austin v. Decker Coal Co., 701 F2d 420 (5th Cir. 1983).

Conflict of Law — Express Contractual Provision Controls: Plaintiff was injured due to a faulty handrail in a missile silo on which he was working. Defendant sought indemnification from the construction company pursuant to a contract between the parties. The contract was executed in Washington and was to be performed in Montana. Under 28-3-102, the contract would be interpreted according to Montana law. However, the contract contained a provision whereby the parties agreed the terms of the contract would be governed by Washington law. When the language of a contract is clear and unambiguous, it is the court's duty to enforce the contract as made by the parties. Therefore, Washington law controlled the issue. Steinke v. The Boeing Co., 525 F. Supp. 234, 38 St. Rep. 1966 (D.C. Mont. 1981).

Landfill Operator to Be Licensed: The appellant had contracted with the refuse board of his county to operate a sanitary landfill. The trial court found that the appellant was required by his contract to obtain a license to operate the landfill. The Supreme Court on review said that when read together, it is apparent that under 75-10-203 and 75-10-221, the County Commissioners, the refuse board, or the appellant could be proper applicants for the landfill license. Finding no exemption from the obligation to seek the required license, it was a question of the parties' contract requirements. The Supreme Court declined to find that 75-10-112 requires all local governments to obtain the requisite license for operation of a disposal site when the operations by contract are to be performed by another individual. Citing 28-3-301 and this section and noting that the language in the contract here was clear and unambiguous, the Supreme Court found its duty to enforce the contract as made. The license requirement imposed by 75-1-221 was clearly applicable to the operation of the disposal site. Therefore, the appellant was required by the terms of the contract to obtain the operator's license. Ryan v. Bd. of County Comm'rs, 190 M 273, 620 P2d 1203, 37 St. Rep. 1965 (1980).

Intent Irrelevant if Agreement Clear and Specific — Subordination: Summary judgment is correct when subordination agreement does not present an issue of fact. The plain and clear meaning of the instrument controls, and the intent of the parties is ascertained from the instrument. Batey Land & Livestock Co. v. Nixon, 172 M 99, 560 P2d 1334 (1977).

Insurance Contract: Evidence that defendant had not purchased an endorsement which was available upon payment of additional premium was not admissible to show the intention to exclude such coverage from the insurance contract where policy provisions were not ambiguous. Safeco Ins. Co. v. Munroe, 165 M 185, 527 P2d 64 (1974).

Nature of Instrument — Condition and Object of Parties: To ascertain the intention of a written agreement, regard must be had to the nature of the instrument itself, the condition of the parties executing it, and the objects which they had in view. Kintner v. Harr, 146 M 461, 408 P2d 487 (1965).

Condemnation Proceedings: Although negotiation file showing value state placed on one adjoining parcel of land was admitted into evidence in condemnation proceedings, this did not warrant the admission of two different files showing further litigation after purchase since, while section 93-401-11, R.C.M. 1947 (since repealed), allows adverse parties to inquire into the whole matter surrounding a writing, inquiry into intent is limited by this section and 28-2-905. St. Highway Comm'n v. Churchwell, 146 M 52, 403 P2d 751 (1965).

Intention — How Determined Generally: In interpreting a written contract, the intention of the parties must be ascertained from the writing alone if possible and resort to extrinsic evidence in aid of interpretations may be had only when the contract appears on its face to be ambiguous or uncertain. Hill Cattle Corp. v. Killorn, 79 M 327, 256 P 497 (1927). See also Glacier Campground v. Wild Rivers, Inc., 182 M 389, 597 P2d 689 (1978).

Bilateral or Unilateral Contract: Whether a contract is bilateral or unilateral depends upon the intention of the parties and when in writing, the intention is to be ascertained from the writing alone, if possible; otherwise the usual rules of construction must be applied to ascertain it. Wandell v. Johnson, 71 M 73, 227 P 58 (1924).

Clear Contract: Evidence of custom is never competent when the contract is clear and explicit in its terms and the necessity for interpretation does not arise. Under these circumstances the intention of the parties is to be ascertained from the writing itself without resort to evidence. Wheeler v. James, 70 M 37, 223 P 900 (1924).

Entire Agreement Determines Intention: A contract must receive such interpretation as will give effect to the intention of the parties at the time of contracting, the intention to be gathered from the entire agreement, its substance rather than its form being controlling. Ferry & Co. v. Forquer, 61 M 336, 202 P 193, 29 ALR 642 (1921).

Interpretation: Where parties to a contract have expressed themselves in the instrument clearly and without ambiguity, it can readily be found afterward, merely by referring to the instrument, whether either party had committed a breach; but where the instrument contains terms or expressions of doubtful import, the necessity for interpretation arises before the instrument can be resorted to for ascertaining the fact of breach. Lehrkind v. McDonnell, 51 M 343, 153 P 1012 (1915).

MISCELLANEOUS

Surrogacy Contract — Express Written Contract Limited to Clear and Unambiguous Terms — Contract Did Not Preclude Subsequent Establishment of Parental Interest Under Montana Law Not Based on Fact of Surrogacy. Sayler v. Yan Sun, 2023 MT 175, 413 Mont. 303, 536 P.3d 399.

Recision of Easement Agreement Based on Material Breach — Award of Attorney Fees and Costs Proper: The parties were neighbors who had entered into an easement to allow the defendants to cross the plaintiffs' property to access their property. After the defendants exceeded the scope of the easement by hunting on it without permission, the plaintiffs rescinded the agreement. However, the defendants continued to use the easement. The plaintiffs then filed a declaratory judgment action to declare the recision proper. The defendants claimed that provisions in the easement agreement were unconscionable and therefore void. At trial, the District Court held that the defendants had materially breached the agreement and granted the plaintiffs summary judgment and awarded fees and costs. On appeal, the Supreme Court affirmed the grant of summary judgment based on the material breach of the agreement and the fee award. Peters v. Hubbard, 2020 MT 282, 402 Mont. 71, 475 P.3d 730.

No Duty to Recover Funds Under Contract — No Breach of Contract or Covenant of Good Faith and Fair Dealing — Statute of Limitations for Equitable Relief Expired: The plaintiff contracted with Bancard Services, Inc. (Bancard), one of the defendants, for Bancard to provide processing services to the plaintiff's ATMs located throughout Montana. Bancard subcontracted with a third-party payment processor to assist in processing transactions, and an agent of the third party made a data entry error that transferred $285,000 of the plaintiff's funds to an out-of-state individual, Leland Ruzicka, and B&B Lounge (collectively Ruzicka), also defendants in the case. Bancard was able to recover all but $35,000 of the plaintiff's funds. Eventually, the plaintiff sued both Bancard and Ruzicka for the outstanding $35,000. The plaintiff also filed several contractual related claims against Bancard. The District Court granted summary judgment to the defendants because Bancard did not have an obligation to recover the funds under the parties' contract and because the statute of limitations had expired on the unjust enrichment claims against Ruzicka. Grizzly Sec. Armored Express, Inc. v. Bancard Serv., LLC, 2016 MT 287, 385 Mont. 307, 384 P.3d 68.

Lack of Express Utility Easements Not Condition Adversely Affecting Title: The buyer of condominium units refused to close on the sale because the sale agreement did not expressly state the existence of utility easements for each parcel. The District Court determined that the lack of express utility easements was not a condition that adversely affected title and held that the buyer breached the contract by refusing to close the sale. On appeal, the Supreme Court affirmed. The entire property was part of the sale, including all units and appurtenances. If the buyer wanted each unit to have a stated right to access the utility areas, the buyer could affirmatively grant that right to each unit after acquiring the property. Also, the buyer could have required the express establishment of the easements in a written addendum to the contract to be a condition precedent to closing, but the buyer did not do so. The buyer failed to establish that the absence of individual unit easements was an adverse condition of title that allowed the buyer to refuse to close the sale. Apple Park, L.L.C. v. Apple Park Condominiums, L.L.C., 2008 MT 284, 345 M 359, 192 P3d 232 (2008).

Ambiguity of Contract Raising Genuine Issues of Fact — Summary Judgment Improper: In a dispute over the sale of aircraft, the District Court considered summary judgment motions from both parties, granted summary judgment for plaintiff on claims of breach of contract and express warranty, and denied defendant's summary judgment counterclaim of breach of contract and express warranty. The Supreme Court examined the contract and found ambiguities regarding whether defendant accepted the aircraft "as is" at signing or maintained the right to inspect and reject the aircraft prior to closing, as well as the parties' extension of the closing date. The ambiguities raised genuine issues of material fact regarding breach of contract and express warranty that were not appropriate for summary judgment, and the Supreme Court reversed for trial on the issues. Corporate Air v. Edwards Jet Center, Mont., Inc., 2008 MT 283, 345 M 336, 190 P3d 1111 (2008).

Tort Claims Not Precluded by Contract Claims Arising From Same Event: In a dispute over the sale of aircraft, the District Court considered summary judgment motions from both parties and granted defendant summary judgment on plaintiff's tort claims on grounds that plaintiff had relied on a contract theory of relief and thus elected to be made whole under the contract. Plaintiff appealed on grounds that tort liability can exist with contract liability and that recovery on a contract theory does not necessarily preclude recovery on tort theories such as fraud. Defendant responded that summary dismissal of the tort claims was proper because plaintiff should not be allowed to make a double recovery and that because plaintiff's claims were commercial, tort damages are not available except in rare cases when a separate tort claim arises from the contractual relationship. Without ruling on the validity of the tort claims, the Supreme Court held that consideration of plaintiff's fraud-based claims was not precluded by the fact that plaintiff also made separate contract claims arising out of the same event. The tort claims were required to be considered individually and could not be dismissed under a blanket rationale that the tort claims and contract claims were mutually exclusive. The District Court's summary judgment was reversed, and the issue was remanded for further consideration. Corporate Air v. Edwards Jet Center, Mont., Inc., 2008 MT 283, 345 M 336, 190 P3d 1111 (2008).

Total Compensation in Condemnation to Include Value of Condemned Property and Severance Damages: The city of Whitefish condemned 7,234 square feet of plaintiff's property, but conveyed to plaintiff 10,175 square feet of city property contiguous to plaintiff's lot. The conveyance was intended as severance damages to offset the harm of condemnation. The parties entered an agreement that plaintiff would grant possession of the condemned property to the city and that the city would pay plaintiff $130,000 to convey the 10,175 square foot adjacent lot. The agreement also stated that the parties were unable to agree on the value of the condemned property, the severance damages to plaintiff's remaining property, and the value of the conveyed property. Eventually plaintiff filed a complaint for inverse condemnation and breach of the agreement when the parties were unable to agree on the property values and severance damages. The District Court held that the only issue for the jury was to determine the amount that plaintiff was entitled to for compensation, and the jury was not asked to determine any severance damages owing to plaintiff. The court also disallowed any evidence of the $130,000 payment because that money was considered for severance damages only and could not be considered by the jury in determining plaintiff's compensation for the condemned property. The court further disallowed the city from presenting any evidence regarding the conveyed property because it had not yet been deeded to plaintiff, and absent unity of ownership, the conveyed property could not be considered when determining the fair market value of plaintiff's remaining property after the condemnation. Last, the court determined that plaintiff's "cost-to-cure" damages were noncompensable because plaintiff's access remained the same after condemnation. During trial, various experts presented differing values for the condemned property. The jury ultimately found for plaintiff and held that the city owed $161,000 for the condemned property. The District Court also awarded plaintiff $94,788.23 as litigation expenses. The city appealed, and plaintiff cross-appealed. The Supreme Court held that the District Court misinterpreted the agreement and improperly limited the issues presented to the jury. The court noted that total compensation in an eminent domain case involves both the value of the condemned property and severance damages, including depreciation suffered as a result of condemnation. In order for the jury to consider all circumstances surrounding the condemnation, a new trial was required, so the case was reversed and remanded. K&R Partnership v. Whitefish, 2008 MT 228, 344 M 336, 189 P3d 593 (2008).

Arbitration Provision in Adhesive Contract Enforceable — Noncompetition Clause Within Weaker Party's Reasonable Expectation: Larsen asserted that an employment contract containing a noncompetition clause was a contract of adhesion and that the arbitration clause in the contract was unenforceable. The Supreme Court applied the factors in Kloss v. Edward D. Jones & Co., 2002 MT 129, 310 M 123, 54 P3d 1 (2002), and determined that the contract was indeed adhesive. However, simply being adhesive does not render a contract invalid and unenforceable under Kloss. The contract must also either fall outside the weaker party's reasonable expectation or be unconscionable. In this case, Larsen had 20 years' experience in the insurance industry and had entered various similar employment agreements that contained arbitration clauses during those years, and the arbitration provision was stated in bold letters on the first page of the agreement. These facts constituted sufficient grounds to support the conclusion that the arbitration clause fell within Larsen's reasonable expectations and was therefore enforceable. However, once the District Court determined the validity of the arbitration clause, the court exceeded its authority in deciding additional substantive issues under the agreement that should have been decided by an arbitrator, so the case was remanded for arbitration. Larsen v. W. St. Ins. Agency, Inc., 2007 MT 270, 339 M 407, 170 P3d 956 (2007), following Martz v. Beneficial Mont., Inc., 2006 MT 94, 332 M 93, 135 P3d 790 (2006).

Easement Limited to Historical Size and Location of Grant: In 1949, plaintiffs' predecessor in interest granted an easement to defendant's predecessor in interest to allow the construction of radio towers on a portion of a 160-acre parcel, conditioned on location and maintenance of the property. Defendant subsequently notified plaintiffs that he intended to expand the radio facilities beyond the original construction site. Plaintiffs sued, asserting that the expansion would encompass property not included in the original grant, while defendant contended that the easement encompassed the entire 160 acres described in the grant, so the facilities could be expanded onto other portions of the parcel or relocated elsewhere within the parcel. The District Court found for plaintiffs, and on appeal, the Supreme Court affirmed. Under the rules of contract construction, the grant language clearly limited placement of the radio facilities on a portion of the 160-acre parcel to be chosen by defendant's predecessor in interest. Thus, the easement did not encumber the full 160-acre parcel, but rather was limited in size and location to the historical location of the radio facilities. The original grant also required that wires, ground radial antennas, conduits, and transmission lines be buried to a minimum depth of 12 inches, and the District Court did not err in ordering defendant to bury the equipment pursuant to the maintenance portion of the grant. Anderson v. Stokes, 2007 MT 166, 338 M 118, 163 P3d 1273 (2007).

Objective Determination of Whether Ambiguity Exists in Contract — Ambiguity Not Created by Disagreement Over Interpretation of Contract Language: The determination whether an ambiguity exists in a contract is made on an objective basis. A conclusion of ambiguity is not compelled by the fact that parties to a document, or their attorneys, have or suggest opposing interpretations of a contract or even disagree as to whether the contract is reasonably open to just one interpretation, nor does ambiguity exist just because a claimant says so. Rather, an ambiguity exists only if the language is susceptible to at least two reasonable but conflicting meanings. In the present case, plaintiffs' backup position was that language in a right-of-way contract was ambiguous, but the three circumstances proffered by plaintiffs, even when considered collectively, did not demonstrate that the contract language was susceptible to at least two reasonable but conflicting meanings. Thus, the trial court did not err in concluding that the language was unambiguous, which was in fact plaintiffs' primary position. Mary J. Baker Revocable Trust v. Cenex Harvest

St., Cooperatives, Inc., 2007 MT 159, 338 M 41, 164 P3d 851 (2007), followed in Wills Cattle Co. v. Shaw, 2007 MT 191, 338 M 351, 167 P3d 397 (2007).

Right-of-Way Contract Granting Language Unambiguous — Summary Judgment Proper: The District Court found that language in a right-of-way contract: (1) granted defendants an easement to bury a fiber optic cable on plaintiffs' land together with a pipeline; (2) did not limit use of the cable to operating and monitoring the pipeline; and (3) gave defendants the right to assign any of their rights, in whole or in part, to any third party. The language was unambiguous, and the court correctly applied the language as written and properly granted summary judgment to defendants. Mary J. Baker Revocable Trust v. Cenex Harvest St., Cooperatives, Inc., 2007 MT 159, 338 M 41, 164 P3d 851 (2007).

Buy-Sell Agreement Not Subject to Financing Contingency Absent Specific Contractual Funding Language: A buy-sell agreement stated that the buyer had sufficient funds to close the sale of a ranch and was not relying upon any contingent source of funds unless otherwise stated in the agreement, but there was no third-party financing specified in the agreement. Nevertheless, when the buyer was not able to close the sale for lack of funds, both parties sought to recover the earnest money, and the buyer asserted that the contract language was clear and unambiguous in conditioning the sale on financing. The District Court disagreed, and on appeal, the Supreme Court concurred. The buyer represented that it had sufficient funds, and nowhere in the agreement or in an addendum extending the closing date was it specified that completing financing meant that the buyer had to obtain a loan from a third party. The District Court's award of the earnest money to the seller was affirmed. Sec. Abstract & Title Co. v. Smith Livestock, Inc., 2006 MT 265, 334 M 172, 146 P3d 732 (2006).

Failure of Teacher to Exhaust Grievance Procedures Required Under Unambiguous Contract — Estoppel Inapplicable Absent Factual Representation of Material Fact — Summary Judgment Proper: When Wurl's speech-language pathology contract was not renewed, Wurl brought an action against the school district alleging that termination procedures were not followed pursuant to a collectively bargained master agreement and also brought claims for wrongful discharge and due process violations. The parties disagreed whether the master agreement applied because Wurl was not certified. The District Court found that the master agreement did not apply and granted summary judgment to the school district, and Wurl appealed. The Supreme Court found that the language of the employment contract unambiguously incorporated the entirety of the master agreement by reference, so the District Court erred in holding otherwise. Wurl also contended that because the District Superintendent had stated that the master agreement did not apply, collateral estoppel should bar the district from asserting that Wurl failed to go through the collectively bargained grievance procedure. On this point, the Supreme Court disagreed. The superintendent's statement was a legal interpretation rather than a factual representation of a material fact, so Wurl failed to prove the first required element of collateral estoppel, and the district was therefore allowed to argue that Wurl's claims should be barred by failure to exhaust the grievance procedure. Because the master agreement applied and Wurl failed to implement the mandatory grievance procedure, Wurl's claims were barred. The Supreme Court affirmed the summary judgment. Wurl v. Polson School District No. 23, 2006 MT 8, 330 M 282, 127 P3d 436 (2006), following Elk Park Ranch, Inc. v. Park County, 282 M 154, 935 P2d 1131 (1997).

Justifiable Cause to Terminate Contractual Relationship — No Breach of Contract or Tortious Interference With Business Relations: In 2000, optometrist Hardy enrolled as a Vision Service Plan (VSP) member with defendant. The agreement provided for automatic annual renewal unless either party terminated the agreement, or VSP could terminate the agreement at any time if Hardy failed to comply with VSP policies, rules, and procedures. One condition for continued membership was that the member maintain majority ownership and complete control of all aspects of the optometric practice. Unbeknownst to VSP, Hardy had previously entered a franchise agreement with another optical supplier that contravened certain provisions of the VSP agreement, so VSP terminated Hardy's agreement. Hardy sued VSP, alleging breach of contract and tortious interference with Hardy's business relations. The District Court granted summary judgment to VSP, and Hardy appealed, but the Supreme Court affirmed. Hardy had no justifiable expectation of a continued contractual relationship with VSP after breaching VSP's policies. The VSP agreement was unambiguous as a matter of law, and VSP had just cause to terminate the agreement based on Hardy's actions in enrolling as a franchisee with another company on terms that violated the VSP agreement. Hardy's tortious interference claim also failed absent evidence that VSP unlawfully engaged in activities to damage Hardy's business. Summary judgment for VSP was proper. Hardy v. Vision Serv. Plan, 2005 MT 232, 328 M 385, 120 P3d 402 (2005).

Reservation of Single Right-of-Way Over Existing Private Road — No Ambiguity or Conflict With Intended Access: The District Court determined that a reservation of rights in a 1965 deed was ambiguous because the reservation of rights over a single roadway conflicted with the grantors' intent to reserve as many means as possible to their remaining property in a mountainous area. Ambiguities in a reservation of rights in any grant of property are to be construed in favor of the grantor; however, the breadth and scope of an easement are determined upon the actual terms of the contract. The easement in this case was described as "a right of way" over "an existing private road which extends across" the servient tenement "for the use and benefit of Section 3 and [parts] of Section 34". That language indicated the use to which the easement would be put, not the scope of the easement itself. The Supreme Court found that the reservation of rights was not ambiguous; rather, the language restricting the easement to a single right-of-way over an existing private road did not conflict with the intended use of the easement to benefit the grantors' remaining properties, nor did the grantors' intent override any limitation of the singular use of the word "road" in the reservation. Van Hook v. Jennings, 1999 MT 198, 295 M 409, 983 P2d 995, 56 St. Rep. 767 (1999).

Adjusting Appraised Value to Enforce Agreement Proper: On appeal of an order granting specific performance of a settlement agreement between the parties to a dispute over operation of a family farm, Hass claimed that the District Court had erred in finding the value of the farm corporations to be higher than that agreed upon by the appraisers appointed by the parties. The Supreme Court affirmed, ruling that since a court has a duty to enforce an agreement that is clear, as this one is, it was proper for the District Court to increase the appraised value by the value of debts owed to the corporations by the parties. Hass v. Hass Land Co., 217 M 246, 704 P2d 63, 42 St. Rep. 1170 (1985).

Responsibility for Accounts Payable Following Default in Sales Contract: Eight months after buyer and sellers entered into a contract for the sale of sellers' business, buyer defaulted and, pursuant to the contract, sellers reassumed possession of the business. The parties agreed that the assets of the business reassumed by the sellers included the accounts receivable, but they disagreed on who was responsible for the accounts payable. The District Court ruled that the sellers assumed the accounts payable, agreeing with the buyer's theory that accounts receivable and accounts payable were analytically indivisible in a determination of which party had assumed the accounts of the business. The Supreme Court affirmed. Heine v. Seibert, 217 M 224, 703 P2d 865, 42 St. Rep. 1152 (1985).

Commission Agreement Found Unambiguous — Use of Extrinsic Evidence to Prove Lack of Ambiguity Upheld: Where the defendant seller of real estate made a commission agreement with the plaintiff providing for payment of the commission out of the receipts from the contract for deed, the District Court did not err in holding that money received by the defendant under a modification of the contract for deed could not be used to calculate the amount of commission owed to the plaintiff. The terms of the commission contract were not ambiguous and show that it was the intent of the parties to count only that money received under the original agreement. The District Court properly looked to the terms of the contract for deed only to determine whether an ambiguity existed in the commission agreement, and having determined there was none, properly excluded other evidence of the parties' intent in making the commission agreement. Martin v. Community Gas & Oil Co., 205 M 394, 668 P2d 243, 40 St. Rep. 1385 (1983).

Time of Mortgage Payments — Where Contract Silent as to Time of Day: According to the terms of the mortgage, monthly payments were to be made no later than 30 days after due date or mortgagor could be declared in default. Mortgagor deposited payment in escrow account after 3 p.m. on the 30th day, a Friday. Because of the time of the deposit, the escrow account was not credited until the 33rd day, the following Monday. The District Court ruled that the mortgage contract had not been breached since contract provided simply for deposit by 30th day and did not require that deposit be made by a particular time of day. The Supreme Court affirmed, ruling that for the District Court to have found in mortgagee's favor, it would have had to rewrite the contract, and this would have been improper. First Bank-Southside Missoula v. Sadler, 199 M 323, 649 P2d 454, 39 St. Rep. 1428 (1982).

"Owned Automobile" Coverage as Controlling "Regular Use" Provision in Insurance Policy: The liability coverage of an insurance policy issued to a partnership and the individual partners extended to any "owned automobile", which was defined as any automobile owned by the partnership. The endorsement covering the individual partners as insureds provided that coverage afforded to them would be the same as that afforded to the partnership. Liability coverage was extended to an automobile which was owned by one of the individual partners but which was not listed on the policy, and the "regular use" provision in the "drive other cars" clause

of the policy did not defeat the coverage, even where the driver was the partner's teenage son. USF&G Co. v. Newman, 656 F2d 457 (9th Cir. 1981).

Language Plain and Unambiguous — Language Controls — Nothing to Interpret or Construe: In a dispute involving a real estate listing contract where the contract was plain and unambiguous, 1-4-102 is irrelevant. When the language is plain and unambiguous, the language alone controls and there is nothing for the court to interpret or construe. Section 1-4-102 applies when an ambiguity exists in the language of the contract. Payne v. Buechler, 192 M 311, 628 P2d 646, 38 St. Rep. 799 (1981), clarified in Mary J. Baker Revocable Trust v. Cenex Harvest St., Cooperatives, Inc., 2007 MT 159, 338 M 41, 164 P3d 851 (2007).

Property Settlement Agreement: The property settlement agreement between Molly and Keith Herrin contained a qualified assignment of stocks to Molly Herrin. The agreement said that if Keith, Jr., died while there was any money or property in any trust, then the trust will cease and all property and income of the trust will revert to Keith Herrin and become his sole property. Keith, Jr., died, but no trust existed since a trust was to be established only if Molly died or remarried during Keith, Jr.'s lifetime. Neither of these events occurred. The Supreme Court found that the stocks belonged to Molly after the death of Keith, Jr. Herrin v. Herrin, 182 M 142, 595 P2d 1152 (1979).

Term of Lease Modified: When an agricultural lease containing a provision for automatic renewal was modified to extend the original term of the lease, the modification constituted a new agreement as to the term of the lease, thus abrogating the automatic renewal provision; the lessee was rendered a holdover tenant upon expiration of the term of the lease, as modified. Nevala v. McKay, 178 M 327, 583 P2d 1065 (1978).

When Damage Award Exceeds Contract: When the terms of a cattle-fattening contract did not include payment for construction of capital items, an award of damages including such a charge was improper. Olson v. Carter, 175 M 105, 572 P2d 1238 (1977).

Unambiguous Contract — No Restriction on Use by Life Tenant: Court erred in imposing a restriction on the use of premises when life tenant was granted the right to use premises "as he may deem fit". Danielson v. Danielson, 172 M 55, 560 P2d 893 (1977).

Reinsurance Contract: Where amended agreement between automobile insurer and reinsurer was the same as that contained in prior agreement, which the parties had interpreted as contended for by the insurer, findings that agreement was ambiguous and that the parties did not intend to give the words in the amendment a different meaning than that given in the agreement, being supported by substantial evidence, warranted judgment in favor of insurer. Peerless Cas. Co. v. Mtn. States Mut. Cas. Co., 283 F2d 268 (9th Cir. 1960).

Reference to Other Contracts: A contract will not be held to incorporate stipulations embodied in another contract save insofar as the same are specifically set forth or identified by reference. St. Bank of Darby v. Pew, 59 M 144, 195 P 852 (1921).

Third Person Appending His Name to Contract: Where a contract is signed by the parties thereto and a third person, not a party to the contract, appends his name under the other signatures preceded by the words "I hereby consent to the above contract", he is not bound beyond his engagement so expressed. Henry O. Shepard Co. v. Freeman, 40 M 144, 105 P 484 (1909).

28-3-304. When writing disregarded.

Case Notes

Request for New Beneficiary Not Appropriate Use of Reformation — Summary Judgment Properly Granted to Stepson: Reformation does not permit the court to create an entirely new contract. In this case, the petitioner asked the court to name her as an entirely new beneficiary, which would be a substantial addition resulting in a new contract. This request went beyond what is permitted by way of reformation. Section 28-3-304 governs the interpretation of contracts, not their reformation, and was properly applied here; however, the standard for disregarding a writing contained in 28-3-304 was not met because the evidence showed the decedent intended to list his estate as his contingent beneficiary, so the District Court properly granted summary judgment to the decedent's stepson. In re Estate of Irvine, 2013 MT 271, 372 Mont. 49, 309 P.3d 986.

Purchase Money Mortgages — Reformation: The bank prepared a mortgage from the buyer to the sellers and a deed of trust from the buyer to the bank as a service to and at the request of the buyer and the sellers. The bank inadvertently inserted the term "no exceptions" into the mortgage through a typographical error. Upon default of the buyer, the sellers filed an action for declaratory ruling that their purchase money mortgage was prior in time and right to the bank's deed of trust. The trial court reformed the sellers' mortgage to delete the term "no exceptions" and held that the bank's deed of trust was prior in time and right to the mortgage. The Supreme Court affirmed. The bank's mistake, while negligent, did not amount to neglect of a legal duty that would preclude reformation. The mistake was mutual because the mortgage as written did not reflect the mutual intentions of the parties which, the evidence indicated, were for the bank to receive a first mortgage and the sellers to receive a second mortgage. Pulse v. N. Am. Land Title Co. of Mont., 218 M 275, 707 P2d 1105, 42 St. Rep. 1578 (1985).

Sufficiency of Pleadings and Proof: The defendant sold real estate to plaintiff on a contract for deed, and the District Court reformed the contract, finding fraud by defendant in orally misrepresenting that there were three good wells on the property, that ownership of a cabin on the property would transfer with the property, and that he would survey or provide papers concerning the boundary of the property. The Supreme Court reversed, finding no basis for fraud in that: (1) the water in the wells had never been tested and proven unfit for use, and the lack of pumps on two wells was obvious from visual inspection at the time the contract was entered; (2) plaintiff had, on a verified complaint, in fact acknowledged defendant's continuing ownership of the cabin, contrary to her testimony and the District Court's finding; and (3) plaintiff never alleged that a survey was to be performed, contrary to the District Court's finding, and plaintiff could have easily ascertained the boundaries by looking at an existing survey and talking with a neighbor. Krone v. McCann, 197 M 380, 642 P2d 584, 39 St. Rep. 500 (1982).

Writing to Control: Where parties called their relationship to a piece of equipment that of lessor and lessee, and lessee was obligated to pay all charges for both the delivery and return of the equipment upon termination or expiration of the lease, pay all maintenance, carry insurance, pay all taxes, and title remained in the lessor, and the instrument defining their relationship was entitled a lease, there was such overwhelming evidence that the arrangement was a lease, and not a contract of sale, that it was error for the trial court to find the latter. Am. Mach. Co. v. Johnson, 157 M 226, 483 P2d 921 (1971).

Extrinsic Evidence: Where defendant charged with grand larceny by bailee did not deny that he received a check from the complaining witness, but his defense was that it was a loan instead of a payment for an automobile, evidence as to whether the check was a loan or payment for the automobile was admissible over objection that it permitted a witness to vary a written instrument by parol testimony. St. v. Ahl, 140 M 305, 371 P2d 7 (1962).

Power to Reform Where Mistake Exists:

This statute does not preclude the trial court from reforming an instrument which by reason of mistake or fraud fails to set forth the correct intentions of the parties. Carroll v. Funk, 222 F2d 508 (9th Cir. 1955).

Section 28-2-1611 provides for the reformation of instruments on the ground of the mutual mistake of the parties. This section declares that when through mistake a written contract fails to express the real intention of the parties, such intention is to be regarded and the erroneous part of the writing disregarded. A court of equity under its inherent power and this section may grant reformation of a deed evidencing a voluntary conveyance even though the mistake was not mutual. Laundreville v. Mero, 86 M 43, 281 P 749 (1929).

Before equity will intervene to correct an alleged mistake in a written instrument, the evidence of the mistake must be clear, convincing, and satisfactory. Humble v. St. John, 72 M 519, 234 P 475 (1925).

Fraud: The parol evidence rule under which, in civil actions, oral testimony is inadmissible to vary the terms of a written instrument has no application in a criminal case involving fraud, where the State seeks by parol testimony to negative the existence of an alleged contract. St. v. Lund, 93 M 169, 18 P2d 603 (1932).

28-3-305. Contract restricted to its apparent objects.

Case Notes

Surrogacy Contract — Express Written Contract Limited to Clear and Unambiguous Terms — Contract Did Not Preclude Subsequent Establishment of Parental Interest Under Montana Law Not Based on Fact of Surrogacy. Sayler v. Yan Sun, 2023 MT 175, 413 Mont. 303, 536 P.3d 399.

Evidence of Circumstances Under Which Instrument Made Admissible for Determining Ambiguity: As a general rule, evidence of the circumstances under which an instrument was made may not be considered when the language of the instrument is clear and certain in its terms. However, objective evidence of those circumstances, including the situation of the subject of the instrument and the parties to it, may be shown and considered to aid the court in determining, as a preliminary matter, whether the instrument contains an ambiguity. If the court determines that no ambiguity exists, then the extrinsic evidence may not be considered further, but if the court determines that an ambiguity is present in the instrument, then the extrinsic evidence may be introduced at trial to allow the trier of fact to determine the intent of the parties in entering into the contract. In the present case, both parties agreed that language in a right-of-way contract was unambiguous, so the trial court did not err in refusing to consider the circumstances under which the contract was made. Mary J. Baker Revocable Trust v. Cenex Harvest St., Cooperatives, Inc., 2007 MT 159, 338 M 41, 164 P3d 851 (2007). See 11 Williston on Contracts, 33:39 (4th Ed. 1999).

Tenant's Estate in Land — Tenant's Share in PIK Benefits: An oral lease granted two-thirds of crops grown to the tenant Popp. The land was later included in the federal payment in kind program (PIK), but in the absence of a written lease, the payments were made to landlords Frank and Gountanis rather than to Popp. The District Court awarded two-thirds of the PIK benefits to Popp. On appeal, Frank questioned whether a lease which required a percentage of crops to go to the tenant but which did not contemplate later federal benefits required the tenant to share in those benefits when the fruits of his labor did not create any entitlements under the federal program. The Supreme Court, in affirming the award, held that Popp had an estate interest in the land for the duration of his tenancy and that the award to Frank and Gountanis was in derogation of Popp's interest. Popp v. Gountanis, 221 M 267, 718 P2d 340, 43 St. Rep. 801 (1986).

Error to Deny Jury Trial on Plaintiffs' Claims for Breach of Contract — Interpretation: Appellants, as developers, entered into subdivision improvement agreement with respondent city. The court held that it was error for trial court to deny appellants a jury trial on their claims for breach of contract based on allegations that the parties either failed to attach like meanings to the word "crossing" (to be installed over a city drain) or, alternatively, that the crossing to be constructed under SID is not comparable to the one contemplated by the parties at time of entering agreement. If, as here, contract term is ambiguous, intention of parties is left to jury. A claim of differing uses of the word "crossing" puts the existence, as well as meaning, of the present contract at issue for a jury determination. Gray v. Billings, 213 M 6, 689 P2d 268, 41 St. Rep. 1910 (1984).

Harvesting of Crops: Where plaintiff and defendant entered into an oral contract whereby plaintiff was to harvest and haul defendant's crops upon notice by defendant with five combines, and after notice plaintiff delayed in harvesting the wheat and then only started with one combine, and as a result, standing wheat was damaged by storm, the defendant on counterclaim could not recover for such loss since the court held that the parties did not contemplate that the plaintiff was to be an "insurer against acts of God". Richardson v. Crone, 127 M 200, 258 P2d 970 (1953). (See, however, dissenting opinion in which the judge feels that the evidence did show that that was contemplated, 127 M 200, 258 P2d 970 (1953).)

Intention of Parties: A contract must receive such an interpretation as will make it lawful, operative, definite, reasonable, and capable of being carried into effect; it may be explained by reference to the circumstances under which it was made and the matter to which it relates and, however broad may be its terms, it extends only to those things concerning which it appears that the parties intended to contract, particular clauses being subordinate to its general intent. Custer v. Missoula Pub. Serv. Co., 91 M 136, 6 P2d 131 (1931).

28-3-306. Interpretation of terms that are ambiguous or intended in different sense by different parties.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

District Court Incorrectly Determined Plain Language of Subdivision Covenant Unambiguous — Related Documents Constituting Instrument Not Reviewed — Negative Easement — Ambiguity Interpreted Against Drafter Not Dispositive — Disputed Facts Whether County Acted Arbitrarily or Capriciously — Doctrine of Impossibility or Impracticality Not Applicable — Attorney Fees Award Reversed. Lewis & Clark County v. Wirth, 2022 MT 105, 409 Mont. 1, 510 P.3d 1206.

Real Estate Contract Prepayment Clause Ambiguous — Payment of Additional Tax Liability Not Fully Performed: A contract for the sale of real estate contained a prepayment clause that required the plaintiff purchaser to pay any additional taxes incurred by the defendant sellers because of the prepayment. The plaintiff tendered payment of the balance due 2 years in advance of the final due date but did not include payment for additional tax liability. The District Court held that the tendered payment of the balance due under the contract without inclusion of the additional tax liability did not constitute full performance of the plaintiff's obligations under the contract. On appeal, the Supreme Court upheld the District Court's ruling. First Nat'l Properties, LLC v. Hillstead Trust, 2020 MT 211, 401 Mont. 59, 472 P.3d 134.

Bodily Injury in Insurance Policy May Include Mental or Psychological Injury Accompanied by Physical Manifestations — Jacobsen Overruled: Defendant caused an automobile accident that injured two brothers, one of whom suffered severe trauma and was hospitalized for an extended period. The boys' mother filed a negligence action against defendant claiming emotional and physical injuries to herself and the brother who was not struck by the vehicle, including the mother's stress, migraine headaches, pain, depression, and a rapid heartbeat when hearing sirens, and the brother's withdrawal. Defendant sought liability coverage from her insurer, and the District Court, relying on Jacobsen v. Farmers Union Mut. Ins. Co., 2004 MT 72, 320 M 375, 87 P3d 995 (2004), granted the insurer's motion for a declaratory judgment on grounds that the insurer was not obligated to provide a defense or coverage to defendant because defendant's policy did not cover the claimed emotional injuries or physical injuries resulting from the emotional injuries within the definition of bodily injury. On appeal, the Supreme Court reexamined the Jacobsen analysis in light of subsequent case law and overruled Jacobsen. Bodily injury as construed in an insurance policy includes a mental or psychological injury that is accompanied by physical manifestations. Defendant's insurance policy provided general coverage for damages that the insured was legally obligated to pay because of a bodily injury sustained by any person, which in this case included the physical manifestations that accompanied the mother's and brother's mental and psychological injuries. Allstate Ins. Co. v. Wagner-Ellsworth, 2008 MT 240, 344 M 445, 188 P3d 1042 (2008), followed in Tucker v. Farmers Ins. Exch., 2009 MT 247, 351 M 448, 215 P3d 1 (2009).

Objective Determination of Whether Ambiguity Exists in Contract — Ambiguity Not Created by Disagreement Over Interpretation of Contract Language: The determination whether an ambiguity exists in a contract is made on an objective basis. A conclusion of ambiguity is not compelled by the fact that parties to a document, or their attorneys, have or suggest opposing interpretations of a contract or even disagree as to whether the contract is reasonably open to just one interpretation, nor does ambiguity exist just because a claimant says so. Rather, an ambiguity exists only if the language is susceptible to at least two reasonable but conflicting meanings. In the present case, plaintiffs' backup position was that language in a right-of-way contract was ambiguous, but the three circumstances proffered by plaintiffs, even when considered collectively, did not demonstrate that the contract language was susceptible to at least two reasonable but conflicting meanings. Thus, the trial court did not err in concluding that the language was unambiguous, which was in fact plaintiffs' primary position. Mary J. Baker Revocable Trust v. Cenex Harvest St., Cooperatives, Inc., 2007 MT 159, 338 M 41, 164 P3d 851 (2007), followed in Wills Cattle Co. v. Shaw, 2007 MT 191, 338 M 351, 167 P3d 397 (2007).

Plain Contract Language Establishing Operating Agreement Rather Than Franchise Agreement — Summary Judgment Proper: Defendant ran residential care facilities for plaintiff and asserted that the parties' contract established a franchise allowing defendant to collect franchise fees and royalties. The District Court found that although there were contractual obligations between the parties, there was no evidence of privity between the parties and no genuine issue of material fact regarding whether a franchise existed, so plaintiff was entitled to summary judgment. On appeal, the Supreme Court examined the plain language of the contract and determined that there was no special meaning ascribed to the term "franchise", that the contract was essentially an operating agreement rather than a franchise agreement, and that no ambiguity was created concerning defendant's rights to collect franchise fees and royalties. No fact question regarding the parties intention existed, so summary judgment was proper, and the District Court was affirmed. SVKV, L.L.C. v. Harding, 2006 MT 297, 334 M 395, 148 P3d 584 (2006).

Buy-Sell Agreement Not Subject to Financing Contingency Absent Specific Contractual Funding Language: A buy-sell agreement stated that the buyer had sufficient funds to close the sale of a ranch and was not relying upon any contingent source of funds unless otherwise stated in the agreement, but there was no third-party financing specified in the agreement. Nevertheless, when the buyer was not able to close the sale for lack of funds, both parties sought to recover the earnest money, and the buyer asserted that the contract language was clear and unambiguous in conditioning the sale on financing. The District Court disagreed, and on appeal, the Supreme Court concurred. The buyer represented that it had sufficient funds, and nowhere in the agreement or in an addendum extending the closing date was it specified that completing financing meant that the buyer had to obtain a loan from a third party. The District Court's award of the earnest money to the seller was affirmed. Sec. Abstract & Title Co. v. Smith Livestock, Inc., 2006 MT 265, 334 M 172, 146 P3d 732 (2006).

Questions of Fact Regarding Ambiguous Contract and Damages — Summary Judgment Inappropriate: Upon remand of a breach of contract action in Bradley v. Crow Tribe of Indians, 2003 MT 82, 315 M 75, 67 P3d 306 (2003), the District Court granted Bradley's motion for summary judgment a second time without considering the merits of defendant's defense to the breach of contract. However, because questions of fact still existed regarding ambiguous language in the contract and potential damages, summary judgment was inappropriate, so the case was again reversed and remanded for further consideration. Bradley v. Crow Tribe of Indians, 2005 MT 309, 329 M 448, 124 P3d 1143 (2005).

Bodily Injury Not Inclusive of Emotional or Psychological Injury Within Terms of Uninsured Motorist Policy: Jacobsen was driving a car insured by defendant when he stopped to assist another motorist who was unconscious with a bleeding head wound. Despite Jacobsen's ministrations, the motorist died a few days later, and the cause was determined to be suicide. The next year, Jacobsen began seeking treatment for emotional distress suffered as a result of the incident and filed a claim with defendant to recover uninsured motorist benefits and medical pay benefits. The District Court granted summary judgment for defendant, and Jacobsen appealed on grounds that his policy for uninsured motorist coverage included damages for bodily injury sustained by the insured caused by an accident. The Supreme Court held that the term "bodily injury" was not ambiguous and was limited to physical injury caused by an accident but did not include emotional or psychological injuries. Thus, Jacobsen's emotional injury, including resulting physical manifestations, did not constitute bodily injury as defined in the insurance contract and was not compensable. Jacobsen v. Farmers Union Mut. Ins. Co., 2004 MT 72, 320 M 375, 87 P3d 995 (2004), following Bain v. Gleason, 223 M 442, 726 P2d 1153 (1986), and Aetna Life & Cas. Co. v. First Sec. Bank of Bozeman, 662 F. Supp. 1126 (D.C. Mont. 1987). Jacobsen was overruled in Allstate Ins. Co. v. Wagner-Ellsworth, 2008 MT 240, 344 M 445, 188 P3d 1042 (2008), to the extent that bodily injuries include mental or psychological injuries that are accompanied by physical manifestations.

Ambiguous Settlement Agreement Language Regarding Maintenance Calculation — Gross Disposable Income Interpreted as Pretax Income: A settlement agreement provided that monthly maintenance payments be 15% of the husband's gross disposable income. In direct opposition to the husband's interpretation, the wife and her expert contended that the amount should be based on pretax rather than after-tax income, and the District Court agreed. The court found that the term gross disposable income was ambiguous because "gross" and "disposable" had mutually exclusive meanings in this context, so the court looked beyond the agreement language to the parties' intent. Because the term was ambiguous, the parties' proposed interpretations were equally proper, so under this section, the ambiguity was construed in the wife's favor because the maintenance provision was for her benefit. The court's allowance of testimony from the wife's expert was also within the court's discretion. In re Marriage of Mease, 2004 MT 59, 320 M 229, 92 P3d 1148 (2004).

Wendell Test Applied to Determination of Whether Bodily Injury Caused by Accident "Resulting From the Use" of Insured Vehicle: Defendant's son was injured in a hunting accident after riding to the hunt in a vehicle owned by Wajahuski and insured by plaintiff. The insurance policy provided for coverage resulting from the use of a vehicle. The District Court applied the test in Wendell v. St. Farm Mut. Auto. Ins. Co., 1999 MT 17, 293 M 140, 974 P2d 623 (1999), and held that the automobile insurance policy did not provide liability coverage with respect to defendant's claims for bodily injury. Defendant appealed. The Supreme Court affirmed. Even though the Wendell test was originally applied in an uninsured motorist case, the expansive, fact-intensive test also applied here. The phrase "resulting from the use" was ambiguous, so the contract terms were construed in a light most favorable to the insured or other beneficiary. The accident could have occurred in any location, regardless of how the hunters reached their destination. The fact that that particular vehicle was used to transport the hunters and assist in the hunt provided no connection between the use of the vehicle and the hunting accident. Thus, the District Court did not err in holding that the personal injuries were not caused by an accident resulting from the use of the insured motor vehicle. St. Farm Mut. Auto. Ins. Co. v. Ferrin, 2002 MT 196, 311 M 155, 54 P3d 21 (2002).

Ambiguity Regarding Whether Settlement Contingent on Alternate Financing — Summary Judgment Improper: Plaintiff sought to foreclose on a loan made to defendant, alleging that defendant's liabilities exceeded the value of the collateral, resulting in default pursuant to the terms of the note. The parties made several attempts to settle the issue, resulting in defendant's payoff to plaintiff, but in an amount that the plaintiff claimed was insufficient. The District Court granted summary judgment to plaintiff and ordered enforcement of the settlement agreement.

However, a letter memorializing the settlement agreement, when considered with the parties' other correspondence, created an ambiguity regarding whether the settlement was contingent on alternate financing. Because there was more than one reasonable interpretation regarding the parties' intention, the parties' affidavits and testimony were admissible to determine intention and raised an issue of fact that precluded summary judgment. The case was remanded for further proceedings. Stockman Bank v. Potts, 2002 MT 178, 311 M 12, 52 P3d 920 (2002).

Ambiguity of Term "Purchaser's Profit" in Real Estate Sales Contract — Special Meaning Not Ascribed to Ambiguous Term: The District Court determined that the language in a contract for deed was ambiguous because it failed to define the term "purchaser's profit", a term that was material to a promise to share profits on resale of the property. The court then went on to find that the term had a special meaning that did not allow for deduction of the buyers' sales costs and the costs of improvements. On appeal, defendants argued that the term referred to the net profit from the sale, meaning the selling price minus the purchase price as well as the sales costs and improvement costs. Plaintiffs contended that the term referred to the gross profit from the sale, meaning the selling price minus only the purchase price. The Supreme Court found that the term could reasonably be subject to either interpretation and was thus ambiguous. Further, the District Court's finding that the term had a special meaning completely contradicted its holding that the phrase was ambiguous. Construing the ambiguity against plaintiffs, who drafted the language, the Supreme Court construed the term in its ordinary rather than special meaning and allowed defendants to deduct the ordinary costs directly associated with the sale of the property, but not the costs of the improvements because no mention was made of any additional sums to be paid to acquire improvements. The Supreme Court also agreed with both parties that the District Court erred in determining the sum that defendants should be allowed to deduct as their purchase price in calculating the purchaser's profit because the sum did not reflect what was actually paid for the property. The Supreme Court arrived at its own calculation of the purchaser's profit and remanded for proceedings consistent with its calculations. Ophus v. Fritz, 2000 MT 251, 301 M 447, 11 P3d 1192, 57 St. Rep. 1037 (2000).

"Arising Out of" Ambiguous — Coverage for Liability Not Excluded: Pablos were injured in a vehicle accident involving Moore, who was transporting a landscaping tractor for his employer. The employer was covered by a commercial general liability insurance policy that provided liability insurance for negligent acts of the corporation and its employees. Pablos contended that the employer was negligent in the hiring, training, and supervision of Moore. The employer conceded that the claim arose during the policy period and fell within the definitions of "bodily injury" and "occurrence" and that the policy would provide coverage unless coverage was denied by an exclusion but contended that coverage was excluded under both the exclusion for damages "arising out of" the use of an automobile and the exclusion for damages "arising out of" the transportation of mobile equipment. The District Court held that the term "arising out of" was ambiguous and, construing the instrument against the drafter-insurer, ruled that coverage for Pablos' accident was not excluded under the policy language. Noting that the phrase "arising out of" has been declared ambiguous in another insurance context in Wendell v. St. Farm Mut. Auto. Ins. Co., 1999 MT 17, 293 M 140, 974 P2d 623 (1999), the Supreme Court applied a similar rationale to the phrase in both exclusionary clauses at issue in the present case. The phrase was reasonably subject to more than one interpretation and thus ambiguous. Pursuant to Head v. Cent. Reserve Life of N. America Ins. Co., 256 M 188, 845 P2d 735, 50 St. Rep. 20 (1993), if the terms of an insurance policy are ambiguous, obscure, or open to different constructions, the construction most favorable to the insured or other beneficiary must prevail, particularly if an ambiguous provision attempts to exclude the liability of the insurer. Here, the policy did not clearly and unambiguously exclude coverage for the theories of liability pleaded by Pablos, and the District Court's summary judgment that coverage was owed on Pablos' claims for negligent hiring, training, and supervision of Moore was affirmed. Pablo v. Moore, 2000 MT 48, 298 M 393, 995 P2d 460, 57 St. Rep. 231 (2000), following Marquis v. St. Farm Fire & Cas. Co., 961 P2d 1213 (Kans. 1998).

Ambiguous Language Regarding Conduct of Mineral Development Operations: An agreement implementing development of a mineral interest indicated that the parties would operate the venture as joint operators, but it was ambiguous as to who would conduct the day-to-day operations of the property, seemingly implying that daily operations would be conducted by the oil company. Evidence indicated that lessor worked as an employee in the operations, so the District Court properly granted the company authority to conduct daily operations subject to a right of inspection by the lessor. Somont Oil Co., Inc. v. Nutter, 228 M 467, 743 P2d 1016, 44 St. Rep. 1685 (1987).

Parol Evidence Necessary to Determine Intention When Latent Ambiguity Exists: A party transferred property back to sellers in lieu of foreclosure. The transfer arguably constituted a technical conveyance. "Conveyance" had different meanings for the parties and therefore was to be interpreted in accord with the manifest intent of the parties. Parol evidence was necessarily admissible to demonstrate and explain this latent ambiguity, and summary judgment on the issue was improper. Ellingson Agency, Inc. v. Baltrusch, 228 M 360, 742 P2d 1009, 44 St. Rep. 1598 (1987), followed in Fox Grain & Cattle Co. v. Maxwell, 267 M 528, 885 P2d 432, 51 St. Rep. 1136 (1994).

Ambiguous Insurance Policy Provision — Summary Judgment Reversed: An insurance policy that did not clearly state whether it provided uninsured motor vehicle coverage when the driver was insured but the ownership of the vehicle was not was held to be ambiguous; therefore, under the rationale that an ambiguous provision is construed against the insurance company, the policy was interpreted to provide coverage. The District Court grant of summary judgment holding that the policy did not provide uninsured motor vehicle coverage was reversed. St. Farm Mut. Auto. Ins. Co. v. Taylor, 223 M 215, 725 P2d 821, 43 St. Rep. 1667 (1986), distinguished in Meyer v. St. Farm Mut. Auto. Ins. Co, 2000 MT 323, 303 M 1, 15 P3d 899, 57 St. Rep. 1363 (2000).

Annexation Agreement — Issue of Intent One of Fact — Summary Judgment Improper: The term "residential purposes" in a "Waiver of Right to Protest Annexation and Agreement on Non-Conforming Use" was not so clear on its face as to preclude multifamily residential purposes. Supreme Court held that District Court erred in granting summary judgment for city based on the District Court's determination of the intention of the parties and remanded the case for trial on the issue of intent. Issue of intent is one of fact and cannot be decided on summary judgment. Derrenger v. Billings, 213 M 469, 691 P2d 1379, 41 St. Rep. 2276 (1984).

Exception for Jointly Drawn Document: Shortly after entering into a land purchase agreement, the parties changed the agreement into a tax-free land exchange agreement. The new agreement gave buyer 3 ½ years to acquire like-kind property to be exchanged for seller's ranch. The like-kind property was to be purchased with funds placed periodically by buyer in an escrow account. Several years later a dispute arose concerning the nature and timing of the payments. Buyer submitted the questions to the District Court in a declaratory judgment action. The District Court interpreted the contract in a manner generally favorable to seller, and buyer appealed, claiming that the District Court's decision was unreasonable, contrary to the parties' intentions, and improper under the rules of construction of contracts. The Supreme Court affirmed, ruling that the District Court's interpretation had not been unreasonable since: (1) its decision on the timing of the rental payments was reflective of the parties' intentions as shown by their past performance; (2) its decision on the timing of the amortization payments was consistent with the rule of construction requiring that a contract be construed in such a way as to give effect to all of its provisions; and (3) its ruling on the intention of the parties was supported by the evidence. Finally, 28-3-206 did not entitle buyer to have ambiguities construed in his favor; even though buyer claimed that the nature of the agreement was changed solely for seller's benefit, the agreement was prepared by an attorney for both parties, not by one party alone. Lewis v. Murphy, 199 M 368, 649 P2d 740, 39 St. Rep. 1459 (1982).

Construction of Agricultural Lease: Where provision in agricultural lease regarding removal of improvements to the land or payment therefor at end of the lease was unclear, the court applied extrinsic evidence to determine that the parties did not intend payment for nonremovable improvements to be required. The fact of lessee's careless documentation of his expenses and his attempt to claim as improvements items that were included in a required maintenance clause were held to support the finding. Overcast v. Akra, 197 M 276, 642 P2d 1058, 39 St. Rep. 558 (1982).

Term "Mineral" as Applied to Sand and Gravel — Inherently Ambiguous: There is a split of authority whether the term "mineral" includes or excludes sand and gravel. The court declined to announce an applicable rule in Montana but found that the use of the term "mineral", as applied to sand and gravel, is inherently ambiguous. Where an ambiguous term is used, the intent of the parties will govern its construction and extrinsic evidence can be used to discover that intent. The court concluded that there was sufficient evidence upon which to conclude that the parties intended the term to include sand and gravel. Adams v. Chilcott, 182 M 511, 597 P2d 1140 (1979).

Reservation of Mineral Interest: In action for specific performance arising over interpretation of contract for conveyance of land reserving mineral interest, where cross-complaint of defendants alleged that the contract was ambiguous and uncertain and prayed for a declaratory judgment to adjudicate the rights of the parties, it was the duty of the trial court to determine the intent of the parties and the exclusion of parol evidence of intent was error. Stokes v. Tutvet, 134 M 250, 328 P2d 1096 (1958).

Oil and Gas Leases:

Where the defendant agreed to assign a specific oil lease and then described land held by him covered by other leases, received the consideration therefor but never completed the assignment, the court was warranted in finding that it called for a transfer of interest of all the lands described in it, since the evidence disclosed that is what the plaintiff thought was being transferred. Bull Creek Oil & Gas Dev. v. Bethel, 127 M 222, 258 P2d 960 (1953).

Where a written contract appears on its face to be uncertain and ambiguous, resort to parol testimony may be had in aid of its interpretation; and under that rule, in an action for breach of a contract of lease of oil and gas lands, providing, inter alia, for drilling of exploratory wells "to such number and extent as the premises will admit of', thus rendering the contract ambiguous as to the number of wells to be drilled, parol testimony was admissible to show the parties' understanding of the clause when the contract was entered into. Brown v. Homestake Exploration Co., 98 M 305, 39 P2d 168 (1934).

Farm Lease: Under 28-3-202 farm lease contracts are to be read as a whole and not by particular paragraphs or sentences, and under this section and 28-3-206 any ambiguities in such a lease should be construed against the lessor. A tenant was entitled to compensation for the summer-fallowing he did during the last year of his holding, where he did not renew and the lease was given to another, and where lease required 80 acres to be summer-fallowed, but tenant found only 74.5 acres of tillable land, he substantially complied (1-3-222). Letz v. Lampen, 110 M 477, 104 P2d 4 (1940).

Burden of Proof: Where the attendant facts and circumstances in the making of an agreement are resorted to as an aid to an understanding of it, no greater burden rests upon the promisor than to show by a preponderance of the evidence that the promisee understood it as the promisor believed he understood it. Blankenship v. Decker, 34 M 292, 85 P 1035 (1906).

28-3-307. Particular clauses subordinate to general intent.

Case Notes

Arbitration Clause Unenforceable: Mueske's contract with a securities firm contained an arbitration clause that was to be governed by the rules of either the New York Stock Exchange, Inc. (NYSE), or the National Association of Securities Dealers, Inc. (NASD). The Supreme Court held that the securities firm had failed to comply with other rules of the NYSE or NASD and therefore was not entitled to enforcement of the arbitration provision. Mueske v. Piper, Jaffray & Hopwood, Inc., 260 M 207, 859 P2d 444, 50 St. Rep. 1009 (1993), followed in Chor v. Piper, Jaffray & Hopwood, 261 M 143, 862 P2d 26, 50 St. Rep. 1234 (1993).

Cost of Asbestos Removal Covered in Policy — Narrow Construction of Policy Exclusions: A "code exclusion" clause in a policy issued on a commercial building relieved insurer of any obligation to pay additional costs for the removal of debris from a fire-damaged building when the cost of removal was increased because of regulatory restrictions. Insurer claimed exemption when the cost of removal was increased because the debris contained asbestos, a substance subject to legal regulation. However, coverage exclusions are contrary to the fundamental protective purpose of an insurance policy and are therefore subject to a rule of narrow construction. Noting that the policy as drafted affirmatively extended coverage for debris removal and that the asbestos in question was considered debris as a result of fire damage, the Supreme Court held that insurer was liable contractually and that the exclusion was inapplicable. Farmers Union Mut. Ins. Co. v. Oakland, 251 M 352, 825 P2d 554, 49 St. Rep. 72 (1992), following Garnett v. Transamerica Ins. Serv., 800 P2d 656 (Idaho 1990), and followed in Newman v. Scottsdale Ins. Co., 2013 MT 125, 370 Mont. 133, 301 P.3d 348.

Purpose of Land Exchange Agreement Effected in Interpretation of Its Provisions: Shortly after entering into a land purchase agreement, the parties changed the agreement into a tax-free land exchange agreement. The new agreement gave buyer 3½ years to acquire like-kind property to be exchanged for seller's ranch. The like-kind property was to be purchased with funds placed periodically by buyer in an escrow account. Several years later a dispute arose concerning the nature and timing of the payments. Buyer submitted the questions to the District Court in a declaratory judgment action. The District Court interpreted the contract in a manner generally favorable to seller, and buyer appealed, claiming that the District Court's decision was unreasonable, contrary to the parties' intentions, and improper under the rules of construction of contracts. The Supreme Court affirmed, ruling that the District Court's interpretation had not been unreasonable since: (1) its decision on the timing of the rental payments was reflective of the parties' intentions as shown by their past performance; (2) its decision on the timing of the amortization payments was consistent both with the rule of construction requiring that a contract be construed in such a way as to give effect to all of its provisions and with this section; and (3) its decision on the intention of the parties was supported by the evidence. Finally, 28-3-206 did not entitle buyer to have ambiguities construed in his favor; even though buyer claimed that the nature of the agreement was changed solely for seller's benefit, the agreement was prepared by an attorney for both parties, not by one party alone. Lewis v. Murphy, 199 M 368, 649 P2d 740, 39 St. Rep. 1459 (1982).

Ambiguous Insurance Policy: Summary judgment on a claim for loss by theft of a commercial carpet cleaner was improperly granted defendant insurer when the policy of insurance was ambiguous as to exclusions from coverage. The particular exclusionary clause was subordinate to the general intent of the contract. Alpha Real Estate Dev., Inc. v. Aetna Life & Cas. Co., 174 M 301, 570 P2d 585 (1977).

Determining Intent — Subject Matter and Circumstances Considered: It is a fundamental rule that in the construction of contracts the courts may look not only to the language employed but to the subject matter and the surrounding circumstances and may avail themselves of the same light which the parties possessed when the contract was made. Kintner v. Harr, 146 M 461, 408 P2d 487 (1965).

Entire Contract to Determine Intent: In the construction of a contract the intention of the parties at the time of contracting must be pursued if possible, which intention must be gathered from the entire instrument and not from particular words or phrases or disjointed parts of it, and in the ascertainment of such intention the subject matter of the contract and the purposes of its execution are material. St. v. Rosman, 84 M 207, 274 P 850 (1929).

Mutuality as to Each Covenant Not Required: Generally it is not essential that each covenant of agreement of the lessor in an oil lease shall be supported by specific reciprocal covenant or agreement by the lessee, it being sufficient if the contract contains mutual obligations binding upon both parties, and provision that the lessee could surrender it "upon payment of $ ______" was not void for want of mutuality in this respect, the other provisions of the contracts being wholly independent of it and enforceable. Hinerman v. Baldwin, 67 M 417, 215 P 1103 (1923).

Part 4
Factors Considered in Determining Intention

Part Case Notes

Failure to Comply With Provisions of Federal Act Incorporated by Reference Into Contract — Affirmative Defense: The Farm Credit Bank instituted suit to foreclose on a loan agreement with the Graveleys and filed for summary judgment. The Graveleys argued that the bank was estopped from foreclosing because it had not complied with the restructuring provisions of the Agricultural Credit Act of 1987, which had been incorporated by reference into the parties' agreement. The Supreme Court held that the Graveleys were entitled to assert as an affirmative defense the failure of the bank to follow the provisions of the Act and that allowing the defense was not synonymous with allowing a foreclosure court to substitute its judgment for that of the bank's loan officers. The Supreme Court also held that the lower court had correctly denied the motion for summary judgment on the basis that factual issues existed with respect to the merits of the Graveleys' affirmative defense. State ex rel. Farm Credit Bank of Spokane v. District Court, 267 M 1, 881 P2d 594, 51 St. Rep. 709 (1994), following Farm Credit Bank of Spokane v. Parsons, 758 F. Supp. 1368 (D.C. Mont. 1990), and followed in AgAmerica, FCB v. Robson, 272 M 413, 901 P2d 100, 52 St. Rep. 800 (1995).

Interpretation of Contract — Time of Performance: On appeal, the seller of a log cabin urged that the agreement required the buyer to remove the logs from the seller's property as soon as possible. The Supreme Court found that the negotiations were quick and informal and that nothing specific was said about the time in which the cabin was to be removed. Noting the seller's testimony that he was in the process of refurbishing his motel and wanted the cabin removed as soon as possible so that he could take advantage of the good building weather to expand the motel and that the cabin was old and had not been used for years and contributed nothing to the value or appearance of the property and little value to the motel, the Supreme Court held that there was substantial evidence to support the trial court's finding that a condition of the sale was that the logs were to be removed as soon as possible. Jeffery v. Neville, 190 M 300, 620 P2d 1218, 37 St. Rep. 1983 (1980).

28-3-401. Extent to which language governs interpretation.

Case Notes

Surrogacy Contract — Express Written Contract Limited to Clear and Unambiguous Terms — Contract Did Not Preclude Subsequent Establishment of Parental Interest Under Montana Law Not Based on Fact of Surrogacy. Sayler v. Yan Sun, 2023 MT 175, 413 Mont. 303, 536 P.3d 399.

Earth Movement Exclusion — Commercial General Liability Policy — Coverage for Homeowner's Claims Reversed — Policy Clearly and Unambiguously Excluded Coverage — Reasonable Expectations Doctrine Not Applicable. Loendorf v. Employers Mut. Cas. Co., 2022 MT 143, 409 Mont. 248, 513 P.3d 1268.

Multiple Contract Interpretations Argued to Court But Only One Reasonable — No Ambiguity Present: The District Court denied the plaintiffs' motion for partial summary judgment on a contract interpretation issue. The plaintiffs argued that a supplemental benefits package purchased by the owner of a motorboat on her insurance policy had the effect of deleting an entire section of the insurance policy, including a watercraft exclusion that would have arguably resulted in coverage for a motorboat accident. The District Court noted that such an interpretation of the policy would also remove several categories of coverage listed in a subheading of the supposedly deleted section, leaving the insured with less coverage despite paying an additional premium for the supplemental endorsement. On appeal, the Supreme Court affirmed, concluding that because there was only one reasonable interpretation of the contract, no ambiguity existed that could be construed against the insurer. Young v. Hammer, Hewitt, Jacobs, & Floch, PLLC, 2021 MT 180, 405 Mont. 65, 491 P.3d 725.

Extrinsic Evidence Not Considered — Deed Unambiguous: When the Water Court held a deed to be unambiguous, the Water Court was precluded from considering extrinsic evidence submitted by the parties. The clear language on the face of the deed allowed the Water Court to determine the parties' intent from the deed alone. Little Big Warm Ranch, LLC v. Doll, 2020 MT 198, 400 Mont. 536, 469 P.3d 689, distinguishing Wicklund v. Sundheim, 2016 MT 62, 383 Mont. 1, 367 P.3d 403.

State-Mandated Reduction in Compensation for Contract Attorneys — Memorandum of Understanding — No Violation of Contract Clause — Budget Cut Reductions Permissible: The petitioners were attorneys who contracted with the office of state public defender (OPD) to provide legal services for indigent clients. To become an OPD contract attorney, the petitioners signed a contract, referred to as a memorandum of understanding (MOU), with OPD. In March 2018, OPD announced a reduction to the hourly contract rate and a reduction of pay for case-related travel time in order to implement budget cuts effective for any services rendered on or after April 1, 2018. The petitioners pursued a class action lawsuit in District Court against the state, seeking declaratory relief, injunctive relief, and damages for breach of contract and violation of the contract clause in Art. II, sec. 31, Mont. Const. The state, in turn, filed a motion for summary judgment based on legal interpretation of the MOU under contract law. The District Court granted the state's motion and the Supreme Court affirmed, reasoning that nothing in the MOU indicated that the compensation rates were locked in place for the duration of the petitioners' representation. Additionally, the MOU's language clearly provided for prospective modification of compensation rates at the state's discretion, which was limited by both 47-1-121 and the implied covenant of good faith and fair dealing. Brooke v. St., 2020 MT 187, 400 Mont. 435, 468 P.3d 351.

On Remand for Calculation of Damages Caused by Breach: The defendants were employed by the plaintiff's accounting firm under an employment agreement containing a covenant restricting competition. When the defendants established a competing accounting firm and solicited the plaintiff's clients, the plaintiff filed a complaint against the defendants to declare the covenant enforceable and to recover damages. After the Supreme Court remanded the issue of damages caused by the breach back to the District Court in Junkermier v. Alborn, 2016 MT 218, 384 Mont. 464, 380 P.3d 747, the District Court determined that the covenant was reasonable, that the defendants were jointly and severally liable for damages arising out of the covenant's breach pursuant to the contractual calculation of 1 year's billings to the plaintiff's clients, and that the plaintiff was entitled to prejudgment interest. The Supreme Court affirmed on all issues with the exception of the date interest began accruing based on the language in the covenant, which was described as de minimus. Junkermier v. Alborn, 2020 MT 179, 400 Mont. 408, 469 P.3d 111.

Contract Interpretation Matter of Law: The District Court entered summary judgment for a bank in a convoluted contracts and tax case. The plaintiff appealed on the basis that an alleged breach of the parties' deed of trust meant that there were disputed material facts. The Supreme Court affirmed the entry of summary judgment, noting that contract interpretation is a question of law. Graham-Rogers v. Wells Fargo Bank, N.A., 2019 MT 226, 397 Mont. 262, 449 P.3d 798.

Contradicting Clauses in Separate Contracts Construed Against Drafter — Employee Waiver — Health Insurance: The plaintiff health insurance company filed a breach of contract action against the defendant, an employer providing health insurance for its employees. The contracts between the parties required the defendant to cover 75% or more of its employees; however, a subsequent contract allowed the defendant's employees to waive coverage. The District Court granted summary judgment in favor of the defendant, finding that the two provisions in the contracts were ambiguous and the contract should be interpreted against the drafter. On appeal, the Supreme Court affirmed, holding that the contracts must be interpreted as part of the same transaction and that giving effect to both contract provisions is not reasonably practical, that the ambiguity is construed against the drafter, that the newer specific contract controlled over the older general contract, and that the waiver provision was meant to modify the minimum employee participation provision. Mont. Health Network, Inc. v. Great Falls Orthopedic Associates, 2015 MT 186, 379 Mont 513, 353 P.3d 483.

Settlement of Legal Actions Against Estate — Settlement Agreement Properly Construed: Evalyn Burrell owned an interest in 200 acres at the time of her death, 80 acres in one parcel and 120 in the other, her grandchildren also having an undivided interest in 40 acres of the 120-acre parcel. In settlement of an action concerning her will and a second action to partition the 120-acre parcel, the grandchildren took 40 acres from both the 80-acre and 120-acre parcels. However, when Evalyn's estate sought to enforce the settlement agreement, the grandchildren claimed that the agreement did not settle their interests in all of Evalyn's property and raised other issues as well. The Supreme Court held that it was inconceivable that the parties did not intend to settle years of litigation over the 200 acres of land and concluded that the language of the agreement, when viewed as a whole, could therefore be interpreted only as applying to the grandchildren's interests in all of the Burrell property. In re Estate of Burrell, 2010 MT 280, 358 Mont. 460, 245 P.3d 1106.

No Duty of Insurer to Cover City's Conversion of Pension Funds: The city of Dillon failed to properly pay pension benefits, even though the city received the money from the state. When a beneficiary sued the city to recover unpaid benefits, the city tendered defense of its claim to its insurer, but the insurer declined to provide coverage or defend the claim based on a financial gain exclusion in the insurance policy. The beneficiary was granted summary judgment, so the city paid the judgment and filed an action to recover against the insurer. The District Court held that the insurer was liable and breached its duty to defend, so the insurer appealed. The Supreme Court held that the insurer had no duty to provide coverage to the city because the city's claim arose in whole or in part from the city's unlawful retention and conversion of the pension funds, so the city had no coverage for the claims for return of principal and interest. The District Court was reversed. Dillon v. Mont. Municipal Ins. Authority, 2009 MT 393, 353 M 370, 220 P3d 623 (2009).

Covenants Intended to Remain in Effect Until Rejected by Property Owners — Failure of Sufficient Tract Owners to Vote to Amend Covenants: Subdivision property owners entered covenants that would automatically extend for "successive period" of 10 years. The covenants could also be amended by a two-thirds vote of the owners of the original tracts. Some of the owners contended that the covenant extension language was ambiguous because it was not clear if the covenants would be renewed only for a single 10-year period or for successive 10-year periods. The District Court held that the language was not ambiguous, but rather contained a typographical error, and that successive 10-year periods applied. Plaintiffs appealed, but the Supreme Court affirmed. Taken as a whole the covenant language intended that the covenants remain in effect until affirmatively rejected by the property owners. In this case, five of the eight original tract owners voted to amend the covenants, so without the required two-thirds vote, the covenants remained unamended. Brewer v. Hawkinson, 2009 MT 346, 353 M 154, 221 P3d 643 (2009). See also Creveling v. Ingold, 2006 MT 57, 331 M 322, 132 P3d 531 (2006).

Genuine Issue of Material Fact Whether Dam Operation Damaged Lakeshore Properties — Summary Judgment Improper — Class Action Vacated: Flathead Lake landowners brought a class action suit against defendant operators of Kerr Dam for operating outside the scope of their easements in a manner that continuously eroded and damaged plaintiffs' lakeshore properties. The District Court rejected plaintiffs' argument that the dam operator was not allowed to affect plaintiffs' properties above an elevation of 2,893 feet, concluding instead that defendants' easements covered entire parcels. The court concluded that erosion, including wave action erosion, was within the scope of the easements and held that any duty defendants had to not cause unreasonable damage to plaintiffs' properties applied only to damage unrelated to use of the easement. Therefore, summary judgment was granted to defendants, and plaintiffs appealed. The

Supreme Court first agreed that the District Court's contour line theory was correct. The "2,893 feet" clause did not establish the vertical limit argued by plaintiffs because although the dam operators' right to flood, subirrigate, drain, or otherwise affect the shoreline was not unlimited, it was not restricted to a maximum elevation of 2,893 feet at each parcel, but rather extended to whatever part of each parcel was affected when the lake was held at 2,893 feet above mean sea level as measured at the dam. The court also agreed that the right to cause some erosion was necessary to the enjoyment of the right to perpetually flood, subirrigate, and drain and was thus included by implication in the easements. However, further factual development and trial were necessary to address the question of whether the erosion was reasonable, necessary, and within the scope of the easements, which could not be resolved by summary judgment. Additionally, the question of whether defendants breached their obligation to not cause unreasonable damage to the shoreline properties and to not unreasonably interfere with plaintiffs' enjoyment also required further factual development and possibly trial. Therefore, the order certifying the case as a class action was vacated and the case was remanded for further consideration. Mattson v. Mont. Power Co., 2009 MT 286, 352 M 212, 215 P3d 675 (2009).

On remand, the District Court decertified the class as to one defendant and denied the plaintiffs' motion for certification as to another defendant on the basis that the question of whether the erosion caused unreasonable damage to or unreasonably interfered with the plaintiffs' properties required an individual, property-by-property analysis that was improper for class certification. On appeal, the Supreme Court reversed, concluding that class certification to both defendants was proper because the reasonableness of the erosion presents a common question that is incapable of being resolved on a property-by-property basis since an aggregate of the benefits and burdens imposed on all of the shoreline properties must be considered together to determine reasonableness. Mattson v. Mont. Power Co., 2012 MT 318, 368 Mont. 1, 291 P.3d 1209.

No Ambiguity in Complete, Final Sales Agreement — Parol Evidence Inadmissible: The parties entered a sale agreement for a ready-mix concrete plant. Plaintiff subsequently filed an action alleging that defendant violated the agreement by breaching the covenant to not compete and the covenant of good faith and fair dealing, which constituted malice resulting in lost profits, sales, and goodwill. The District Court granted summary judgment to defendant and plaintiff appealed, but the Supreme Court affirmed. The District Court correctly concluded that the sales agreement constituted a complete, final agreement and unambiguously did not include a noncompetition provision, but in fact provided that plaintiff would sell concrete to defendant for use in the area. The intention of the parties was ascertainable from the writing alone, and the agreement was presumed to represent all transactions regarding elements extrinsic to the agreement and was thus considered complete and final, so parol evidence was inadmissible. Richards v. JTL Group, Inc., 2009 MT 173, 350 M 516, 212 P3d 264 (2009). See also Lindey's, Inc. v. Professional Consultants, Inc., 244 M 238, 797 P2d 920 (1990), and Mary J. Baker Revocable Trust v. Cenex Harvest States, Cooperatives, Inc., 2007 MT 159, 338 M 41, 164 P3d 851 (2007).

Ambiguity of Contract Raising Genuine Issues of Fact — Summary Judgment Improper: In a dispute over the sale of aircraft, the District Court considered summary judgment motions from both parties, granted summary judgment for plaintiff on claims of breach of contract and express warranty, and denied defendant's summary judgment counterclaim of breach of contract and express warranty. The Supreme Court examined the contract and found ambiguities regarding whether defendant accepted the aircraft "as is" at signing or maintained the right to inspect and reject the aircraft prior to closing, as well as the parties' extension of the closing date. The ambiguities raised genuine issues of material fact regarding breach of contract and express warranty that were not appropriate for summary judgment, and the Supreme Court reversed for trial on the issues. Corporate Air v. Edwards Jet Center, Mont., Inc., 2008 MT 283, 345 M 336, 190 P3d 1111 (2008).

Tort Claims Not Precluded by Contract Claims Arising From Same Event: In a dispute over the sale of aircraft, the District Court considered summary judgment motions from both parties and granted defendant summary judgment on plaintiff's tort claims on grounds that plaintiff had relied on a contract theory of relief and thus elected to be made whole under the contract. Plaintiff appealed on grounds that tort liability can exist with contract liability and that recovery on a contract theory does not necessarily preclude recovery on tort theories such as fraud. Defendant responded that summary dismissal of the tort claims was proper because plaintiff should not be allowed to make a double recovery and that because plaintiff's claims were commercial, tort damages are not available except in rare cases when a separate tort claim arises from the contractual relationship. Without ruling on the validity of the tort claims, the Supreme Court held that consideration of plaintiff's fraud-based claims was not precluded by the fact that plaintiff also made separate contract claims arising out of the same event. The tort claims were required to be considered individually and could not be dismissed under a blanket rationale that the tort claims and contract claims were mutually exclusive. The District Court's summary judgment was reversed, and the issue was remanded for further consideration. Corporate Air v. Edwards Jet Center, Mont., Inc., 2008 MT 283, 345 M 336, 190 P3d 1111 (2008).

Ambiguous Employment Contract — Question of Parties' Intent Properly Submitted to Jury: West's employment contract contained two different provisions regarding how West would be compensated in the event of termination of employment. The District Court construed the ambiguous clauses against the employer who drafted the contract and submitted the issue to the jury. On appeal by the employer, the Supreme Court examined the contract language and affirmed. The employment agreement was ambiguous on the issue of whether West would be paid trailing commissions or bonuses if West were terminated for cause, so the District Court did not err in ordering that the parties' intent on the issue be submitted to the jury. West v. The Club at Spanish Peaks, LLC, 2008 MT 183, 343 M 434, 186 P3d 1228 (2008), following Eschenbacher v. Anderson, 2001 MT 206, 306 M 321, 34 P3d 87 (2001).

Question Whether Condition Precedent Satisfied and Contract Formed — Remand: The parties negotiated for the purchase of a new vehicle, and the terms of the contract documents set the interest rate at 3.9%. The plain language of the contract was clear that there was no binding contract until the contract terms were accepted by a bank or finance company. A week after negotiations when the bank would not accept the 3.9% rate, the car dealer notified the buyers that they would have to sign new finance papers with a higher annual percentage rate of 4.9%, but the buyers refused. The buyers then sued the dealer, but the District Court compelled arbitration and stayed the proceedings. On appeal, the car dealer asserted that the contract language was not binding to the dealer unless financing was obtained and that the condition precedent applied only to the dealer and not the buyers. The Supreme Court disagreed. The totality of the contract language demonstrated that the condition precedent also applied to the buyers, even though that was not expressly stated. The total sales price and the corresponding finance charge agreed to by the buyers were based on financing at 3.9%, and a change in rate required renegotiation by both parties, so the condition precedent applied to both parties. Because there were questions of disputed fact whether the condition precedent was satisfied and a contract formed, the case was remanded to District Court for further factfinding and discovery. Thompson v. Lithia Chrysler Jeep Dodge of Great Falls, 2008 MT 175, 343 M 392, 185 P3d 332 (2008).

Lessor Fully Compensated for Loss of Truck Under Rental Agreement — Agreed Value of Truck Inapplicable to Damage Claim: Plaintiff leased a truck to defendant for construction work. The truck had an agreed value of $250,000 and a rental rate of $12,000 a month. While in defendant's possession, the truck was heavily damaged. Plaintiff initially sought to repair the truck, but eventually it was stripped of usable parts, and the remaining shell was sold for $15,000. Plaintiff received $114,500 from its insurer, based on the insurer's calculation that the truck had a $126,000 cash replacement value minus the $2,500 policy deductible owed to plaintiff by defendant and minus a $9,000 salvage value. Plaintiff then sued defendant for the unpaid balance of the agreed value, including the monthly payments because the agreed value had not been paid. The District Court noted that even though the parties did not have a signed, enforceable, written contract, defendant had properly insured the truck pursuant to a reasonable lease term, identifying plaintiff as beneficiary, and held that defendant had no independent obligation to pay damages beyond the deductible. Because plaintiff had recovered all damages to which it was entitled, judgment was entered for defendant, and plaintiff appealed. The Supreme Court found that the language of the rental agreement did not require the lessee to pay the agreed value if the truck was damaged or destroyed, so defendant was not liable for the agreed value. Plaintiff failed to show the actual replacement cost of the truck and failed to establish that the District Court's finding was clearly erroneous, so the court did not err in holding that plaintiff was not entitled to additional compensation for replacing the truck. Additionally, plaintiff did not demonstrate what additional rental payments were owed, so defendant had no further obligation to pay damages for loss of use. The District Court did not err in holding that plaintiff was fully compensated under the rental agreement, and judgment was affirmed. Performance Mach. Co., Inc. v. Yellowstone Mtn. Club, LLC, 2007 MT 250, 339 M 259, 169 P3d 394 (2007).

Objective Determination of Whether Ambiguity Exists in Contract — Ambiguity Not Created by Disagreement Over Interpretation of Contract Language: The determination whether an ambiguity exists in a contract is made on an objective basis. A conclusion of ambiguity is not compelled by the fact that parties to a document, or their attorneys, have or suggest opposing interpretations of a contract or even disagree as to whether the contract is reasonably open to just one interpretation, nor does ambiguity exist just because a claimant says so. Rather, an ambiguity exists only if the language is susceptible to at least two reasonable but conflicting meanings. In the present case, plaintiffs' backup position was that language in a right-of-way contract was ambiguous, but the three circumstances proffered by plaintiffs, even when considered collectively, did not demonstrate that the contract language was susceptible to at least two reasonable but conflicting meanings. Thus, the trial court did not err in concluding that the language was unambiguous, which was in fact plaintiffs' primary position. Mary J. Baker Revocable Trust v. Cenex Harvest St., Cooperatives, Inc., 2007 MT 159, 338 M 41, 164 P3d 851 (2007), followed in Wills Cattle Co. v. Shaw, 2007 MT 191, 338 M 351, 167 P3d 397 (2007).

Right-of-Way Contract Granting Language Unambiguous — Summary Judgment Proper: The District Court found that language in a right-of-way contract: (1) granted defendants an easement to bury a fiber optic cable on plaintiffs' land together with a pipeline; (2) did not limit use of the cable to operating and monitoring the pipeline; and (3) gave defendants the right to assign any of their rights, in whole or in part, to any third party. The language was unambiguous, and the court correctly applied the language as written and properly granted summary judgment to defendants. Mary J. Baker Revocable Trust v. Cenex Harvest St., Cooperatives, Inc., 2007 MT 159, 338 M 41, 164 P3d 851 (2007).

Y2K Computer Problems Considered Faulty Design and Inherent Vice — Insurance Coverage Precluded by Policy Exclusions: The state filed insurance claims related to remediation of problems associated with the Y2K transition. The claims were denied, and the state sued. The District Court held that the claims were precluded from coverage by policy language that excluded coverage for damage caused by faulty design and inherent vice. On appeal, the Supreme Court affirmed. An inherent vice is an existing defect, disease, or decay or the inherent nature of a commodity that will cause it to deteriorate over time and also means a loss not covered by a policy that is not related to an extraneous cause but to a loss entirely from internal decomposition or some quality that brings about its own injury or destruction and that must be inherent in the property for which recovery is sought. The state's Y2K problem was an excluded inherent vice because the date field was an inherent problem that brought about its own problem. The faulty design and inherent vice policy exclusions were not ambiguous and clearly excluded the claimed losses. Even though the state did not receive copies of the policies, the policies were renewals of existing policies that contained identical coverage provisions and exclusions, so the state could not reasonably claim that it was unaware of the relevant policy terms and exclusions, and the insurer could rely on valid exclusions in the policy when the state had notice of the exclusions. St. v. Allendale Mut. Ins. Co., 2007 MT 83, 337 M 49, 154 P3d 1233 (2007), following Port of Seattle v. Lexington Ins. Co., 48 P3d 334 (Wash. App. 2002), and GTE Corp. v. Allendale Mut. Ins. Co., 372 F3d 598 (3rd Cir. 2004).

Plain Contract Language Establishing Operating Agreement Rather Than Franchise Agreement — Summary Judgment Proper: Defendant ran residential care facilities for plaintiff and asserted that the parties' contract established a franchise allowing defendant to collect franchise fees and royalties. The District Court found that although there were contractual obligations between the parties, there was no evidence of privity between the parties and no genuine issue of material fact regarding whether a franchise existed, so plaintiff was entitled to summary judgment. On appeal, the Supreme Court examined the plain language of the contract and determined that there was no special meaning ascribed to the term "franchise", that the contract was essentially an operating agreement rather than a franchise agreement, and that no ambiguity was created concerning defendant's rights to collect franchise fees and royalties. No fact question regarding the parties intention existed, so summary judgment was proper, and the District Court was affirmed. SVKV, L.L.C. v. Harding, 2006 MT 297, 334 M 395, 148 P3d 584 (2006).

Contract Interpretation Applicable to Restrictive Covenants — How Ambiguity Resolved — Restrictive Covenants Strictly Construed: General rules of contract interpretation apply to restrictive covenants, and any person having an interest under a restrictive covenant may seek declaratory relief concerning any question of construction arising under the covenant. When a restrictive covenant has been reduced to writing, the intent of the parties is to be ascertained, when possible, from the writing alone, and when the language of a covenant is clear, a court must apply the language as written. Restrictive covenants are strictly construed, and ambiguities in covenants are resolved to allow free use of property. The determination of whether an ambiguity exists in a restrictive covenant is a question of law for a court to decide, but mere disagreement between the parties as to interpretation of a restrictive covenant does not automatically create an ambiguity. Creveling v. Ingold, 2006 MT 57, 331 M 322, 132 P3d 531 (2006). See also Newman v. Wittmer, 277 M 1, 917 P2d 926 (1996), and Toavs v. Sayre, 281 M 243, 934 P2d 165 (1997).

Payment of Actual Costs and Discretionary Attorney Fees Under Contract: A real estate contract provided that the award of reasonable attorney fees to the prevailing party was discretionary with the court and also provided that the prevailing party was entitled to actual costs. The District Court deducted fees and costs related to actions in which plaintiff did not prevail, resulting in a reduction of both attorney fees and costs. On appeal, the Supreme Court affirmed the attorney fee award as an appropriate exercise of the District Court's discretion, but reversed the reduced award of costs because plaintiff was entitled to actual costs under the contract. Gullett v. Van Dyke Constr. Co., 2005 MT 105, 327 M 30, 111 P3d 220 (2005).

Coverage Under Products Completed Operations Hazard Policy Inapplicable When Work Never Completed: Defendant had a products completed operations hazard policy with plaintiff insurer that triggered coverage when all contracted work was completed or when part of the work completed was put to its intended use but future service, maintenance, correction, repair, or replacement might be required. A complaint against defendant alleged that despite repeated requests and promises, the work in question was never completed. Because the work was not completed, materials were not installed, labor was not performed, and the system that was installed was inadequate for the intended purpose, coverage pursuant to defendant's products completed operations hazard policy did not apply. The reasonable expectations doctrine was also inapplicable because the policy language excluded such coverage. Generali-U.S. Branch v. Alexander, 2004 MT 81, 320 M 450, 87 P3d 1000 (2004), following Wellcome v. Home Ins. Co., 257 M 354, 849 P2d 190 (1993).

Dispute Over Contract to Deliver Log Home — No Requirement That Seller Provide Name of Third Party Boom Truck Operator — Rescission Proper Remedy for Material Breach of Contract: Anderson agreed to purchase a log home from Eschenbacher. The home was designed to be constructed on Anderson's homesite. Eschenbacher drafted the purchase contract, which provided that Eschenbacher would act only as a manufacturer, not as a building contractor, and also required Anderson to coordinate and ensure availability of a boom truck to assemble the structure at the site. Anderson contacted a third party to supply a boom truck instead of using Eschenbacher's truck. Eschenbacher then refused to deliver the logs unless Anderson supplied the name of the other boom truck operator. Both parties sued for breach of contract. The District Court concluded that Anderson was under no duty to provide Eschenbacher with the name of the boom truck operator, and the Supreme Court agreed. The contract clearly placed the responsibility for acquiring a boom truck with Anderson, but did not require Eschenbacher to use it, because other language required Anderson to pay any expenses incurred by Eschenbacher for waiting once the logs were delivered, if, for instance, the boom truck that Anderson provided was inadequate. Construing the contract most strongly against the drafter, Eschenbacher, the court found that Eschenbacher could easily have inserted provisions in the contract regarding specifications of an adequate boom truck, but he did not. Eschenbacher materially breached the contract by refusing to deliver the logs until the boom truck dispute was settled. The contract did not specify a remedy; thus, the District Court did not err in granting Anderson rescission of the contract. Eschenbacher v. Anderson, 2001 MT 206, 306 M 321, 34 P3d 87 (2001).

Ambiguity of Term "Purchaser's Profit" in Real Estate Sales Contract — Special Meaning Not Ascribed to Ambiguous Term: The District Court determined that the language in a contract for deed was ambiguous because it failed to define the term "purchaser's profit", a term that was material to a promise to share profits on resale of the property. The court then went on to find that the term had a special meaning that did not allow for deduction of the buyers' sales costs and the costs of improvements. On appeal, defendants argued that the term referred to the net profit from the sale, meaning the selling price minus the purchase price as well as the sales costs and improvement costs. Plaintiffs contended that the term referred to the gross profit from the sale, meaning the selling price minus only the purchase price. The Supreme Court found that the term could reasonably be subject to either interpretation and was thus ambiguous. Further, the District Court's finding that the term had a special meaning completely contradicted its holding that the phrase was ambiguous. Construing the ambiguity against plaintiffs, who drafted the language, the Supreme Court construed the term in its ordinary rather than special meaning and allowed defendants to deduct the ordinary costs directly associated with the sale of the property, but not the costs of the improvements because no mention was made of any additional sums to be paid to acquire improvements. The Supreme Court also agreed with both parties that the District Court erred in determining the sum that defendants should be allowed to deduct as their purchase price in calculating the purchaser's profit because the sum did not reflect what was actually paid for the property. The Supreme Court arrived at its own calculation of the purchaser's profit and remanded for proceedings consistent with its calculations. Ophus v. Fritz, 2000 MT 251, 301 M 447, 11 P3d 1192, 57 St. Rep. 1037 (2000).

Shareholders' Agreement Enforceable Independent of Stock Exchange — Different Intent Contained in Separate Agreements Separately Enforceable: Following his termination from employment with Bitterroot International Systems, Inc. (Bitterroot), Knutson sought to exercise his buyout rights under the shareholders' agreement. Bitterroot refused to pay, contending that an earlier merger transaction and the subsequent shareholders' agreement should be read together and citing Rumph v. Dale Edwards, Inc., 183 M 359, 600 P2d 163 (1979), for the proposition that when construing an agreement that is part of a larger transaction, the intention of the parties must be determined by examining the entirety of the larger transaction. However, Rumph was distinguishable here because all the agreements in question occurred at different times and did not reference or depend upon each other. Each agreement was clear and unambiguous. Under Gerdes v. Omaha Home for Boys, 89 NW 2d 849 (Nebr. 1958), a court may not avoid the language of a complete, unambiguous contract by consolidating it with another writing if the effect of doing so would be to avoid an essential part of the contract. The District Court properly concluded that the shareholders' agreement was enforceable independent of the stock exchange between the parties. Knutson v. Bitterroot Int'l Sys., Inc., 2000 MT 203, 300 M 511, 5 P3d 554, 57 St. Rep. 800 (2000), followed in O'Brien v. O'Brien, 2022 MT 246, 411 Mont. 101, 532 P.3d 831.

No District Court Jurisdiction to Grant Summary Judgment When Dispute Subject to Arbitration: A condition of Burkhart's employment agreement with Semitool, Inc. (Semitool), was that employment disputes would be subject to Montana law and the Uniform Arbitration Act. After 8 months of employment, Burkhart was terminated. He later brought suit against Semitool, alleging that: (1) he had been terminated without good cause; (2) his termination was in retaliation for his refusal to violate public policy; (3) Semitool's opposition to his application for unemployment benefits was without probable cause and motivated by malice; and (4) representations made to him prior to employment were deceptive and motivated by malice, contained misrepresentations, and included false advertisements concerning the kind or character of the employment. In its answer, Semitool demanded arbitration, and Burkhart accepted the arbitration offer on the first two issues. The parties agreed that because trade secrets were involved, the record would be sealed and hearings closed to the public to avoid disclosure of confidential information. Semitool then moved to dismiss for failure to state a claim or, alternatively, to compel arbitration of all four claims. The District Court converted the motion to dismiss into a motion for summary judgment and held a hearing to discuss both motions, after which it granted summary judgment to Semitool and dismissed all four claims. The court determined that because proof of the allegations in the complaint would require disclosure of confidential attorney-client matters and because violation of the attorney-client privilege prejudiced the public interest, that prejudice was a proper ground upon which to invalidate the arbitration agreement. Burkhart appealed. On appeal, the Supreme Court cited 39-2-914 and Ratchye v. Lucas, 1998 MT 87, 288 M 345, 957 P2d 1128 (1998), as controlling. Once an offer to arbitrate has been accepted, neither the District Court nor the parties have a right to continue the lawsuit. The exception relating to the public interest pertains to the validity of the arbitration agreement, not to the merits of the underlying dispute. Thus, the District Court erred in deciding the merits of the issues because it lacked jurisdiction to do so once the parties agreed to arbitrate. Summary judgment was reversed and the claims were remanded for arbitration. Burkhart v. Semitool, Inc., 2000 MT 201, 300 M 480, 5 P3d 1031, 57 St. Rep. 785 (2000).

Title Insurer Not Obligated to Search City Engineer or Water Department Records — Public Records as Properly Recorded Documents — Reasonable Expectations Doctrine Inapplicable: The Millers sought to hold a title insurance company responsible for costs involved in relocating a neighbor's water and sewer lines that were discovered on the property. The lines were of record with the city engineer and the water department, but their existence was not recorded in the chain of title. The title insurance policy defined public records as "those records which by law impart constructive notice of matters relating to said land". The Supreme Court held that the definition was unambiguous and clearly related to records filed and docketed with the County Clerk and Recorder because it was proper recordation that imparted constructive notice of matters relating to the property. Nothing in Montana recordation law required the title insurer to search city engineer or water department records. For the same reason, the Millers' attempt to apply the reasonable expectations doctrine also failed because the policy did not insure against loss or damage by reason of "easements, or claims of easements, not shown by the public records". Miller v. Title Ins. Co. of Minn., 1999 MT 230, 296 M 115, 987 P2d 1151, 56 St. Rep. 908 (1999).

See also Am. Family Mut. Ins. Co. v. Livengood, 1998 MT 329, 292 M 244, 970 P2d 1054, 55 St. Rep. 1336 (1998).

Reservation of Single Right-of-Way Over Existing Private Road — No Ambiguity or Conflict With Intended Access: The District Court determined that a reservation of rights in a 1965 deed was ambiguous because the reservation of rights over a single roadway conflicted with the grantors' intent to reserve as many means as possible to their remaining property in a mountainous area. Ambiguities in a reservation of rights in any grant of property are to be construed in favor of the grantor; however, the breadth and scope of an easement are determined upon the actual terms of the contract. The easement in this case was described as "a right of way" over "an existing private road which extends across" the servient tenement "for the use and benefit of Section 3 and [parts] of Section 34". That language indicated the use to which the easement would be put, not the scope of the easement itself. The Supreme Court found that the reservation of rights was not ambiguous; rather, the language restricting the easement to a single right-of-way over an existing private road did not conflict with the intended use of the easement to benefit the grantors' remaining properties, nor did the grantors' intent override any limitation of the singular use of the word "road" in the reservation. Van Hook v. Jennings, 1999 MT 198, 295 M 409, 983 P2d 995, 56 St. Rep. 767 (1999).

Vehicle Not Considered Utility Trailer if Not Being Towed — Liability Coverage Not Extended: George parked his fifth-wheel trailer on the shoulder of a road, unattached to a towing vehicle. A person driving on the road collided with the trailer and subsequently filed an action against George for damages for bodily injury and property damage resulting from the collision. George submitted a claim with his insurer requesting liability coverage. The insurer denied coverage and requested a determination that it had no obligation to defend George or pay any damage award, based on the definition of "utility trailer" in the policy. The policy defined a utility trailer as "a vehicle designed to be towed by a private passenger car or farm car, including a farm wagon or farm implement, while towed by a private passenger car, utility car, or farm car". The District Court correctly determined that George's trailer was not a utility trailer because it was not being towed by another vehicle at the time of the accident, so coverage was excluded. Based on the clear policy language, the Supreme Court affirmed. Nat'l Farmers Union Property & Cas. Co. v. George, 1998 MT 205, 290 M 386, 963 P2d 1259, 55 St. Rep. 873 (1998).

Rules Agreed Upon in Settlement Agreement as Binding Upon Arbitration: Parties agreed in a settlement agreement that controversies would be settled pursuant to the Commercial Arbitration Rules of the American Arbitration Association. A contention by one party that arbitration under those rules would be less efficient, slower, or more expensive than arbitration under Montana's Uniform Arbitration Act was immaterial. The parties were required to arbitrate according to the rules specifically designated in the settlement agreement. Ratchye v. Lucas, 1998 MT 87, 288 M 345, 957 P2d 1128, 55 St. Rep. 354 (1998).

Attorney Fees Payable Under Clear Language of Contract — Costs Awarded as Matter of Course: It was error for the trial court to order the parties to pay their own attorney fees and costs when the clear and unambiguous language of the property sale contract in question provided that plaintiffs, as the successful party, were entitled to recover fees. Further, under 25-10-101, plaintiffs were entitled to the award of court costs, as a matter of course, by virtue of receiving judgment in their favor. Quigley v. Acker, 1998 MT 72, 288 M 190, 955 P2d 1377, 55 St. Rep. 295 (1998).

Five Agreements Constituting Integrated Sales Agreement With Condition Precedent — Overriding Previous Partnership Agreements and Providing for Attorney Fees: Daines argued that of the five agreements executed by the parties, the option agreement should have been read separately and interpreted as an option to buy conferring a privilege but not imposing an obligation and that on that basis, he could not be liable for not completing a purchase agreement. The Supreme Court held that the lower court had properly looked at the five agreements as a whole in interpreting the parties' intent and had correctly concluded that the agreements constituted an integrated sales agreement subject to conditions precedent. The Supreme Court further held that since the five agreements constituted a sales agreement, they superseded the previous partnership agreements. The respondents were not liable for capital contributions as partners, and the default provision in the option agreement providing for attorney fees did apply to the agreement created by all five of the documents executed by the parties. Daines v. Knight, 269 M 320, 888 P2d 904, 52 St. Rep. 8 (1995).

Insurance Contract:

Waller's injuries arose out of the operation and use of an aircraft, but he was not a residence employee or farm employee at the time. Policy coverage was explicitly excluded for bodily injury arising from the ownership, maintenance, operation, use, loading, or unloading of aircraft. The clear language of the contract exempted the airplane accident from coverage. Summary judgment on the issue of policy inapplicability was proper. Truck Ins. Exch. v. Waller, 252 M 328, 828 P2d 1384, 49 St. Rep. 318 (1992), followed in Wellcome v. Home Ins. Co., 257 M 354, 849 P2d 190, 50 St. Rep. 305 (1993).

Even though auto dealer remained record owner of automobile after its sale by his failure to send proper certificates to Registrar of Motor Vehicles, dealer's liability insurance policy, which was limited in its coverage by clear and explicit language, did not insure motorist who had purchased vehicle. Universal Underwriters Ins. Co. v. St. Farm Mut. Auto. Ins. Co., 166 M 128, 531 P2d 668 (1975).

Inability of insurer to write malpractice insurance in state and fact that insured carried malpractice insurance with another company could not be considered in determining intentions of parties to comprehensive liability insurance policy, since policy was unambiguous. Home Ins. Co. v. Pinski Bros., Inc., 156 M 246, 479 P2d 274 (1971).

Improper Modification of Maintenance Awarded "For Life": The District Court modified a property settlement agreement, which provided that the wife receive $300 a month "as maintenance for life" in lieu of property for which she was to receive income, after husband unilaterally discontinued maintenance when wife began receiving social security payments. The maintenance agreement was a plain and unambiguous contract between the parties that was not subject to later interpretation or construction by a court. The agreement was drawn up by husband, a practicing attorney, who clearly understood the meaning of the term "for life". The District Court erred in modifying the agreement, absent a showing of substantial credible evidence that modification was warranted, without considering all necessary information in the original settlement agreement. In re Marriage of McKeon, 252 M 15, 826 P2d 537, 49 St. Rep. 127 (1992), followed in In re Marriage of Woodford, 254 M 501, 839 P2d 574, 49 St. Rep. 887 (1992).

Parked Trailers Unattached to Insured Tractors — No Coverage Under Unambiguous Policy Provisions: The District Court found an insurance policy to be ambiguous regarding coverage for trailers that had been used to haul beer but that were parked and used for storage at the time they were accidentally run into and granted summary judgment for insurer based on that ambiguity. The Supreme Court found no ambiguity in policy language that clearly covered only trailers that were attached to an insured tractor. Citing its authority in Hereford v. Hereford, 183 M 104, 598 P2d 600 (1979), the Supreme Court reversed and granted summary judgment to the nonmoving party based on the fact that the unambiguous policy language created no genuine issue of material fact. Canal Ins. Co. v. Bunday, 249 M 100, 813 P2d 974, 48 St. Rep. 597 (1991).

Contingency to Exist in Language of Agreement: The plaintiff held a security interest in 50% of the stock of a business as security for a promissory note from her ex-husband. The defendants wanted to purchase the entire business and executed a promissory note to the plaintiff for her interest. Thereafter, the defendants were unable to complete the purchase and sought a declaratory ruling that the promissory note with the plaintiff was contingent on their being able to acquire full ownership of the business. The lower court ruled that the note was contingent on purchase of the remaining interest, but the Supreme Court reversed on the grounds that the lower court could not look beyond the four corners of the document. Bain v. Williams, 245 M 228, 800 P2d 693, 47 St. Rep. 2049 (1990).

Commission as Evidence of Fiduciary Relationship — Rescission by Principal: The District Court did not err in relying on the explicit definition of the word "commission" in finding that a real estate agent who was granted a commission for the sale of a resort while intending to be one of the ultimate purchasers was acting in a fiduciary capacity in his relationship with the principal. Because the relationship existed, the sales agreement was voidable and subject to rescission by the principal. Boyne, U.S.A., Inc. v. Mallas, 236 M 305, 769 P2d 1235, 46 St. Rep. 380 (1989).

Obligation to Veracity of Warrant by Party Drafting It: Real estate was conveyed to plaintiff by "special warranty deed", drafted by defendant, which warrant defendant claimed limited liability to defendant's own acts. It was argued that because defendant did not cause latent defects, liability did not attach. However, by warranting the house, defendant contractually obligated itself to the veracity of the warrant. Because plaintiff relied on defendant's misrepresentations to her detriment, defendant was held liable for the latent defects. Wagner v. Cutler, 232 M 332, 757 P2d 779, 45 St. Rep. 1092 (1988).

Assignment of Estate Rights — Certificate of Deposit Held by Surviving Joint Tenant Not Transferred: A $10,000 certificate of deposit (C.D.) held by a surviving joint tenant was properly not included as an asset of the estate; therefore, a transfer and assignment of the tenant's right, title, and interest in the estate did not affect the C.D., of which tenant was sole owner upon the death of the nonsurviving joint tenant. Yellowstone Bank of Absarokee v. Morse, 226 M 126, 733 P2d 1310, 44 St. Rep. 524 (1987).

Issue of Authorship of Agreement Not Precluding Summary Judgment Where Agreement Not Ambiguous: Where the plaintiffs brought an action for default of a mining lease, arguing that summary judgment for the defendants was precluded by the ambiguity of the lease and a dispute as to its authorship, the Supreme Court held that the provisions governing royalty payments were not ambiguous, that authorship was therefore irrelevant, and that summary judgment was properly granted. The plaintiffs' interpretation of the agreement was absurd because that interpretation required payment of royalties before net smelter returns were received or before the royalties themselves could be calculated. The time and method of calculation of payment by the defendants were entirely consistent with the terms of the parties' agreement. Reading the agreement as a whole, there was no factual issue to preclude summary judgment. Lewis v. St., 207 M 361, 675 P2d 107, 41 St. Rep. 9 (1984).

Intent Clear — No Need to Interpret: Courts have no authority to change a contract when its intent is clear. Courts do interpret contracts when an ambiguity exists. An ambiguity exists when the contract taken as a whole in its wording or phraseology is reasonably subject to two different interpretations. No ambiguity exists in the clause in question in this case. The first sentence states the intent of the clause. The formula following dictates how the intent shall be accomplished. Taken as a whole, the contract is reasonably subject to only one interpretation. The formula is clear and express. Courts may not disregard the express language of a contract. Therefore the District Court properly adopted the formula contained in the clause. Lemley v. Bozeman Community Hotel Co., 200 M 470, 651 P2d 979, 39 St. Rep. 1877 (1982), followed in N.H. Ins. Group v. Strecker, 244 M 478, 798 P2d 130, 47 St. Rep. 1736 (1990). See also Brigham Young Univ. v. Seman, 206 M 440, 672 P2d 15, 40 St. Rep. 1767 (1983), Farmers Union Mut. Ins. v. Kienenberger, 257 M 107, 847 P2d 1360, 50 St. Rep. 179 (1993), and Harris v. St. Vincent Healthcare, 2013 MT 207, 371 Mont. 133, 305 P.3d 852.

Termination of Lease — Use of Appraisal in Arriving at Value: Defendant leased a truck from plaintiff and later defaulted on the lease. A paragraph of the lease provided that "Upon premature termination, lessor shall promptly obtain the highest available cash offer at wholesale. . .". In a suit to collect amounts owing, the District Court relied upon appraisals obtained by plaintiff and disregarded the actual purchase price of the leased vehicle. The Supreme Court held that sufficient testimony was introduced on the value of the vehicle, and the District Court's use of a "wholesale value" and "retail value" in arriving at the figure used was within the meaning of the leasing agreement. R & W Leasing v. Mosher, 195 M 285, 636 P2d 832, 38 St. Rep. 1857 (1981).

Language Plain and Unambiguous — Language Controls — Nothing to Interpret or Construe: In a dispute involving a real estate listing contract where the contract was plain and unambiguous, 1-4-102 is irrelevant. When the language is plain and unambiguous, the language alone controls and there is nothing for the court to interpret or construe. Section 1-4-102 applies when an ambiguity exists in the language of the contract. Payne v. Buechler, 192 M 311, 628 P2d 646, 38 St. Rep. 799 (1981), clarified in Mary J. Baker Revocable Trust v. Cenex Harvest St., Cooperatives, Inc., 2007 MT 159, 338 M 41, 164 P3d 851 (2007).

Language of Lease Controlling on Payment of Property Taxes: In an action for breach of a lease of certain commercial property, the District Court did not err in granting the plaintiff's motion for partial summary judgment, finding the defendants liable for payment of property taxes on the leased property. The District Court granted the motion only by finding that the lease and option to purchase agreement entered into by the parties required the defendants to make the payments. The agreement specifically provided for the payments in clear and unambiguous terms and did not condition payment of the taxes upon exercise of the option. As the language of the contract is clear, its terms must be given effect. Ragen v. Weston, 191 M 546, 625 P2d 557, 38 St. Rep. 456 (1981).

Custody Agreement Interpreted as Contract — No Contempt Found Under Joint Custody Agreement: Where the plaintiff and defendant entered into an agreement for the joint custody of their three children and the agreement was incorporated into a decree divorcing the parties, the trial court committed reversible error in finding, upon a later petition by the plaintiff for modification of the divorce decree, that the decree granted custody of the children to the defendant and in holding the plaintiff in contempt for her custody of one of the children. Agreements for the dissolution of marriage are to be interpreted by the law of contracts, and the language of the agreement controls if it is clear and unambiguous. The plaintiff committed no contemptuous act by retaining custody of one child under a joint custody agreement. Quinn v. Quinn, 191 M 133, 622 P2d 230, 38 St. Rep. 93 (1981).

Employment Contract Controls: There was no need for further interpretation or parol evidence of an employment contract which expressly exempted appellant from recovering overtime compensation. There was no need for construction of any implied contract since there can be no express and implied contract for the same thing existing at the same time. Thus, summary judgment was appropriate. Weston v. Mont. Highway Comm'n, 186 M 46, 606 P2d 150 (1980).

Contract for Joint Purchase of Property — Construction of Contract as a Whole: Where the appellant and respondent entered into an agreement whereby the respondent agreed to loan appellant the downpayment for the purchase of real property on a contract for deed, the District Court correctly looked to the clear language of the instrument as a whole to determine the intention of the parties, and phrases relied on by the appellant would not be taken out of context to reach the result urged by the appellant. Downs v. Smyk, 185 M 16, 604 P2d 307 (1979).

Property Settlement Agreement: The property settlement agreement between Molly and Keith Herrin contained a qualified assignment of stocks to Molly Herrin. The agreement said that if Keith, Jr., died while there was any money or property in any trust, then the trust will cease and all property and income of the trust will revert to Keith Herrin and become his sole property. Keith, Jr., died but no trust existed since a trust was to be established only if Molly died or remarried during Keith, Jr.'s lifetime. Neither of these events occurred. The Supreme Court found that the stocks belonged to Molly after the death of Keith, Jr. Herrin v. Herrin, 182 M 142, 595 P2d 1152 (1979).

Intent Irrelevant if Agreement Clear and Specific — Subordination: Summary judgment is correct when subordination agreement does not present an issue of fact. The plain and clear meaning of the instrument controls and the intent of the parties is ascertained from the instrument. Batey Land & Livestock Co. v. Nixon, 172 M 99, 560 P2d 1334 (1977).

Unambiguous Contract — No Restriction on Use by Life Tenant: Court erred in imposing a restriction on the use of premises when life tenant was granted the right to use premises "as he may deem fit". Danielson v. Danielson, 172 M 55, 560 P2d 893 (1977).

Profit Sharing Agreement: When the intent of the contracting parties was clear from the contract itself that plaintiff was to receive 6% of the gross income of the business without regard to operating gain or deficit, the defendant could not assert a defense that performance of the contract was impossible due to a lack of funds after payment of business debts and expenses. Veterans Rehab. Center v. Birrer, 170 M 182, 551 P2d 1001 (1976).

Lease Modification Must Be Supported by Adequate Consideration: When lessee was entitled to two-thirds of all grain crops harvested, lessor-purchaser's claim that crop belonged to his seller was without merit because the lease was plain and unambiguous and needed no construction. Under the terms of the lease proof of adequate consideration is required to force the lessee to remake that portion of the lease requiring him to give up his two-thirds share. Edwards v. Peavey Co., 170 M 45, 549 P2d 1082 (1976).

Wheat Crop: Unambiguous provision in insurance policy stating that the insurance company agreed to pay all damages which the insured was obligated to pay resulting from injury to tangible property applied to negligent sale of winter wheat seed instead of spring wheat seed, since wheat field and crops were tangible property. Safeco Ins. Co. v. Munroe, 165 M 185, 527 P2d 64 (1974).

Verbal Clarity:

Restrictive covenant giving lessee exclusive right to operate drugstore did not extend to property beyond the plot described in the lease, and summary judgment for lessor was properly granted because the intent of the parties at the time they entered into the agreement was reduced to writing and expressed in clear and explicit language that the exclusive covenant applied to "the entire premises covered by the plans and specifications". Matteucci's Super Save Drug v. Hustad Corp., 158 M 311, 491 P2d 705 (1971).

Clause in disability insurance policy which provided that benefits were payable only in cases involving continuous and total disability within 30 days of date of accident preventing performance of every duty pertaining to insured's occupation precluded insured from recovering benefits under policy where he had returned to work and was able to perform part of his duties since, under this section, language of contract governs its interpretation if language is clear and explicit and as matter of law insured did not come within policy coverage. Nelson v. Combined Ins. Co. of Am., 155 M 105, 467 P2d 707 (1970).

Intention Ascertained From Language: Although a contract of insurance should be construed liberally in favor of insured and strictly against the insurer, contracts of insurance should be given a fair and reasonable construction. In arriving at such construction, no matter how strictly construed against the insurer, the intention of both insurer and insured should be ascertained from the language of the policy. Kansas City Fire & Marine Ins. Co. v. Clark, 217 F. Supp. 231 (D.C. Mont. 1963), affirmed in 329 F2d 647 (9th Cir. 1964).

Crop-Share Agreement: Where contract provided that farm laborer would be paid $150 per month cash, would get 10% of the harvested crops after harvest, and would be expected to stay for a 12-month period, he was entitled to his share of the crop due on his crop-share agreement when wheat and barley were placed in storage at elevator although safflower, in which laborer did not share, had not been cut. Failure of employer to pay laborer's share on demand constituted a breach of contract and it was not necessary for laborer to complete the 12-month term in order to recover his percentage of the crops. Laughnan v. Sorenson, 139 M 531, 366 P2d 433 (1961).

Release: As against the contention that a release given by a claimant to one tortfeasor did not release the other joint tortfeasors because no consideration moved from the others to the plaintiff, and that they were not parties thereto, where the release expressly recited its purpose and intention and showed on its face full satisfaction of the claim arising out of the accident as against all, it was not necessary that consideration move from the other tortfeasors to the claimant, and these matters could not controvert the clear, unambiguous language of the release under this section. Lisoski v. Anderson, 112 M 112, 112 P2d 1055 (1941).

Language Taken as a Whole: In the construction of a contract its language is to be resorted to in the first instance, but the conclusion to be reached depends not upon the verbal clarity of the particular sentences or paragraphs but upon the view to be taken of it in its entirety. Roecher v. Commercial Nat'l Bank, 87 M 570, 289 P 388 (1930).

Court Not to Make New Contract:

Where no legal impediment is shown which would have prevented parties to a contract from entering into it or from expressing it in language of their own, courts must give effect to the meaning and intention of the parties as expressed in the language employed and may not make a new contract for them. The mere fact that as made the contract may appear unreasonable, burdensome, or unwise to one of them is insufficient to avoid it, where the latter party was of legal age, had all the facts clearly before him long prior to its execution, and his alleged damage was due to his own inattention and carelessness. Hinerman v. Baldwin, 67 M 417, 215 P 1103 (1923).

It is the province of courts to interpret contracts which are open to interpretation, not to make new ones for the parties, or to alter or amend those which they themselves have made. Emerson-Brantingham Implement Co. v. Raugstad, 65 M 297, 211 P 305 (1922).

28-3-402. Reference to circumstances permissible.

Case Notes

Port Authority Insured Under County Insurance Policy — Extrinsic Evidence Considered — Policy Construed Against Drafter — Insurer Not Immune From Suit as Reinsurer: After a port authority building was destroyed by a fire, the port claimed that it qualified as an insured under a county insurance company policy that included county members and any other county entities that receive insurance through a county joint insurance authority. The insurance company claimed that the language in the policy did not extend to county entities such as the port. Additionally, the insurance company claimed that it was a reinsurer and therefore it was improper for the port to bring a direct claim against it. The Supreme Court held that the port qualified as an insured under terms of the policy and that a direct claim was proper. In reaching a conclusion that was contrary to the language of the policy, the court gave meaning to the entire contract, considered extrinsic evidence, and construed ambiguous language in the policy against the insurer as the drafter. In determining that a direct claim was proper, the court reasoned that the port dealt directly with the insurance company, and therefore the insurer was an excess insurance carrier, rather than a reinsurer. Lincoln County Port Authority v. Allianz Global Risks US Ins. Co., 2013 MT 365, 373 Mont. 60, 315 P.3d 934.

Genuine Issue of Material Fact Whether Dam Operation Damaged Lakeshore Properties — Summary Judgment Improper — Class Action Vacated: Flathead Lake landowners brought a class action suit against defendant operators of Kerr Dam for operating outside the scope of their easements in a manner that continuously eroded and damaged plaintiffs' lakeshore properties. The District Court rejected plaintiffs' argument that the dam operator was not allowed to affect plaintiffs' properties above an elevation of 2,893 feet, concluding instead that defendants' easements covered entire parcels. The court concluded that erosion, including wave action erosion, was within the scope of the easements and held that any duty defendants had to not cause unreasonable damage to plaintiffs' properties applied only to damage unrelated to use of the easement. Therefore, summary judgment was granted to defendants, and plaintiffs appealed. The Supreme Court first agreed that the District Court's contour line theory was correct. The "2,893 feet" clause did not establish the vertical limit argued by plaintiffs because although the dam operators' right to flood, subirrigate, drain, or otherwise affect the shoreline was not unlimited, it was not restricted to a maximum elevation of 2,893 feet at each parcel, but rather extended to whatever part of each parcel was affected when the lake was held at 2,893 feet above mean sea level as measured at the dam. The court also agreed that the right to cause some erosion was necessary to the enjoyment of the right to perpetually flood, subirrigate, and drain and was thus included by implication in the easements. However, further factual development and trial were necessary to address the question of whether the erosion was reasonable, necessary, and within the scope of the easements, which could not be resolved by summary judgment. Additionally, the question of whether defendants breached their obligation to not cause unreasonable damage to the shoreline properties and to not unreasonably interfere with plaintiffs' enjoyment also required further factual development and possibly trial. Therefore, the order certifying the case as a class action was vacated and the case was remanded for further consideration. Mattson v. Mont. Power Co., 2009 MT 286, 352 M 212, 215 P3d 675 (2009).

No Ambiguity in Complete, Final Sales Agreement — Parol Evidence Inadmissible: The parties entered a sale agreement for a ready-mix concrete plant. Plaintiff subsequently filed an action alleging that defendant violated the agreement by breaching the covenant to not compete and the covenant of good faith and fair dealing, which constituted malice resulting in lost profits, sales, and goodwill. The District Court granted summary judgment to defendant and plaintiff appealed, but the Supreme Court affirmed. The District Court correctly concluded that the sales agreement constituted a complete, final agreement and unambiguously did not include a noncompetition provision, but in fact provided that plaintiff would sell concrete to defendant for use in the area. The intention of the parties was ascertainable from the writing alone, and the agreement was presumed to represent all transactions regarding elements extrinsic to the agreement and was thus considered complete and final, so parol evidence was inadmissible. Richards v. JTL Group, Inc., 2009 MT 173, 350 M 516, 212 P3d 264 (2009). See also Lindey's, Inc. v. Professional Consultants, Inc., 244 M 238, 797 P2d 920 (1990), and Mary J. Baker Revocable Trust v. Cenex Harvest States, Cooperatives, Inc., 2007 MT 159, 338 M 41, 164 P3d 851 (2007).

Evidence of Circumstances Under Which Instrument Made Admissible for Determining Ambiguity: As a general rule, evidence of the circumstances under which an instrument was made may not be considered when the language of the instrument is clear and certain in its terms. However, objective evidence of those circumstances, including the situation of the subject of the instrument and the parties to it, may be shown and considered to aid the court in determining, as a preliminary matter, whether the instrument contains an ambiguity. If the court determines that no ambiguity exists, then the extrinsic evidence may not be considered further, but if the court determines that an ambiguity is present in the instrument, then the extrinsic evidence may be introduced at trial to allow the trier of fact to determine the intent of the parties in entering into the contract. In the present case, both parties agreed that language in a right-of-way contract was unambiguous, so the trial court did not err in refusing to consider the circumstances under which the contract was made. Mary J. Baker Revocable Trust v. Cenex Harvest St., Cooperatives, Inc., 2007 MT 159, 338 M 41, 164 P3d 851 (2007). See 11 Williston on Contracts, 33:39 (4th Ed. 1999).

Use of Phrase "Together With" in Contract Not Considered Limiting Language: The contract for a utility right-of-way granted defendants the right to construct, maintain, and operate a pipeline for the transportation of oil, liquids, and gases "together with" a buried fiber optic communications cable. The right-of-way landowners contended that the phrase "together with" unambiguously limited the use of the cable to operating and monitoring the pipeline and precluded defendants from leasing part of the cable to a third party for telecommunication purposes. The District Court disagreed, holding that the phrase meant nothing more than "and", rather than plaintiffs' limiting interpretation "in connection with", and granted summary judgment for defendants. The landowners appealed, but the Supreme Court affirmed. The term "together with" in the granting language did not unambiguously limit defendants' use of the fiber optic cable to operating and monitoring the pipeline. Mary J. Baker Revocable Trust v. Cenex Harvest St., Cooperatives, Inc., 2007 MT 159, 338 M 41, 164 P3d 851 (2007).

Five Agreements Constituting Integrated Sales Agreement With Condition Precedent — Overriding Previous Partnership Agreements and Providing for Attorney Fees: Daines argued that of the five agreements executed by the parties, the option agreement should have been read separately and interpreted as an option to buy conferring a privilege but not imposing an obligation and that on that basis, he could not be liable for not completing a purchase agreement. The Supreme Court held that the lower court had properly looked at the five agreements as a whole in interpreting the parties' intent and had correctly concluded that the agreements constituted an integrated sales agreement subject to conditions precedent. The Supreme Court further held that since the five agreements constituted a sales agreement, they superseded the previous partnership agreements. The respondents were not liable for capital contributions as partners, and the default provision in the option agreement providing for attorney fees did apply to the agreement created by all five of the documents executed by the parties. Daines v. Knight, 269 M 320, 888 P2d 904, 52 St. Rep. 8 (1995).

Sufficient Evidence to Establish Contract for Line of Credit: The execution of a promissory note and the procurement by the bank of a contract of guarantee issued by the Farmers Home Administration (FmHA) pointed to and confirmed an agreement between plaintiffs and the bank for a line of credit, despite bank's contention that the contract of guarantee was between the bank and FmHA and created no obligation on bank's part to loan money to plaintiffs. Weinberg v. Farmers St. Bank of Worden, 231 M 10, 752 P2d 719, 45 St. Rep. 391 (1988), distinguished in Shiplet v. First Sec. Bank of Livingston, Inc., 234 M 166, 762 P2d 242, 45 St. Rep. 1816 (1988), and in Lachenmaier v. First Bank Sys., Inc., 246 M 26, 803 P2d 614, 47 St. Rep. 2244 (1990).

Commission Agreement Found Unambiguous — Use of Extrinsic Evidence to Prove Lack of Ambiguity Upheld: Where the defendant seller of real estate made a commission agreement with the plaintiff providing for payment of the commission out of the receipts from the contract for deed, the District Court did not err in holding that money received by the defendant under a modification of the contract for deed could not be used to calculate the amount of commission owed to the plaintiff. The terms of the commission contract were not ambiguous and show that it was the intent of the parties to count only that money received under the original agreement. The District Court properly looked to the terms of the contract for deed only to determine whether an ambiguity existed in the commission agreement, and having determined there was none, properly excluded other evidence of the parties' intent in making the commission agreement. Martin v. Community Gas & Oil Co., 205 M 394, 668 P2d 243, 40 St. Rep. 1385 (1983).

Contract Provisions Ascertainable by Conduct of Parties: Where electrical contractor submitted a bid on a job based not on written specifications but on a previous similar job and the previous pattern of conduct between the parties indicated that both parties contemplated the rendering of particular services and materials, contract was not so ambiguous as to render its object wholly unascertainable. Mathis v. Daines, 196 M 252, 639 P2d 503, 39 St. Rep. 73 (1982).

Written and Oral Real Property Agreements — No Timing of Valuation Provision: The parties were married in 1973. They entered a prenuptial agreement providing that the real and personal property of each would remain separate. In 1974, defendant brought a quiet title action against his sisters. He executed a handwritten agreement with plaintiff that if she would finance the legal expenses of the action he would give her 10% of the land or the value thereof. He was successful, and the parties entered into an oral agreement containing the same provisions for appellate costs. The trial court found that defendant owed plaintiff 20% of the value of the land and that the value was to be determined at the time he elected to pay and be based on 20% of the value of all the land. The Supreme Court held that the defendant, under the clear terms of the written contract, had the option to select the acreage which he wished to convey. The District Court disregarded this language in ordering him to convey the percentage of his land as a whole. Since no contract provision addressed the timing of the valuation of the land and conflicting evidence was presented, the District Court's determination that it be valued at the time of payment was upheld. Kartes v. Kartes, 195 M 383, 636 P2d 272, 38 St. Rep. 1941 (1981).

Termination of Lease — Removal of Holdover Tenant — Agricultural Exception to Landlord-Tenant: Defendant sold plaintiff her property. The instrument contained a lease back to defendant of the buildings and 6 acres. Plaintiff gave notice that the lease was to terminate. Defendant refused to vacate. Plaintiff brought an action under the unlawful detainer statutes which provide for an award of treble damages. Defendant contended the dispute was governed by the Montana Residential Landlord and Tenant Act of 1977. Plaintiff contended the lease was within the "agricultural" exclusion contained in 70-24-104(8). The lease provisions gave no indication of the nature of the buildings or of the intended use of the 6 acres. The trial court allowed the introduction of photographs and oral testimony regarding the lease, which established that the use of the land was for maintenance of defendant's livestock. The trial court properly allowed parol evidence to resolve an ambiguity in the lease. The Supreme Court determined that the legislative intent of 70-24-104 was for a comprehensive coverage of all agricultural operations, whether they are large-scale operations for profit or small-scale operations secondary to the use of the residence. The unlawful detainer provisions were properly applied. Dussault v. Hjelm, 192 M 282, 627 P2d 1237, 38 St. Rep. 738 (1981).

Serious Weight: This section requires that a court give serious weight to the purpose and circumstances leading up to the execution of a contract when the court is required to interpret the language. Energy Oils, Inc. v. Mont. Power Co., 626 F2d 731 (C.A. Mont. 1980).

"Sell or Otherwise Dispose" — Reference to Circumstances to Explain: It was proper for the District Court to look to the circumstances to explain the ambiguous phrase "sell or otherwise dispose". Jappe v. Co-op Supply, Inc., 183 M 397, 600 P2d 184 (1979).

Contract for Lease of Vehicle: When a dispute as to whether a truck which was transferred to defendant was subject to an agreement to lease the truck to defendant, evidence of the conduct of the parties in transferring title to protect the plaintiff from liability and of agreed monthly payments was sufficient to establish a rental agreement. Veterans Rehab. Center v. Birrer, 170 M 182, 551 P2d 1001 (1976).

Contract of Sale:

Substantial credible extrinsic evidence warranted resolution of ambiguity concerning grazing permits in real estate sales contract in favor of buyers who were repeatedly assured during final negotiations that permits would be transferred to them as part of deal. Dooling v. Casey, 152 M 267, 448 P2d 749 (1969).

A telegram, "Wire lowest price you will sell 7,000 S. & W. yearling ewes", and an answering telegram, "Lowest price on S. & W. yearling ewes eleven fifty this subject to immediate acceptance", together with custom and usage and 28-3-201, 28-3-102, and this section, evidenced a complete contract for the sale of the sheep, where defendant's offer was accepted within 24 hours, as against an objection that there was no meeting of the minds of the parties upon the price to be paid for the sheep, in that price could only be determined upon delivery and that the offer was not accepted immediately. Story v. Stanfield, 275 F 401 (9th Cir. 1921).

Evidence explanatory of the circumstances leading up to the making of a written contract of sale as well as of the conversation had between the defendant and plaintiff's agent at the time it was made is admissible under this section. Nat'l Cash Register Co. v. Wall, 58 M 60, 190 P 135 (1920).

Intention of Parties:

Where there is ambiguity in a contract, it is open under this section and 28-3-301 to interpretation by the aid of evidence aliunde, so as to give effect to the mutual intention of the parties to it at the time it was made. McNussen v. Graybeal, 146 M 173, 405 P2d 447 (1965); Butte Water Co. v. Butte, 48 M 386, 138 P 195 (1914).

Extrinsic evidence is admissible to explain the true intentions of the parties to an "output" contract since the terms of the contract are ambiguous and such contracts must be interpreted in light of circumstances surrounding prior business dealings. McNussen v. Graybeal, 146 M 173, 405 P2d 477 (1965).

A contract must receive such an interpretation as will make it lawful, operative, definite, reasonable, and capable of being carried into effect; it may be explained by reference to the circumstances under which it was made and the matter to which it relates, and however broad may be its terms, it extends only to those things concerning which it appears that the parties intended to contract, particular clauses being subordinate to its general intent. Custer v. Missoula Pub. Serv. Co., 91 M 136, 6 P2d 131 (1931).

Lease: Where there is an uncertainty in a contract it is to be interpreted most strongly against the person who caused the uncertainty to exist. Thus where there was a question as to what were intended to be improvements as contemplated by the $1200 rent provisions of the lease and both the lessor and the lessee gave testimony, it was error for the court to disregard such testimony. Consideration of the improvements made by the lessee should be given by the lower court and the value of these items offset against the rents contemplated. Hempstead v. Allen, 126 M 578, 255 P2d 342 (1953).

Intent Ascertained From Conduct:

In the construction of contracts such as a teacher's contract of employment, courts may look not only to the language employed but to the subject matter and the surrounding circumstances and may avail themselves of the same light which the parties possessed when the contract was made. To ascertain the intention of the parties to a contract, regard must be had to the nature of the instrument, the condition of the parties executing it, the objects which they had in view, and the words employed. If the words are capable of more than one meaning, they are to be given that meaning which it is apparent the parties intended them to have. The practical interpretation of a contract which the parties placed upon it by their course of conduct over a period of years is entitled to great, if not controlling, influence in ascertaining what they understood by its terms. Smith v. School District, 115 M 102, 139 P2d 518 (1943).

Lease was not void for failing to designate the time and place for a division of the crops provided for since under 28-3-102 any uncertainty in that respect was determinable by the custom or usage observed in the vicinity in the light of the surrounding facts and circumstances bearing upon the transaction. McDonald v. McNinch, 63 M 308, 206 P 1096 (1922).

Endorsement of Note: The minutes of a meeting of the Board of Directors of a corporation attested as correct by its president, plaintiff in an action on the corporation's note against endorsers thereon, acquired by plaintiff after maturity, tending to show that plaintiff knew that when the endorsements were made, defendants endorsed as representatives of various farmers' associations and not in their individual capacities, were admissible in support of the defense disclaiming personal responsibility for its payment. Anderson v. Border, 75 M 516, 244 P 494 (1926).

Application of Section:

In an action by the payee of a promissory note against the maker, it was a valid defense that the note was delivered upon the condition that the maker should not be held liable thereon, pursuant to a written agreement between the parties, and in support of the plea evidence of the circumstances leading up to the making of the agreement and resulting in the delivery of the note was admissible. U.S. Nat'l Bank of Red Lodge v. Chappell, 71 M 553, 230 P 1084 (1924).

While in the interpretation of a contract, the language of which is ambiguous and uncertain, the attending circumstances may be examined to determine its proper construction, this may not be done where its language is clear and unambiguous. Berne v. Stevens, 67 M 254, 215 P 803 (1923).

Commission Sales: Where a commission agreement for sale of automobiles was little more than a memorandum of certain points of the parties' agreement, it was proper for the court to go into the circumstances surrounding the agreement. Brockway v. Blair, 53 M 531, 165 P 455 (1917).

Part 5

Interpretation of Words

28-3-501. Words generally understood in their ordinary sense.

Case Notes

Damage From Rain Event Discovered Months Later Sudden and Accidental: The roof of an RV sustained a large tear, likely from an overhanging tree branch, that went unnoticed by the owners. Soon after, the RV was parked uncovered in a storm during which a large amount of rain fell in a short period of time. Water entered the RV through the tear, seeped through cavities in the wall panel, and eventually became evident to the owners months later. The defendant insurance company covered the roof repair but declined to cover the repair of the wall panel. The owners filed suit to recover for the wall panel repair and associated expenses, and the parties filed cross-motions for summary judgment. The District Court ruled in favor of the defendant insurance company, finding that because the damage from the water entering the wall cavity did not become evident for months after the storm, it was not "sudden" as required for coverage under the policy. On appeal, the Supreme Court disagreed, finding that the wall panel would have needed to be removed for repairs as soon as the water entered, and the value of the RV was diminished as soon as the water became trapped. The Supreme Court reversed the grant of summary judgment and remanded the case. Kaul v. State Farm Mut. Auto. Ins. Co., 2021 MT 67, 403 Mont. 387, 482 P.3d 1196.

Fire Disposing of Felled Trees That Posed Risk to Vehicles — No Coverage for Damages Caused by Fire Under Motor Vehicle Policy: The neighbor of the plaintiff felled dead trees on his property because he was concerned they might fall on his work vehicles. After felling the trees, he burned them and ashes from that fire caused another fire that damaged the plaintiff's property. The neighbor conceded negligence and assigned the rights to his insurance to the plaintiff, who then sued the defendant insurance company. Although the defendant denied coverage, the District Court granted summary judgment in the plaintiff's favor. On appeal, the Supreme Court reversed, holding that the fire did not result from the maintenance of the neighbor's vehicles. The Supreme Court explained that the neighbor's decision to burn the trees after they had been cut and no longer posed a threat to his vehicles was not an inherent part of vehicle maintenance. Assoc. Dermatology & Skin Cancer Clinic of Helena, P.C. v. Mtn. West Farm Bureau Mut. Ins. Co., 2017 MT 30, 386 Mont. 298, 389 P.3d 1027.

No Duty of Insurer to Cover City's Conversion of Pension Funds: The city of Dillon failed to properly pay pension benefits, even though the city received the money from the state. When a beneficiary sued the city to recover unpaid benefits, the city tendered defense of its claim to its insurer, but the insurer declined to provide coverage or defend the claim based on a financial gain exclusion in the insurance policy. The beneficiary was granted summary judgment, so the city paid the judgment and filed an action to recover against the insurer. The District Court held that the insurer was liable and breached its duty to defend, so the insurer appealed. The Supreme Court held that the insurer had no duty to provide coverage to the city because the city's claim arose in whole or in part from the city's unlawful retention and conversion of the pension funds, so the city had no coverage for the claims for return of principal and interest. The District Court was reversed. Dillon v. Mont. Municipal Ins. Authority, 2009 MT 393, 353 M 370, 220 P3d 623 (2009).

Casino That Serves Alcohol Considered Bar or Tavern: Defendant owned a shopping center where plaintiff leased space. Pursuant to a 1973 lease agreement, no part of the shopping center was to be leased for a bar or tavern without the tenant's prior written consent. Defendant leased space to a casino and card room that also served alcoholic beverages. Plaintiff contended that defendant violated the original lease provisions prohibiting a bar or tavern. The District Court held that the casino fell under the common and ordinary understanding of a bar or tavern and granted summary judgment for plaintiff without a hearing. On appeal, defendant contended that the term "bar or tavern" in the lease language was ambiguous and created an issue of fact regarding the intent of the original parties to the contract, noting that the District Court used two separate dictionary definitions and a statutory definition in the Montana Clean Air Act to define the term. Defendant asserted ambiguity because any of three definitions might apply: (1) an establishment with the primary purpose of selling alcohol to be consumed on the premises; (2) an establishment that sells alcohol pursuant to a state liquor license for consumption on the premises; or (3) an establishment that does not include a casino or card room. However, defendant provided no authority to show that its alternative definitions reflect the ordinary or popular meaning of bar or tavern. The District Court's use of three definitions simply illustrated that the casino qualified as a bar or tavern under any of the three definitions, not that ambiguity existed in the definition. The District Court correctly concluded that the casino constituted a bar or tavern. The District Court also did not abuse its discretion in granting summary judgment without a hearing under these circumstances, given that either party could have requested a hearing to present evidence of a genuine issue of material fact but failed to do so. Dollar Plus Stores, Inc. v. R-Mont. Associates, 2009 MT 164, 350 M 476, 209 P3d 216 (2009), following SVKV, LLC v. Harding, 2006 MT 297, 334 M 395, 148 P3d 584 (2006).

Bodily Injury in Insurance Policy May Include Mental or Psychological Injury Accompanied by Physical Manifestations — Jacobsen Overruled: Defendant caused an automobile accident that injured two brothers, one of whom suffered severe trauma and was hospitalized for an extended period. The boys' mother filed a negligence action against defendant claiming emotional and physical injuries to herself and the brother who was not struck by the vehicle, including the mother's stress, migraine headaches, pain, depression, and a rapid heartbeat when hearing sirens, and the brother's withdrawal. Defendant sought liability coverage from her insurer, and the District Court, relying on Jacobsen v. Farmers Union Mut. Ins. Co., 2004 MT 72, 320 M 375, 87 P3d 995 (2004), granted the insurer's motion for a declaratory judgment on grounds that the insurer was not obligated to provide a defense or coverage to defendant because defendant's policy did not cover the claimed emotional injuries or physical injuries resulting from the emotional injuries within the definition of bodily injury. On appeal, the Supreme Court reexamined the Jacobsen analysis in light of subsequent case law and overruled Jacobsen. Bodily injury as construed in an insurance policy includes a mental or psychological injury that is accompanied by physical manifestations. Defendant's insurance policy provided general coverage for damages that the insured was legally obligated to pay because of a bodily injury sustained by any person, which in this case included the physical manifestations that accompanied the mother's and brother's mental and psychological injuries. Allstate Ins. Co. v. Wagner-Ellsworth, 2008 MT 240, 344 M 445, 188 P3d 1042 (2008), followed in Tucker v. Farmers Ins. Exch., 2009 MT 247, 351 M 448, 215 P3d 1 (2009).

Use of Phrase "Together With" in Contract Not Considered Limiting Language: The contract for a utility right-of-way granted defendants the right to construct, maintain, and operate a pipeline for the transportation of oil, liquids, and gases "together with" a buried fiber optic communications cable. The right-of-way landowners contended that the phrase "together with" unambiguously limited the use of the cable to operating and monitoring the pipeline and precluded defendants from leasing part of the cable to a third party for telecommunication purposes. The District Court disagreed, holding that the phrase meant nothing more than "and", rather than plaintiffs' limiting interpretation "in connection with", and granted summary judgment for defendants. The landowners appealed, but the Supreme Court affirmed. The term "together with" in the granting language did not unambiguously limit defendants' use of the fiber optic cable to operating and monitoring the pipeline. Mary J. Baker Revocable Trust v. Cenex Harvest St., Cooperatives, Inc., 2007 MT 159, 338 M 41, 164 P3d 851 (2007).

Plain Contract Language Establishing Operating Agreement Rather Than Franchise Agreement — Summary Judgment Proper: Defendant ran residential care facilities for plaintiff and asserted that the parties' contract established a franchise allowing defendant to collect franchise fees and royalties. The District Court found that although there were contractual obligations between the parties, there was no evidence of privity between the parties and no genuine issue of material fact regarding whether a franchise existed, so plaintiff was entitled to summary judgment. On appeal, the Supreme Court examined the plain language of the contract and determined that there was no special meaning ascribed to the term "franchise", that the contract was essentially an operating agreement rather than a franchise agreement, and that no ambiguity was created concerning defendant's rights to collect franchise fees and royalties. No fact question regarding the parties intention existed, so summary judgment was proper, and the District Court was affirmed. SVKV, L.L.C. v. Harding, 2006 MT 297, 334 M 395, 148 P3d 584 (2006).

No Ambiguity in Restrictive Covenant Prohibiting Placement of Trailers and Mobile Homes Upon Property — Development of Recreational Vehicle Park Precluded: A restrictive covenant provided that no trailers or mobile homes were to be placed upon the property conveyed by a deed. The District Court held that the term "placed upon" contemplated permanent placement, and that temporary placement was therefore not precluded. The court also held that the covenant disallowed only trailer houses or mobile homes used for residences. The court thus concluded that the covenant did not disallow development of the property as a campground for recreational vehicles and travel trailers. On appeal, the Supreme Court noted that language in a restrictive covenant should be understood in its ordinary and popular sense. It is not the role of a court to insert modifying language into clearly written and unambiguous written instruments, and the unambiguous language in the covenant contained no words to indicate the parties' intent to allow temporary trailers or mobile homes not used as residences. The District Court erred in modifying the covenant language to allow trailers to be placed on the property, so the conclusion that a campground for recreational vehicles and travel trailers was allowable was reversed. Creveling v. Ingold, 2006 MT 57, 331 M 322, 132 P3d 531 (2006).

Process for Amending Restrictive Covenant to Be Strictly Followed: Myers contended that a subdivision corporation did not follow the proper method for amending a restrictive covenant disallowing the rental of subdivision property for less than 30 days. The District Court disagreed, holding that the amendment was properly adopted and restrained Myers from renting the property for less than 30 days. Myers appealed. The Supreme Court held that because restrictive covenants must be strictly construed, when a covenant is amended to impose an impediment on use of the property, the method prescribed for amending the covenant must also be strictly followed. In this case, Myers established that the prescribed amendment method was not used, so the Supreme Court reversed the judgment. Point Serv. Corp. v. Myers, 2005 MT 322, 329 M 502, 125 P3d 1107 (2005).

No Contractual Definition of Cause — Discretionary Termination of Professional Sports Team Coach Related to Legitimate Business Needs Warranted: Cole was fired as a professional hockey coach because of the team's poor performance. Cole's 5-year employment agreement contained a clause, drafted by Cole, providing that if Cole was terminated without cause, he would receive 1 year's salary and a bonus. Although the contract did not contain a definition of cause, the District Court found that the termination was without cause. The Supreme Court disagreed. Applying de novo review of the District Court's summary judgment to interpret the employment contract terms in their ordinary and popular sense and construing any uncertainty in the contract language against Cole, who drafted it, the Supreme Court held that discharging the coach of a poorly performing professional sports team was a discretionary decision related to the legitimate needs of the business and constituted cause, so the employer had a legitimate business reason to terminate the coach. Thus, Cole was not entitled to recover under the contract. Cole v. Valley Ice Garden, LLC, 2005 MT 115, 327 M 99, 113 P3d 275 (2005).

Payment of Actual Costs and Discretionary Attorney Fees Under Contract: A real estate contract provided that the award of reasonable attorney fees to the prevailing party was discretionary with the court and also provided that the prevailing party was entitled to actual costs. The District

Court deducted fees and costs related to actions in which plaintiff did not prevail, resulting in a reduction of both attorney fees and costs. On appeal, the Supreme Court affirmed the attorney fee award as an appropriate exercise of the District Court's discretion, but reversed the reduced award of costs because plaintiff was entitled to actual costs under the contract. Gullett v. Van Dyke Constr. Co., 2005 MT 105, 327 M 30, 111 P3d 220 (2005).

Rules for Interpretation of Restrictive Covenants: Restrictive covenants are construed under the same rules of construction as other contracts. Declarations of covenants are read on their four corners as a whole, and terms are construed in their ordinary or popular sense. Bordas v. Virginia City Ranches Ass'n, 2004 MT 342, 324 M 263, 102 P3d 1219 (2004), following Windemere Homeowners Ass'n, Inc. v. McCue, 1999 MT 292, 297 M 77, 990 P2d 769 (1999), and followed in Point Serv. Corp. v. Myers, 2005 MT 322, 329 M 502, 125 P3d 1107 (2005).

Bodily Injury Not Inclusive of Emotional or Psychological Injury Within Terms of Uninsured Motorist Policy: Jacobsen was driving a car insured by defendant when he stopped to assist another motorist who was unconscious with a bleeding head wound. Despite Jacobsen's ministrations, the motorist died a few days later, and the cause was determined to be suicide. The next year, Jacobsen began seeking treatment for emotional distress suffered as a result of the incident and filed a claim with defendant to recover uninsured motorist benefits and medical pay benefits. The District Court granted summary judgment for defendant, and Jacobsen appealed on grounds that his policy for uninsured motorist coverage included damages for bodily injury sustained by the insured caused by an accident. The Supreme Court held that the term "bodily injury" was not ambiguous and was limited to physical injury caused by an accident but did not include emotional or psychological injuries. Thus, Jacobsen's emotional injury, including resulting physical manifestations, did not constitute bodily injury as defined in the insurance contract and was not compensable. Jacobsen v. Farmers Union Mut. Ins. Co., 2004 MT 72, 320 M 375, 87 P3d 995 (2004), following Bain v. Gleason, 223 M 442, 726 P2d 1153 (1986), and Aetna Life & Cas. Co. v. First Sec. Bank of Bozeman, 662 F. Supp. 1126 (D.C. Mont. 1987). Jacobsen was overruled in Allstate Ins. Co. v. Wagner-Ellsworth, 2008 MT 240, 344 M 445, 188 P3d 1042 (2008), to the extent that bodily injuries include mental or psychological injuries that are accompanied by physical manifestations.

Ambiguous Settlement Agreement Language Regarding Maintenance Calculation — Gross Disposable Income Interpreted as Pretax Income: A settlement agreement provided that monthly maintenance payments be 15% of the husband's gross disposable income. In direct opposition to the husband's interpretation, the wife and her expert contended that the amount should be based on pretax rather than after-tax income, and the District Court agreed. The court found that the term gross disposable income was ambiguous because "gross" and "disposable" had mutually exclusive meanings in this context, so the court looked beyond the agreement language to the parties' intent. Because the term was ambiguous, the parties' proposed interpretations were equally proper, so under 28-3-306, the ambiguity was construed in the wife's favor because the maintenance provision was for her benefit. The court's allowance of testimony from the wife's expert was also within the court's discretion. In re Marriage of Mease, 2004 MT 59, 320 M 229, 92 P3d 1148 (2004).

Wendell Test Applied to Determination of Whether Bodily Injury Caused by Accident "Resulting From the Use" of Insured Vehicle: Defendant's son was injured in a hunting accident after riding to the hunt in a vehicle owned by Wajahuski and insured by plaintiff. The insurance policy provided for coverage resulting from the use of a vehicle. The District Court applied the test in Wendell v. St. Farm Mut. Auto. Ins. Co., 1999 MT 17, 293 M 140, 974 P2d 623 (1999), and held that the automobile insurance policy did not provide liability coverage with respect to defendant's claims for bodily injury. Defendant appealed. The Supreme Court affirmed. Even though the Wendell test was originally applied in an uninsured motorist case, the expansive, fact-intensive test also applied here. The phrase "resulting from the use" was ambiguous, so the contract terms were construed in a light most favorable to the insured or other beneficiary. The accident could have occurred in any location, regardless of how the hunters reached their destination. The fact that that particular vehicle was used to transport the hunters and assist in the hunt provided no connection between the use of the vehicle and the hunting accident. Thus, the District Court did not err in holding that the personal injuries were not caused by an accident resulting from the use of the insured motor vehicle. St. Farm Mut. Auto. Ins. Co. v. Ferrin, 2002 MT 196, 311 M 155, 54 P3d 21 (2002).

Doctrine of Reasonable Expectations Inapplicable When Policy Language Excludes Coverage — Liability Coverage on Borrowed Horse Trailer Limited to Policy Terms: Babcock borrowed a horse trailer from her neighbor, and even though the trailer ball on Babcock's truck was too small for the trailer hitch, she attempted to tow the trailer anyway. The trailer came unhooked, left the road, and struck a fence. Farmers Insurance Exchange (Farmers) paid Babcock the full cost of the fence repair. Babcock requested that Farmers also pay for damages to the trailer. Farmers paid $500 toward the trailer, which constituted Babcock's policy limit for collision and comprehensive coverage. Babcock sued, claiming that Farmers was required to pay for the trailer damage under the liability coverage. The District Court granted summary judgment for Farmers, concluding that the plain policy language limited coverage to $500. Babcock appealed, asserting that the policy language was ambiguous but nevertheless created a reasonable expectation that a trailer was covered and that the exclusion for damage "to property owned or being transported by an insured person" did not apply because the trailer was not being "transported" when it was damaged, having separated from the truck. Farmers argued that, under Babcock's interpretation, a passenger ejected from a car would have no claim for medical payments because the passenger did not "occupy" the vehicle at the time of injury. The Supreme Court agreed. The doctrine of reasonable expectations does not apply to create coverage when the terms of the policy clearly demonstrate an intent to exclude particular coverage. In this case, the policy language clearly excluded liability coverage for the borrowed trailer because it was in Babcock's charge and she was transporting it at the time of the accident. Babcock v. Farmers Ins. Exch., 2000 MT 114, 299 M 407, 999 P2d 347, 57 St. Rep. 479 (2000).

"Arising Out of" Ambiguous — Coverage for Liability Not Excluded: Pablos were injured in a vehicle accident involving Moore, who was transporting a landscaping tractor for his employer. The employer was covered by a commercial general liability insurance policy that provided liability insurance for negligent acts of the corporation and its employees. Pablos contended that the employer was negligent in the hiring, training, and supervision of Moore. The employer conceded that the claim arose during the policy period and fell within the definitions of "bodily injury" and "occurrence" and that the policy would provide coverage unless coverage was denied by an exclusion but contended that coverage was excluded under both the exclusion for damages "arising out of" the use of an automobile and the exclusion for damages "arising out of" the transportation of mobile equipment. The District Court held that the term "arising out of" was ambiguous and, construing the instrument against the drafter-insurer, ruled that coverage for Pablos' accident was not excluded under the policy language. Noting that the phrase "arising out of" has been declared ambiguous in another insurance context in Wendell v. St. Farm Mut. Auto. Ins. Co., 1999 MT 17, 293 M 140, 974 P2d 623 (1999), the Supreme Court applied a similar rationale to the phrase in both exclusionary clauses at issue in the present case. The phrase was reasonably subject to more than one interpretation and thus ambiguous. Pursuant to Head v. Cent. Reserve Life of N. America Ins. Co., 256 M 188, 845 P2d 735, 50 St. Rep. 20 (1993), if the terms of an insurance policy are ambiguous, obscure, or open to different constructions, the construction most favorable to the insured or other beneficiary must prevail, particularly if an ambiguous provision attempts to exclude the liability of the insurer. Here, the policy did not clearly and unambiguously exclude coverage for the theories of liability pleaded by Pablos, and the District Court's summary judgment that coverage was owed on Pablos' claims for negligent hiring, training, and supervision of Moore was affirmed. Pablo v. Moore, 2000 MT 48, 298 M 393, 995 P2d 460, 57 St. Rep. 231 (2000), following Marquis v. St. Farm Fire & Cas. Co., 961 P2d 1213 (Kans. 1998).

Original Declaration of Restrictive Covenants Broad Enough to Authorize New or Unexpected Restrictions: A supermajority of subdivision property owners authorized an amendment creating new and unexpected restrictions not contained or contemplated in the original declaration of restrictive covenants, resulting in assessment against subdivision landowners of the costs of paving a common road. Strictly construing the original amendment language, the District Court ruled that the clause in the covenants allowing amendment was broad enough to authorize new or unexpected restrictions. The Supreme Court agreed. Under the rule of strict construction, covenants should not be extended by implication or enlarged by construction. In this case, the drafters of the original covenants used universal language to describe the kinds of changes that could be made, clearly providing that each aspect of the covenants, conditions, restrictions, and uses was subject to amendment by a supermajority. Further, under the universal language, it was unnecessary that amendments to the restrictive covenants be connected to a provision in the original covenants. Windemere Homeowners Ass'n, Inc. v. McCue, 1999 MT 292, 297 M 77, 990 P2d 769, 56 St. Rep. 1173 (1999), following Sunday Canyon Property Owners Ass'n v. Annett, 978 SW 2d 654 (Tex. App. 1998), and distinguishing Lakeland Property Owners Ass'n v. Larson, 459 NE 2d 1164 (Ill. App. 1984), Caughlin Ranch Homeowners Ass'n v. Caughlin Club, 849 P2d 310 (Nev. 1993), and Boyles v. Hausmann, 517 NW 2d 610 (Nebr. 1994).

Gradual Accumulation of Smoke and Soot — "Sudden and Accidental" Construed — Damage Not Covered Under Pollution Exception to All-Risk Homeowner's Policy: During a 4- or 5-week holiday season, the Sokoloskis burned scented candles in their home, which caused a discharge of smoke and soot, damaging their home and belongings. Their insurer denied coverage under a pollution exclusion because smoke and soot were defined as pollutants in the policy. The District Court held that coverage was barred under the exclusion and that the damages were not sudden and accidental. The Supreme Court affirmed on both issues. The very use of the words "sudden" and "accidental" reveals a clear intent to state two separate requirements, so that "sudden" means more than "unexpected". "Sudden", even if it includes the concept of unexpectedness, also encompasses a temporal element because unexpectedness is already expressed by the word "accidental". Having determined that the damage was not sudden, the Supreme Court did not address the additional requirement of being accidental. Under the clear language of the policy definitions and exclusion clause, coverage was properly barred and summary judgment proper. Sokoloski v. Am. W. Ins. Co., 1999 MT 93, 294 M 210, 980 P2d 1043, 56 St. Rep. 392 (1999), citing N. Ins. Co. of N.Y. v. Aardvark Assoc., Inc., 942 F2d 189 (3rd Cir. 1991), and followed in Travelers Cas. & Sur. Co. v. Ribi Immunochem Research, Inc., 2005 MT 50, 326 M 174, 108 P3d 469 (2005).

Liability Coverage of Newly Acquired Vehicle — Date of Delivery Determinative: Powell purchased a truck from his brother and sister-in-law, making monthly payments to his brother. During the time that Powell made payments, the truck remained in the possession of Powell's brother, who continued to use the truck as in the past. In January, Powell's brother executed a title in Powell's name, but the intent of both parties was that the truck would be owned by Powell after the payments were completed. When all of the payments were completed, Powell's brother executed a bill of sale and canceled his insurance policy on the truck. Several days later, Powell struck and killed a pedestrian with the truck. The pedestrian's insurance company claimed that title to the truck passed more than 30 days prior to the accident and that because Powell had failed to give notice to the company of his new ownership of the truck, the truck was not a "newly acquired car" within the meaning of the insurance policy. The Supreme Court held that "delivery" of the truck, as contemplated by the insurance policy, would be construed in the ordinary sense of the word to mean the passage of physical possession of the truck. Because that occurred on July 10, when the payments were completed and the bill of sale signed, the period for notification of a newly acquired car had not yet expired and the policy was therefore construed to apply to the truck. St. Farm Fire & Cas. Co. v. Powell, 274 M 92, 906 P2d 198, 52 St. Rep. 1138 (1995).

Meaning of Provision for Bonus if "Competition" Is Beaten: A contract between television station and a news editor/reporter that provided for a bonus if the station led its competitors meant that the station had to lead both competitors in the city. No bonus was due when the station led one but not the other. Berry v. KRTV Communications, Inc., 262 M 415, 865 P2d 1104, 50 St. Rep. 1617 (1993).

"Deposit" — Spending of Earnest Money Not Material Breach: In a contract for sale of real estate, use of words such as "deposit", "depositing", and "held on deposit" prohibited the sellers from spending the earnest money paid by the buyer pending the closing of the sale; however, the sellers' failure to keep earnest money on deposit until the closing did not constitute a material breach of contract. The buyer was entitled to seek contract damages but not rescission. Cady v. Burton, 257 M 529, 851 P2d 1047, 50 St. Rep. 395 (1993).

Improper Modification of Maintenance Awarded "For Life": The District Court modified a property settlement agreement, which provided that the wife receive $300 a month "as maintenance for life" in lieu of property for which she was to receive income, after husband unilaterally discontinued maintenance when wife began receiving social security payments. The maintenance agreement was a plain and unambiguous contract between the parties that was not subject to later interpretation or construction by a court. The agreement was drawn up by husband, a practicing attorney, who clearly understood the meaning of the term "for life". The District Court erred in modifying the agreement, absent a showing of substantial credible evidence that modification was warranted, without considering all necessary information in the original settlement agreement. In re Marriage of McKeon, 252 M 15, 826 P2d 537, 49 St. Rep. 127 (1992), followed in In re Marriage of Woodford, 254 M 501, 839 P2d 574, 49 St. Rep. 887 (1992).

Subjective Standard Applicable to Term "Satisfactory": A real estate listing contract contained the following clause, typed in by the realtor: "This listing is subject to Fultz being able to satisfactory [sic] trade the above lands for lands in Big Horn Co. on a tax free exchange." The realtor argued that an objective standard for a satisfactory trade should be used. The District Court found that because the realtor drafted the contract, any ambiguities should be construed against him. The term "satisfactory" was found to be a subjective standard rather than a reasonable man standard. Because the trade arrangement set up by the realtor did not meet the requirement of a tax-free exchange, the arrangement was properly found to be unsatisfactory under the contract terms. Watson v. Fultz, 239 M 364, 782 P2d 361, 46 St. Rep. 1751 (1989).

Covenant — "For Residence Purposes Only" Defined: A home owners' association brought suit to have a garage declared in violation of the subdivision's restrictive covenants. The Supreme Court ruled that a private garage is a proper appurtenance necessary to the enjoyment of a dwelling. However, if the garage is not appurtenant to a home, then it does violate the restrictive covenant. Hillcrest Homeowners Ass'n v. Wiley, 239 M 54, 778 P2d 421, 46 St. Rep. 1507 (1989), followed in Tipton v. Bennett, 281 M 379, 934 P2d 203, 54 St. Rep. 229 (1997), and Micklon v. Dudley, 2007 MT 265, 339 M 373, 170 P3d 960 (2007).

"Sale": A transfer of property in exchange for a valuable consideration constitutes a "sale". A sale occurred when a bank gave valuable consideration to a contractor by releasing him from his construction loan debt and the costs and expenses of foreclosure in exchange for title to the property. Schultz v. Stevens, 233 M 42, 758 P2d 287, 45 St. Rep. 1277 (1988).

Restrictive Covenant Allowing Disapproval of House Plans Based on "Harmony of External Design" — Specific Objective Standards Required: A restrictive covenant that allowed a design review committee to disapprove house plans and prevent construction based on "harmony of external design" was held to be too vague to be enforceable absent some general plan or scheme defining the standard of approval or an objective standard of design. Town & Country Estates Ass'n v. Slater, 227 M 489, 740 P2d 668, 44 St. Rep. 1257 (1987), contrasted in Jarrett v. Valley Park, Inc., 277 M 333, 922 P2d 485, 53 St. Rep. 671 (1996).

Responsibility for Accounts Payable Following Default in Sales Contract: Eight months after buyer and sellers entered into a contract for the sale of sellers' business, buyer defaulted and, pursuant to the contract, sellers reassumed possession of the business. The parties agreed that the assets of the business reassumed by the sellers included the accounts receivable, but they disagreed on who was responsible for the accounts payable. The District Court ruled that the sellers assumed the accounts payable, agreeing with the buyer's theory that accounts receivable and accounts payable were analytically indivisible in a determination of which party had assumed the accounts of the business. The Supreme Court affirmed. Heine v. Seibert, 217 M 224, 703 P2d 865, 42 St. Rep. 1152 (1985).

Ambiguous Phrase — Entire Contract to Determine Intent: A coal contract was entered on March 31, 1974. In 1976, the Montana Department of State Lands (functions now transferred to Department of Environmental Quality) determined that Decker was precluded under Title 82, ch. 4, part 2, from disturbing a certain portion of land within the mine area contemplated by the contract. It was conceded this would increase mining costs. The contract contained a price adjustment provision that allowed for price adjustments due to new government regulation. Decker contended the nondisturbance determination was a "new regulation" even though the statute under which the Department acted was enacted in 1973. The court in construing "new regulation" looked to the entire contract to determine mutual intent. The court determined, in light of adjustment provisions for all other cost increases, that "new regulation" meant increases required by government action taken after the effective date of the contract. Austin v. Decker Coal Co., 701 F2d 420 (5th Cir. 1983).

"Majority of Owners of Lots": Where the phrase "a majority of the then owners of the lots affected thereby" is not used in a technical sense, has no special meaning in its common usage, and is not ambiguous, the term means a majority of the owners, not the owners of a majority of the lots. Cieri v. Gorton, 179 M 167, 587 P2d 14 (1978).

"Denies Coverage" — Interpretation: Plaintiff settled with tortfeasor's insurance company for injuries sustained in an auto accident but the company became insolvent before making payment. Plaintiff's own company was not liable under its "uninsured automobile" clause because there was no affirmative act by the insolvent insurer whereby it "denied coverage". Application of the Montana Insurance Guaranty Association Act protects plaintiff as effectively as a strained judicial construction of the uninsured motorist policy terms. Murray v. Mont. Ins. Guar. Ass'n, 175 M 220, 573 P2d 196 (1977).

Water Rights: Where buyer and seller of real property discuss "water rights" in general terms, the term "water rights" in a contractual agreement will be used in its ordinary and popular sense, not in its statutory and technical sense. Moore v. Swanson, 171 M 160, 556 P2d 1249 (1976).

Strict Construction of Restrictive Covenants: Where the language of a restrictive covenant is plain, direct, and certain and admits of but one meaning, it is the duty of the court to declare what the terms of the covenant contain and not to insert a limitation. Higdem v. Whitham, 167 M 201, 536 P2d 1185 (1975), followed in Jarrett v. Valley Park, Inc., 277 M 333, 922 P2d 485, 53 St.

Rep. 671 (1996). See also Windemere Homeowners Ass'n, Inc. v. McCue, 1999 MT 292, 297 M 77, 990 P2d 769, 56 St. Rep. 1173 (1999), in which the universal language of an original declaration of restrictive covenants was found to be broad enough to authorize subsequent amendment, by a supermajority of affected property owners, authorizing creation of new or unexpected restrictions not contained or contemplated in the original covenants.

"Final and Conclusive": Contract stating that the architect/engineer's estimates and decisions shall be "final and conclusive" was properly interpreted by the court to mean that the engineer's certificate of completion was binding upon the parties, absent any proof of fraud or mistake on the part of the engineer. United Pac. Ins. Co. v. County of Flathead, 499 F2d 1235 (9th Cir. 1974).

"Trailer": "Trailer" as used in restrictive covenant against their use was construed to refer to a type of structure and not the mobility of that structure. Timmerman v. Gabriel, 155 M 294, 470 P2d 528 (1970).

Intended Meaning: The words employed in a written agreement, if capable of more than one meaning, are to be given that meaning which it is apparent the parties intended them to have. Kintner v. Harr, 146 M 461, 408 P2d 487 (1965).

Insurance Contract: The words of an insurance contract are to be understood in their usual meaning. Kansas City Fire & Marine Ins. Co. v. Clark, 217 F. Supp. 231 (D.C. Mont. 1963), affirmed in 329 F2d 647 (9th Cir. 1964).

"Actual Cash Value": Where dealer's trucks were insured for "actual cash value" it was not error to allow insured to recover the retail market value of the destroyed property rather than the wholesale market value. Johnson v. Equitable Fire & Marine Ins. Co., 142 M 128, 381 P2d 778 (1963).

"Finance Plan": In an action to recover the purchase price of merchandise (sewing machines) claimed to have been sold to defendants but alleged by them to have been delivered on consignment, plaintiff introduced in evidence a printed order for the goods obtained by its agent, which under the subject "Terms" contained the words "Finance Plan". Defendants, contending that the contract did not contain all the terms agreed upon and that the words "Finance Plan" rendered the contract ambiguous, were properly permitted to introduce parol evidence to explain the term as the meaning of the term was not so free from doubt that it might be said, as a matter of law, that it furnished its own interpretation. New Home Sewing Mach. Co. v. Songer, 91 M 127, 7 P2d 238 (1931), explained in Brown v. Homestake Exploration Co., 98 M 305, 39 P2d 168 (1934).

"Commence Drilling Operations": In an action to have an oil and gas lease forfeited for failure of the lessee to "commence drilling operations for oil" within the time specified in the lease, the quoted phrase meant the commencement of actual drilling and not the commencement of preliminary work necessary to such drilling; evidence that the well was not "spudded in" being sufficient to make out a prima facie case, the granting of a nonsuit was error. Solberg v. Sunburst Oil & Gas Co., 73 M 94, 235 P 761 (1925).

"Spudding In": The terms "spudding in" of an oil well, as understood by oil operators, and "commence drilling operations", used in an oil lease, denote the first movement of the drill in penetrating the ground. Solberg v. Sunburst Oil & Gas Co., 73 M 94, 235 P 761 (1925).

"Vacation": Under a partnership providing for a 6 weeks' vacation for each member of the firm without deduction from the income, "vacation" meant absence from any cause and therefore included absence on account of sickness. Kettlekamp v. Watkins, 70 M 391, 225 P 1003 (1924).

Operation and Effect: Where there are no technical words in a contract, the words must be given their ordinary and popular meaning. Frank v. Butte & Boulder Min. & Lumber Co., 48 M 83, 135 P 904 (1913).

"Out of the First Earnings of Its Business, After Deducting Running Expenses": A written contract that a loan to a corporation shall be repaid monthly "out of the first earnings of its business, after deducting running expenses" does not create a general liability on the part of the company, to be paid after a reasonable time, but makes the indebtedness payable out of a special fund, consisting of the net proceeds, as rapidly as they accumulate. Frank v. Butte & Boulder Min. & Lumber Co., 48 M 83, 135 P 904 (1913), distinguished in Howard v. Hancock Oil Co., 68 F2d 694 (9th Cir. 1934).

Bankable Note: The words employed in a contract shall be given definite meaning. A bankable note is one receivable as cash by a bank, and a note that banks will not buy is not bankable, regardless of the bank's reasons for refusing to buy, or the high character of the paper. Pasha v. Bohart, 45 M 76, 122 P 284 (1912).

"Firm": The word "firm" was used in the will of a testator as an equivalent for "Gans & Klein", and had no technical reference to the copartnership of Gans & Klein. In re Klein's Estate, 35 M 185, 88 P 798 (1907).

"Connected": Where in an action to recover the amount of an insurance policy it appeared that the assured had represented in his application for the policy that he was not in any way connected with the manufacture or sale of spirituous liquors, the word "connected" must be presumed to have been used in its popular sense, involving the idea of permanency. Collins v. Metro. Life Ins. Co., 32 M 329, 80 P 609 (1905).

28-3-502. Interpretation of technical words.

Case Notes

Default: Against contention that failure to procure consent constituted a breach as opposed to a default, the failure was determined to be a default of the contract for deed. Dobitz v. Oakland, 172 M 126, 561 P2d 441 (1977).

Judicial Notice: A court cannot take judicial notice of the meaning of technical words; such words are to be interpreted as usually understood by persons in the profession or business to which they relate, unless used in a clearly different sense than the technical one. Lehrkind v. McDonnell, 51 M 343, 153 P 1012 (1915).

Mining Lease: Witnesses who are qualified may testify as to the meaning of the following words in a mining lease: "There shall be no ores stoped, except at the three hundred foot level, and all ores shall be extracted from the drifts, raises, or winzes." Chambers v. Lowry, 21 M 478, 54 P 816 (1898).

28-3-503. Inconsistent words to be rejected.

Case Notes

Contradictory Provisions: In suit by contractor for additional expenses incurred in obtaining suitable gravel to perform road construction contract, contradiction whereby State Highway Commission (now Transportation Commission) on one hand warranted condition of gravel pit but on other hand disclaimed any liability from reliance on such representations, would be resolved in favor of contractor for reason that contractor was in "take it or leave it" situation and justifiably relied upon Commission's warranty. Haggart Constr. Co. v. St. Highway Comm'n, 149 M 422, 427 P2d 686 (1967).

Meaningless Words: Under this section where a word appears in a contract which is meaningless in the connection in which it is employed, it must be disregarded in the interpretation of the writing. Davis v. Park Sec. Corp., 117 M 393, 159 P2d 323 (1945); Norwegian Lutheran Church of Am. v. Armstrong, 112 M 528, 118 P2d 380 (1941); Shelley v. Normile, 109 M 117, 94 P2d 206 (1939); Kasun v. Todevich, 71 M 315, 229 P 714 (1924).

Part 6
Time of Performance

Part Case Notes

Failure of Insurer to Pay Within Sixty-Day Period Specified in Insurance Contract — No Error in Interpretation of Contract: An insurance contract required the insurer to pay for a loss within 60 days after the insurer received proof of loss and: (1) the parties reached an agreement; (2) there was a final judgment; or (3) the insured filed an appraisal with the insurer. The insured sought money damages because the claim was not paid within the 60-day period following the joint appraisal, which resulted in plaintiffs' alleged mental anguish and emotional distress. However, given a lengthy dispute over the amount of damages, the significant disparity between estimates, and plaintiffs' rejection of the joint appraisal, the District Court found that the agreement contemplated by the contract that would trigger the 60-day payment period was never reached. Plaintiffs appealed on grounds that the District Court misinterpreted the contract. The Supreme Court affirmed. The rejected joint appraisal did not constitute an agreement. Because the contractual requirements for the 60-day payment period were not met, the District Court did not err when it declined to conclude that the insurer should have made payment within 60 days of the joint appraisal. Nelson v. Farmers Union Mut. Ins. Co., 2003 MT 101, 315 M 268, 68 P3d 689 (2003).

Exceptions to Requirement for Matching Terms in Offer Made Under Right of First Refusal: A right of first refusal does not give the rightholder the power to compel an unwilling owner to sell, but merely requires the owner, when and if a decision is made to sell, to offer the property first to the rightholder at the stipulated price. The preemptive right ripens into an option when the owner elects to sell, at which point the owner has the contractual obligation to offer the property to the optionee on the same terms and conditions as the offer made to the owner by a third party. (See 77 Am. Jur. 2d Vendor Purchaser § 40 (1997).) In order that each party to the contract receives the benefit bargained for, under Miller v. LeSea Broadcasting, Inc., 87 F3d 224 (7th Cir. 1996), three exceptions to the requirement for the exact matching of terms have been recognized: (1) the grantor of the option can waive exact matching; (2) proper names need not be matched; and (3) the grantor of the option may not act in bad faith, including procuring from the third party terms that the grantor knows are unacceptable to the optionee for the purpose of discouraging exercise of the right of first refusal. As long as the conditions of the sale are commercially reasonable, imposed in good faith, and not specifically designed to defeat the right of first refusal, the optionee is obliged to match the offer if the right is to be exercised. Here, although attorneys for the parties engaged in discussions concerning whether poison pill provisions included in an offer were an attempt to dissuade exercise of the right of first refusal, the discussions were not found to impact the effective exercise of the right, so the District Court's conclusion that the right had been properly exercised was not in error. Kennedy v. Dawson, 1999 MT 265, 296 M 430, 989 P2d 390, 56 St. Rep. 1078 (1999). See also Story v. Bozeman, 242 M 436, 791 P2d 767, 47 St. Rep. 850 (1990), and Lee v. Shaw, 251 M 118, 822 P2d 1061 (1992).

Involuntary Satisfaction of Judgment — Request for Stay of Execution Not Required: Following entry and satisfaction of judgment in District Court, the parties were aware of a contemplated appeal, but no stay of execution was requested or supersedeas bond posted. After plaintiff acquired title to the disputed property pursuant to the judgment, defendant filed a notice of appeal and lis pendens, effectively preserving the status quo pending appeal. Plaintiff moved to dismiss, contending that by voluntarily satisfying the judgment, defendants waived their right to appeal. Applying Turner v. Mtn. Eng'r & Constr., Inc., 276 M 55, 915 P2d 799, 53 St. Rep. 23 (1996), the Supreme Court held that the parties' course of conduct illustrated the involuntary, rather than voluntary nature of the satisfaction of judgment. Because satisfaction was involuntary, the right to appeal was not waived. Further, under former Rule 7, M.R.App.P. (now superseded), a party could request a stay of execution, but the request was not mandatory, even though a party choosing not to seek a stay ran the risk of having the appeal become moot. Plaintiff's motion to dismiss was denied. Kennedy v. Dawson, 1999 MT 265, 296 M 430, 989 P2d 390, 56 St. Rep. 1078 (1999).

Conduct Constituting Waiver of Right of First Refusal to Purchase Property: After a determination by the Supreme Court in Lee v. Shaw, 251 M 118, 822 P2d 1061 (1992), that the Lees' lease-management agreement contained a valid right of first refusal to purchase ranch property, notification of intent to sell was given and extensive sale negotiations were begun to finalize purchase of the ranch. Although none of the various proposed contracts was signed by all of the parties, an agreement was reached to complete the sale on a specified closing date, thus triggering the running of the preemptive right to purchase, which was set by the agreement at 45 days. However, the Lees failed to show up for the closing, despite an extension of the closing date. The District Court properly determined that the Lees' actions constituted an intentional relinquishment of their right of first refusal and thus a waiver of that right. In re Estate of Pelzman, 261 M 461, 863 P2d 1019, 50 St. Rep. 1408 (1993).

Contract Construed as Right of First Refusal and Not Option Contract — Ambiguity Resolved Against Lessee Drafters of Agreement: Lessor signed two documents giving the lessees certain rights in lessor's 800-acre ranch. The first document, granting a "first option" to purchase, required other offers to be in writing and gave the lessees 45 days from the day of notification of intent to sell to make payment. The Supreme Court held that this document created a right of first refusal. The second document granted a "first option to purchase [my] property . . . upon or before my passing . . ." and also granted 45 days for payment "[u]pon notification of intent to sell". The Supreme Court found that while some of the language in the second document was consistent with a true option, the insertion of the last sentence granting 45 days for payment upon notification of intent to sell indicated a right of first refusal. Because the lessees had drafted the second document, the Supreme Court construed the ambiguity against the lessees and held that the document created a right of first refusal and not an option contract. Because notice of intent to sell had never been given by lessor's estate, the right of first refusal did not come into effect. Lee v. Shaw, 251 M 118, 822 P2d 1061, 48 St. Rep. 1110 (1991). See also a subsequent appeal addressing waiver of the right of first refusal in In re Estate of Pelzman, 261 M 461, 863 P2d 1019, 50 St. Rep. 1408 (1993).

Specified Time of Performance — Nonperformance of Condition Precedent: Contract farmer and landowner orally agreed that farmer would seed landowner's land between August 25 and

September 20, with the condition that landowner would help farmer with the downpayment on drills needed for seeding. The help with the downpayment was a condition precedent that had to be performed by landowner before farmer was bound to the time frame in the contract. When landowner did not help with the downpayment, farmer was relieved of his obligation to meet the contract performance dates and the contract was to be performed within a reasonable time. Weyler v. Kaufman, 196 M 132, 638 P2d 393, 38 St. Rep. 2197 (1981).

Interpretation of Contract — Time of Performance: On appeal, the seller of a log cabin urged that the agreement required the buyer to remove the logs from the seller's property as soon as possible. The Supreme Court found that the negotiations were quick and informal and that nothing specific was said about the time in which the cabin was to be removed. Noting the seller's testimony that he was in the process of refurbishing his motel and wanted the cabin removed as soon as possible so that he could take advantage of the good building weather to expand the motel and that the cabin was old and had not been used for years and contributed nothing to the value or appearance of the property and little value to the motel, the Supreme Court held that there was substantial evidence to support the trial court's finding that a condition of the sale was that the logs were to be removed as soon as possible. Jeffery v. Neville, 190 M 300, 620 P2d 1218, 37 St. Rep. 1983 (1980).

28-3-601. Time of performance when not specified.

Case Notes

Reasonableness Considered on Case-by-Case Basis — Forty-Five Days to Finalize Settlement Agreement Not Unreasonable: Plaintiff moved to enforce the terms of a settlement agreement, and defendant subsequently satisfied its settlement obligation to pay plaintiff $80,000. Plaintiff then sought interest for the 45 days that elapsed between the date of the settlement agreement and the time the settlement obligation was actually paid. The District Court denied the request for interest, and plaintiff appealed. The question of whether a given length of time is reasonable can either be one of fact or of law, depending on the surrounding circumstances. Reasonableness does not lend itself to a precise bright line definition but hinges on the underlying factual circumstances, which vary from case to case. The question of whether a party has performed its obligations under a settlement agreement must be assessed on a case-by-case basis, taking into account the matters that need to be accomplished before a settlement can be finalized. In this case, defendant's obligation consisted of more than just the payment of money. The settlement agreement also required defendant to prepare a mutually agreeable release of claims form and to submit a stipulation for dismissal of the case, so immediate performance was neither feasible nor required. The Supreme Court recommended that a date of performance be negotiated as part of a settlement agreement to avoid the prospect and cost of a court making the decision. However, under the circumstances of this case, 45 days to finalize the settlement was considered reasonable, and the District Court's denial of interest during that time was affirmed. Dambrowski v. Champion Int'l Corp., 2003 MT 233, 317 M 218, 76 P3d 1080 (2003).

Decree of Specific Performance — Enforcement of Purchase Option in Lease Agreement — Remand for Establishment of Performance Schedule: McDonald constructed a restaurant on leased real property in Bozeman. The lease included a provision allowing McDonald a limited option to purchase the property. The property was appraised pursuant to the lease conditions, and McDonald indicated that he was prepared to purchase the property at the appraised price. The lessors refused to complete the transaction, resulting in an action by McDonald to enforce the agreement. The District Court found that the option provision contained all material terms and was legally enforceable and that the requirements of the option had been met, so specific performance was awarded to McDonald. The lessors appealed. The remedy of specific performance is allowed under 27-1-411, and contracts for the sale of real property are specifically enforceable under 27-1-419 because it is presumed that the breach of an agreement to transfer real property cannot be adequately relieved by pecuniary compensation. The lessors contended that the option clause was ambiguous and represented only "an agreement to agree" and that a further contract between the parties was necessary if the option was to be enforced. The Supreme Court noted that the option clause set forth the time in which the option was exercisable, the method for calculating the purchase price and interest rate, the method by which the purchase price would be paid, and the parties' rights in case of default. Thus, the option contained all the material terms to make the acts necessary to purchase the property clearly ascertainable and was not ambiguous. The lessors nevertheless complained that the option provision did not state who was responsible for paying taxes or provide fully for forfeiture remedies. However, under Keaster v. Bozik, 191 M 293, 623 P2d 1376 (1981), absolute certainty in every detail is not a prerequisite for specific performance and collateral matters, such as responsibility for taxes and insurance, need not be expressed in the contract. The District Court's finding that the purchase option was enforceable was therefore affirmed, but the Supreme Court remanded to allow the District Court to set up a schedule for performance of the obligations and the commencement of interest, as required in Keaster. McDonald v. Cosman, 2000 MT 126, 299 M 499, 6 P3d 956, 57 St. Rep. 522 (2000), distinguishing Henkel v. Hewitt Agency, Inc., 206 M 303, 671 P2d 582 (1983), and Quirin v. Weinberg, 252 M 386, 830 P2d 537 (1992).

Nine Years Unreasonable Time to Hold Property — Specific Performance Appropriate: When dissolving a business relationship, the parties agreed by contract that property would be transferred in consideration for cash payments, but the contract did not provide a specific time for transfer or make the property subject to a security interest in case of default. The time to transfer the property was at the time the contract was executed, and as a matter of law, 9 years was an unreasonable length of time to hold the property. Under the circumstances, specific performance of the contract was appropriate as a remedy in equity. First Sec. Bank of Anaconda v. Vander Pas, 250 M 148, 818 P2d 384, 48 St. Rep. 900 (1991).

"Reasonable Time" Defined — Question of Law: "Reasonable time" is defined to be so much time as is necessary, under the circumstances, to do conveniently what the contract or duty requires should be done in a particular case. When the facts are clearly established or are admitted or undisputed, the question of what is a reasonable time is one of law; however, when surrounding circumstances are in dispute, the question is at least partially one of fact and requires resolution by the trier of fact. Walters v. Getter, 232 M 196, 755 P2d 574, 45 St. Rep. 986 (1988), citing Dunjo Land Co. v. Hested Stores Co. of Wyo., 163 M 87, 515 P2d 961 (1973), and Henderson v. Daniels, 62 M 363, 205 P 964 (1922).

Certainty of Option Contract — Specific Performance of Reformed Contract: Where the plaintiff and defendant entered into an option contract giving the plaintiff an option to purchase certain real estate but the parties failed to specify the interest which would be retained by the defendant in certain improvements and failed to specify the dates upon which the downpayment and annual payments would be made and the date upon which interest would accrue, the contract was nonetheless sufficiently definite to allow its enforcement by specific performance. At trial, the court took testimony of the parties and reformed the contract so as to make it sufficiently definite as to the defendant's retained interest to allow specific performance. The fact that certain dates were not specified is not fatal to the contract, as it need not be absolutely certain in every detail, and where a time of performance is not specified, a reasonable time will be implied. Keaster v. Bozik, 191 M 293, 623 P2d 1376, 38 St. Rep. 194 (1981).

Time Fixed for Convenience of Parties: The general rule is that a bill payable on condition does not mature until the performance of the condition. When the time fixed, however, is for the convenience of the parties and the future event does not happen as contemplated, the law implies a promise to pay in a reasonable time. Kinjerski v. Lamey, 185 M 111, 604 P2d 782 (1979).

Crop-Share Agreement: Where contract provided that farm laborer would be paid $150 per month cash, would get 10% of the harvested crops after harvest, and would be expected to stay for a 12-month period, he was entitled to his share of the crop due on his crop-share agreement when wheat and barley were placed in storage at elevator although safflower, in which laborer did not share, had not been cut. Failure of employer to pay laborer's share on demand constituted a breach of contract and it was not necessary for laborer to complete the 12-month term in order to recover his percentage of the crops. Laughnan v. Sorenson, 139 M 531, 366 P2d 433 (1961).

Reasonable Time:

That no definite time was stipulated for performance by the purchaser of the payment of money is immaterial, for our law implies an agreement here to perform within a reasonable time. Bennett v. Dodgson, 129 M 228, 284 P2d 990 (1955).

Where under contract for sale of real estate deed was placed in escrow to be delivered to purchaser upon making certain payments, but no time limit was provided for in the contract, the reasonable time for compliance with the contract would not extend beyond the date the purchaser was to have "possession of the premises on expiration of present lease" which was 7 months thereafter. Hart v. Barron, 122 M 350, 204 P2d 797 (1949).

Where under an executed oral agreement the terms of an oil and gas lease were modified to the extent of granting an indefinite extension of time of payment of delay rentals by the lessee, the latter had a reasonable time within which to make payment. Griffith v. Cedar Creek Oil & Gas Co., 91 M 553, 8 P2d 1071 (1932).

Where no time is specified for the performance of an act required to be done by a contract a reasonable time therefor is allowed under this section. Orem v. Hansen Packing Co., 91 M 222, 7 P2d 546 (1932).

Time of Payment — Reasonable Time or Upon Demand: Where time of payment is not specified in contract the law implies that payment will be made within a reasonable time or upon demand. Johnson v. Elliot, 123 M 597, 218 P2d 703 (1950). However, when demand is made, the other party still must be given reasonable time after demand in which to perform. Walters v. Getter, 232 M 196, 755 P2d 574, 45 St. Rep. 986 (1988).

Reasonable Time Implied — Ranch Lease — Completion of Fencing by Tenant: Where a ranch lease requiring the tenant to rebuild fences and clear brush lands fixed no time for completion of fencing or clearing of brush, a reasonable time therefor was implied. Morris v. Hall, 122 M 418, 205 P2d 800 (1949).

Complaint — Allegation as to Time of Payment:

Where in an action against an estate to recover on a rejected claim based on the oral agreement of decedent to pay half the expense incident to repairs of residence property owned by him and plaintiff, his sister, jointly, the complaint did not allege when payment should be made, but it was pleaded therein that a verified claim had been presented to the administratrix, which allegation was admitted, the complaint was sufficient under this section to show that the amount due was ascertained and that it was due and payable when the complaint was filed. Binzel v. Viehmann, 111 M 6, 106 P2d 187 (1940).

In order to state a cause of action for the breach of a contract calling for payment within a reasonable time, the complaint must allege a time of performance so that it may appear what relation time bore to the alleged breach of duty and that the cause of action had accrued before the commencement of suit. Evankovich v. Howard Pierce, Inc., 91 M 344, 8 P2d 653 (1932).

Where a contract is wholly silent as to the time of performance and contains no statement from which any particular time may be inferred, a complaint based thereon was insufficient unless it alleged that the contract was to be performed within a reasonable time; however a promise to perform (make payment) when convenient is construed as a promise to do so within a reasonable time. Evankovich v. Howard Pierce, Inc., 91 M 344, 8 P2d 653 (1932), distinguished in Bennett v. Dodgson, 129 M 228, 284 P2d 990 (1955).

Alternative or Unstated Conditions: Where the place of performance of a contract is in the alternative, ordinarily the promisor may elect what act he will perform, the obligation being discharged by the performance of either of the enumerated acts, and if one contracts to do one of two things by a given date and allows the day to elapse without performing either, his right of election is lost. If a given date is not stated, the expiration of a reasonable time has the same effect. Thomas v. Cloyd, 110 M 343, 100 P2d 938 (1940).

Sale of Personalty — Time of Delivery as Time of Payment: Where one buys personal property at a stipulated price and no time of payment is agreed upon, the law fixes the time of delivery as the time of payment, and the rule declared by this section that if no time is specified for the performance of an act, a reasonable time for performance is allowed, has no application. Burden v. Elling St. Bank, 76 M 24, 245 P 958 (1926).

Mining Claim Development:

Where purchasers of an interest in mining property agreed to develop the property and proceeded to do so at once and continued doing so until an action was commenced by the owner to cancel the contract upon the ground, among others, that it did not provide a specified time within which operations should be begun and prosecuted to completion, plaintiff was not in a position to complain on the latter ground. Lee v. Lee Gold Min. Co., 71 M 592, 230 P 1091 (1924).

Failure of a contract for the development of mining claims to provide a specified time within which defendants should begin operations and prosecute the work of development to completion is alone insufficient to void the contract since under this section they were allowed a reasonable time within which to do the acts required. Lee v. Lee Gold Min. Co., 71 M 592, 230 P 1091 (1924).

28-3-602. When time considered of the essence.

Case Notes

Modification of Nonexistent Contract Impossible — Minutes of Preconstruction Meeting Inadmissible Extrinsic Evidence Absent Ambiguity in Subsequent Contract: Keeney Construction (Keeney) subcontracted to perform certain construction work for James Talcott Construction Co., Inc. (Talcott). The subcontract stated that time was of the essence, but contained no specific date of completion, Rather, Keeney was to complete the work as directed by Talcott and on Talcott's completion schedule. Keeney asserted that the parties intended a 1996 completion date, but the project was not finished until 1997. Keeney sued for damages for delay and extra work, contending that extrinsic evidence in the form of minutes from a preconstruction meeting, held 2 days before the contract was finalized, would verify the parties' intent and represented an executed oral agreement that modified the written contract. The Supreme Court found no ambiguity in the written contract to warrant further examination of the intent of the parties. Because the intent of the contract was clear, the extrinsic evidence was inadmissible to support the contention that a specific completion date was intended. Keeney could not assert a claim for damages based on Talcott's direction of the timing of the completion of the project when the contract authorized Talcott to do so. Further, because an oral agreement cannot modify a contract that does not yet exist, the meeting and conversations held prior to the contract signing could not be interpreted as a modification of the subsequent written contract. Keeney Constr. v. James Talcott Constr. Co., Inc., 2002 MT 69, 309 M 226, 45 P3d 19 (2002).

Contract Part Oral, Part Written — Bid Not Contract — Parol Evidence Rule Inapplicable — Time of Essence by Oral Agreement: The plaintiff in a breach of contract case obtained a bid on a job building a basement. The defendant contractors on appeal argued: (1) that their bid constituted a contract and therefore the parol evidence rule barred testimony concerning a completion date not contained in the writing; and (2) time was not of the essence unless expressly provided in the writing. The Supreme Court said that the bid was an offer and that a purported acceptance which varied or added to the terms of the offer was not an acceptance but a counteroffer. The trial court's finding that the parties had agreed orally to a specific completion date was not clearly erroneous. The contract was partially written and partially oral. Because there was not a final, complete written document intended by the parties to contain all of the terms of the contract, the parol evidence rule did not apply. By agreeing to the completion date with the knowledge that the plaintiff considered the date essential because of approaching cold weather, the defendants agreed that time was of the essence. Therefore, the defendants were in substantial breach on the agreed date. Carriger v. Ballenger, 192 M 479, 628 P2d 1106, 38 St. Rep. 864 (1981), distinguishing Higby v. Hooper, 124 M 331, 221 P2d 1043 (1950).

Time of the Essence in Oil and Gas Leases: Oil and gas leases are construed liberally in favor of the lessor, and time is of the essence even though the contract does not so provide. Thus, failure of lessee to timely pay a draft executed at the same time as the lease was sufficient justification for cancellation of the lease. Clawson v. Berklund, 188 M 48, 610 P2d 1168 (1980).

Parol Evidence — Delivery Date Under Contract for Sale: Where the correspondence which constituted the memoranda of agreement in a contract for the sale did not specifically provide that time was of the essence, it was error to admit evidence regarding discussions of the delivery date. Martel Constr., Inc. v. Gleason Equip., Inc., 166 M 479, 534 P2d 883 (1975).

Meaning of "Time Is of the Essence" — Reasonable Time: Where a contract provided that "time is of the essence" in the performance of its terms, and a specific time is not set for performance, a reasonable time is implied. Maxted v. Stenberg, 166 M 460, 534 P2d 864 (1975).

Omission of Statement: Where a lease with option to purchase does not state that time is of the essence, failure of the optionee to perform the covenants strictly at the time they may or should be performed will not cause him to lose his right to specific performance of the option. Cont. Oil Co. v. McNair Realty Co., 137 M 410, 353 P2d 100 (1960).

When Time Is of the Essence:

Where escrow agreement in connection with sale of land required $700 to be paid by a certain date for delivery of the deed, provision in such agreement that "time is and shall be in so far as the Escrow Agent is concerned of the essence of this agreement" did not by its express terms make time the essence of the contract so far as the purchaser was concerned and did not require the $500 original payment to be forfeited. Herman v. Herman, 123 M 39, 207 P2d 1155 (1949).

An oil and gas lease is merely an option contract and time is of its essence even though a stipulation to that effect is absent from the writing, and failure of the lessee to act promptly renders his rights subject to termination at the election of the lessor. Thomas v. Standard Dev. Co., 70 M 156, 224 P 870 (1924).

Under this section, only one subject is open to discussion, and that is not what the parties may have intended to say but what they did say in their contract. It is true, of course, that no set form or arrangement of words is necessary but the contract must, upon its face, convey the meaning that time shall be of the essence. Curtis v. Parham, 49 M 140, 140 P 511 (1914).

Under a contract of sale by the terms of which failure to pay an installment of the purchase price ends the contract, time being expressly declared of the essence of it, notice that an installment has fallen due is not required and therefore a claim that plaintiff was guilty of laches because of delay in giving it had no merit. Fratt v. Daniels-Jones Co., 47 M 487, 133 P 700 (1913).

Where an oral contract was made to sell real property and suit was brought by the vendee for specific performance, the court could not say, according to the facts of the case, that time was of the essence of the agreement. Stevens v. Trafton, 36 M 520, 93 P 810 (1908).

What Sufficient to Meet Requirement of Statute — Life Insurance Policy: Under this section a provision in a life insurance policy that payment of a premium should not maintain the policy beyond the due date when the next premium is payable was tantamount to a declaration that time should be considered as of the essence of the contract and sufficient to meet the requirement of the statute, and failure to make prompt payment ipso facto voided the contract. Johnson v. Metro. Life Ins. Co., 107 M 133, 83 P2d 922 (1938).

Exception to Forfeiture Disfavor: While the general rule is that forfeitures are not favored, an exception is where time is made of the essence and default is provided for upon not meeting the time requirements. Huffine v. Lincoln, 87 M 267, 287 P 629 (1930).

Oral Evidence Not Admissible to Show Time to Be of Essence: Where a contract for the sale of sheep was silent as to time being of the essence of the contract it was error to permit oral evidence that such was nevertheless the intention of the parties. Curtis v. Parham, 49 M 140, 140 P 511 (1914).

Duty of Court When Time Is of Essence:

When the provision that time is of the essence of the contract is included in the contract, it is the duty of courts to carry out the intention of the parties by giving effect to that provision; for to ignore or circumvent it when deliberately written into a contract by the parties or by any sort of construction to nullify its effects is to make a new contract for the parties different from the one which they themselves constructed—something even a court of equity is not authorized to do. Fratt v. Daniels-Jones Co., 47 M 487, 133 P 700 (1913).

Courts will not undertake to make contracts for parties different from those which the parties themselves intended, but will enforce a provision making time of the essence of a contract, unless the party for whose benefit it was inserted has waived it or is estopped to insist upon its enforcement, or performance has been prevented by intervening circumstances sufficient to relieve the party from the performance of any other provision of the contract. Fratt v. Daniels-Jones Co., 47 M 487, 133 P 700 (1913).

Effect of Breach of Provision Relative to Time: Where a contract of sale provides that the vendor shall have the right to declare it at an end, upon failure by the vendor to make payment on a date fixed, time being expressly made of the essence of the contract, breach by the vendee does not ipso facto terminate the agreement, but an election is necessary on the part of the vendor requiring some sort of notice on his part to make the provision effective. Fratt v. Daniels-Jones Co., 47 M 487, 133 P 700 (1913).

Validity of Provision Making Time of Essence: Neither the provision making time of the essence of a contract of sale nor the contract containing such a provision is invalid as against positive law or public policy. Fratt v. Daniels-Jones Co., 47 M 487, 133 P 700 (1913).

Unenforceable Note: A note was given in consideration of payee's written promise to purchase or procure a purchaser for certain mining property before a certain stated date. Time was expressly declared to be of the essence. Where the property was not sold within the stated time, the note was unenforceable. Talbott v. Heinze, 25 M 4, 63 P 624 (1901).

28-3-603. Postponement of performance date which falls on holiday.

Case Notes

Section as Providing Grace Period Not Prohibition: Instead of embodying a prohibition, this section merely provides an extra day of grace. Any of the enumerated acts may be done lawfully on a holiday, but are in time if not done until the next business day. State ex rel. Hay v. Alderson, 49 M 387, 142 P 210 (1914).

Public Act Performed on Sunday: There is no prohibition against the performance of any public act on Sunday as such. State ex rel. Hay v. Alderson, 49 M 387, 142 P 210 (1914), distinguished in Miller v. Emerson, 120 M 380, 186 P2d 220 (1947).

Part 7
Provisions Implied by Law

Part Case Notes

Recoupment of Costs Provided for Defense of Claims Outside Insurance Policy Coverage: Plaintiff defended claims from third parties against defendant, but the claims were subsequently determined to be barred by exclusionary language in defendant's policy. Plaintiff sought to recoup the costs expended on defendant's behalf, and the District Court awarded plaintiff's costs.

On appeal, the Supreme Court affirmed the award. Plaintiff timely and explicitly reserved the right to recoup the defense costs by notifying defendant of plaintiff's reservation of rights prior to paying the costs and thus expressly reserved its right to recoup defense costs if a court determined that plaintiff had no duty to provide the costs. Defendant implicitly accepted plaintiff's reserved rights by posing no objection to the reservation. Travelers Cas. & Sur. Co. v. Ribi Immunochem Research, Inc., 2005 MT 50, 326 M 174, 108 P3d 469 (2005). See also Grinnell Mut. Reins. Co. v. Shierk, 996 F. Supp. 836 (S.D. Ill. 1998), United Nat'l Ins. Co. v. SST Fitness Corp., 309 F3d 914 (6th Cir. 2002), and Horace Mann Ins. Co. v. Hanke, 2013 MT 320, 372 Mont. 350, 312 P.3d 429.

Witness Testimony — Substantial Evidence to Support Implied Fee Agreement: The trial court's determination that an oral agreement was entered into between the parties but that no express agreement was reached as to the fee to be paid plaintiff for architectural services and that there was an implied agreement at law to pay the reasonable value of those services was supported by substantial evidence. Most of the evidence consisted of witness testimony, and where the credibility of the witness is of prime importance, the determination of weight given to the testimony is the primary function of the trial judge sitting without a jury. Knight & Co. v. Manaras, 184 M 448, 603 P2d 675 (1979).

28-3-701. Stipulations necessary for reasonableness or conformity to usage.

Case Notes

Written and Oral Real Property Agreements — No Timing of Valuation Provision: The parties were married in 1973. They entered a prenuptial agreement providing that the real and personal property of each would remain separate. In 1974, defendant brought a quiet title action against his sisters. He executed a handwritten agreement with plaintiff that if she would finance the legal expenses of the action he would give her 10% of the land or the value thereof. He was successful, and the parties entered into an oral agreement containing the same provisions for appellate costs. The trial court found that defendant owed plaintiff 20% of the value of the land and that the value was to be determined at the time he elected to pay and be based on 20% of the value of all the land. The Supreme Court held that the defendant, under the clear terms of the written contract, had the option to select the acreage which he wished to convey. The District Court disregarded this language in ordering him to convey the percentage of his land as a whole. Since no contract provision addressed the timing of the valuation of the land and conflicting evidence was presented, the District Court's determination that it be valued at the time of payment was upheld. Kartes v. Kartes, 195 M 383, 636 P2d 272, 38 St. Rep. 1941 (1981).

Sale of Real Estate: Corporation which sold apartments in condominium was properly enjoined from selling space for commercial purposes in the same building since even though restrictions requiring residential use were not included in the sales contract or deed to apartment buyers, equitable servitude could be implied as a reasonable part of the deed. Thisted v. Country Club Tower Corp., 146 M 87, 405 P2d 432 (1965).

Oil and Gas Lease — Marketing Product: The parties entered into an oil and gas lease under which plaintiffs were to receive royalties. A producing gas well was completed. No royalties were paid as the gas was not marketed. The court found that where the principal consideration for a lease is the payment of a royalty, the lease carries an implied covenant to use reasonable diligence to market the product. Severson v. Barstow, 103 M 526, 63 P2d 1022 (1936).

Implied Stipulation: Where a person makes an offer by mail and requires an answer of acceptance by return mail, the making of the offer is accompanied by an implied stipulation that the answer shall be so sent. If it is not so sent, the person making the offer is released from it. Beale v. Lingquist, 92 M 480, 15 P2d 927 (1932).

28-3-702. Necessary and incidental terms.

Case Notes

Waiver of Contract Rights — Late Payments Not Considered Breach Based on Prior Acceptance: The uninsured employers' fund (UEF) sought indemnity from an employer that did not have workers' compensation insurance using a monthly payment arrangement that was agreed to by the parties. The UEF accepted four late payments before turning the employer over to collections, at which point the employer sued UEF for breach of contract. The Supreme Court held that UEF waived its right to terminate the contract based on late payment when it accepted late payments without objection. Consequently, it was a breach of contract for the UEF to turn the employer over to collections and the employer was entitled to damages. Elk Mtn. Motor Sports, Inc. v. Dept. of Labor and Industry, 2012 MT 261, 367 Mont. 36, 289 P.3d 165.

Allowance for Suspension Without Pay Contained in Policies Covered by Employment Manual — Suspension Proper: A doctor was suspended without pay by a health care facility for failing to sign outstanding warrants. The doctor contended that the suspension was improper because the employment contract allowed for suspension without pay only under specific circumstances, none of which were present in this case. However, the employment contract also contained a provision requiring the doctor to follow the facility policies and procedures, and that reference clearly incorporated the facility's employment manual into the employment contract. The employment contract was not inconsistent with the employment manual, nor was the disciplinary procedure used by the facility to suspend the doctor inconsistent with the employment contract. Thus, the District Court correctly held that the doctor was properly suspended without pay and that the suspension did not violate the employment contract. The doctor's claim for wages during the suspension also failed absent evidence of the hours worked and the ability to calculate the value of those hours. Marias Healthcare Serv., Inc. v. Turenne, 2001 MT 127, 305 M 419, 28 P3d 491 (2001).

Date Contract Enforceable — Effect of Absence of Collateral Terms to Be Added: In an action by a real estate broker against a seller for a brokerage commission, it was argued that if the sale of the property was enforceable on January 31, 1978, the broker would be entitled to his commission. If the sale was not enforceable until August 18, 1978 (90 days after expiration of broker's contract), he would not be entitled to his commission. The buy-sell was executed on January 31, 1978, but two financial terms within the contract were left out. The terms left out involve the method of payment, a collateral issue to the contract. The contract for deed was valid and enforceable on January 31, 1978, and the broker is entitled to his commission. Nardi v. Smalley, 197 M 321, 643 P2d 228, 39 St. Rep. 606 (1982).

Sale of a Water Right With Implied Reservation of Another Water Right: Landowner owned two water rights on a river and each had a related ditch right; one was called the "McNiven Right" and the other was called the "Grannis Right". He sold part of his land together with part of the McNiven Right and "related ditch rights". The Supreme Court held that the words "related ditch rights" in the deed's water right grant referred only to the McNiven ditch, and further held that since the landowner held two water rights and related ditch rights, the conveyance of the McNiven water and ditch right impliedly reserved to landowner the Grannis water right and related ditch right. Castillo v. Kunnemann, 197 M 190, 642 P2d 1019, 39 St. Rep. 460 (1982), reversing on rehearing, 38 St. Rep. 1618 (1981).

Sale of Apartments in Condominium: Where corporation selling apartments in condominium sought to sell space for commercial purposes in the same building, injunction was proper since even though restriction was not stated in sales contract or deed to apartment buyers, an equitable servitude could be implied as an essential part of the deed. Thisted v. Country Club Tower Corp., 146 M 87, 405 P2d 432 (1965).

Water Right Conveyance: Where a deed to a tract of farmland expressly conveyed a water right sufficient in amount to irrigate the acreage sold, all other rights theretofore used in connection with the land were impliedly excluded and did not pass under the general appurtenance clause in the deed. Lensing v. Day & Hansen Sec. Co., 67 M 382, 215 P 999 (1923).

Farm Lease: A lease of agricultural lands which did not impose upon either party the work of preparing them for crops or provide who should furnish seed, bear the expense of harvesting, extra help, etc., was not void for uncertainty, it being implied under this section from the fact that the lessees were to have possession for the purpose of producing crops, that they were to do these things. McDonald v. McNinch, 63 M 308, 206 P 1096 (1922).

28-3-703. When promise presumed to be joint and several.

Law Review Articles

Presumptions Concerning Contracts, Clarke, 37 Mont. L. Rev. 101 (1976).

28-3-704. Contractual right to attorney fees treated as reciprocal — exception.

Compiler's Comments

2017 Amendment: Chapter 313 in (1) at beginning inserted exception clause; inserted (2) concerning contracts involving a party with condemnation authority and a private party subject to the condemnation authority; and made minor changes in style. Amendment effective October 1, 2017.

Applicability: Section 2, Ch. 313, L. 2017, provided: "[This act] applies to contracts or obligations between a private party and a party with condemnation authority over the private party's property entered into on or after [the effective date of this act]." Effective October 1, 2017.

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Reciprocal Right 457
Prevailing Party 459
General 463

RECIPROCAL RIGHT

Reciprocity Requirement Correctly Applied to Attorney Fees Only, Not Costs: The borrower prevailed in a contract dispute between the borrower and its lending bank. The contract provided that the bank was entitled to an award of its costs and fees but did not provide a reciprocal right to the borrower. The borrower argued that this provision should be read to be reciprocal pursuant to 28-3-704. The District Court awarded statutory costs under 25-10-201 but not the borrower's total costs. On appeal, the Supreme Court affirmed, holding that the plain language of the reciprocal attorney fees statute does not apply to costs. Masters Group Int'l, Inc. v. Comerica Bank, 2021 MT 161, 404 Mont. 434, 491 P.3d 675.

Valid Choice-of-Law Provision Governing Entire Contract Properly Applied to Attorney Fee Provision: A contract between a borrower and a bank contained a choice-of-law provision stating that all disputes arising out of the contract would be resolved under Michigan law. The contract also provided that the borrower was required to reimburse the bank's costs and expenses but did not provide for the bank to reimburse the borrower's costs and expenses. The District Court found that the choice-of-law provision applied and that the bank breached the contract. The District Court performed a separate choice-of-law analysis and determined that Montana law applied to the attorney fee provision. It awarded attorney fees to the borrower, reasoning that the nonreciprocal attorney fee provision in the contract would be statutorily reciprocal under 28-3-704. On appeal, the Supreme Court reversed, holding that Michigan law governed all disputes regarding the contract, including disputes regarding attorney fees, and that under Michigan law there was no authority to award attorney fees to the borrower under the contract. Masters Group Int'l, Inc. v. Comerica Bank, 2021 MT 161, 404 Mont. 434, 491 P.3d 675.

Contractual Right to Attorney Fees Reciprocal: A credit agreement provided that the creditor would be awarded collection costs and legal fees as a reasonable cost of the suit in the event that it became necessary for the creditor to initiate any legal or collection action under the agreement. The Supreme Court held that the effect of 28-3-704 given this term is to provide a reciprocal right to attorney fees to the debtor. Kenyon-Noble Lumber Co. v. Dependant Foundations, Inc., 2018 MT 308, 393 Mont. 518, 432 P.3d 133.

Contract Provisions Granting Attorney Fees to One Party — Fees Granted Against That Party — Reciprocal by Statute: The plaintiff health insurance company filed a breach of contract action against the defendant, an employer providing health insurance for its employees. The contracts between the parties required the defendant to indemnify the plaintiff for all expenses arising out of a breach of contract action. Ultimately, the Supreme Court ruled in favor of the defendant, holding that attorney fees were reciprocal by statute, and therefore appropriate against the plaintiff. Mont. Health Network, Inc. v. Great Falls Orthopedic Associates, 2015 MT 186, 379 Mont 513, 353 P.3d 483.

Improper Reciprocal Right — Attorney Fees: The covenants of a homeowners' association allowed recovery of attorney fees for failure of an owner to pay the association's assessments. A plaintiff prevailed in a declaratory action against the homeowners' association, arguing that an assessment for a capital improvement was subject to the covenants' requirements for special assessments. On appeal, the Supreme Court affirmed the District Court's grant of declaratory judgment for the plaintiff. However, the Supreme Court also reversed in part, finding that the District Court erred in awarding reciprocal attorney fees to the plaintiff under this section because the plaintiff initiated the lawsuit to determine whether the homeowner's covenants required a special approval for a capital improvement assessment, and reciprocity would apply only to an action in which the plaintiff prevailed over the homeowners' association concerning the recovery of unpaid assessments by the plaintiff. Beebe v. Bd. of Directors of the Bridger Creek Subdivision Community Ass'n, 2015 MT 183, 379 Mont. 484, 352 P.3d 1094.

Reciprocal Attorney Fees Not Allowed — No Allegations Related to Default Provision: The plaintiff was not entitled to reciprocal fees under this section because the provision that provided for attorney fees applied only to default situations, and the plaintiff's complaint raised no allegations relating to default. Hoff v. Lake County Abstract & Title Co., 2011 MT 118, 360 Mont. 461, 255 P.3d 137.

Reciprocal Attorney Fees and Costs Under Loan Guaranty: A loan guaranty provided that the guarantor would pay costs and expenses incurred in connection with enforcement of the guaranty. After holding for the defendant guarantors, the trial court awarded witness fees and litigation costs to defendants, and the plaintiff bank appealed. The Supreme Court affirmed. Contractual attorney fees and costs provisions are reciprocal under 28-3-704, so the award to defendants was not in error. First Citizens Bank v. Sullivan, 2008 MT 428, 347 M 452, 200 P3d 39 (2008).

Attorney Fees Through Fee-Shifting, but Limited Fees-for-Fees, Recoverable for Defendants Under Declaration of Covenants: A declaration of covenants provided that the applicant for relief was entitled to recover attorney fees in any action for enforcement of the covenants. Plaintiffs applied for relief, but defendants were granted summary judgment and sought attorney fees. Plaintiffs contended that defendants were not allowed attorney fees under the declaration because defendants were not the applicant for relief. However, this section renders contractual fee-shifting provisions reciprocal, so as the prevailing party, defendants were entitled to reasonable attorney fees, including fees-for-fees to the extent that attorney fees were incurred in establishing defendants' entitlement to fees under the contract. Defendants' claim for attorney fees for fees incurred in establishing the amount of attorney fees was not compensable under the contract, and the District Court erred in awarding attorney fees to defendants incurred in establishing the amount of fees. In addition, the court erred in awarding defendants' attorney fees incurred in securing the withdrawal of plaintiffs' attorney because of a conflict of interest because that cost was not a necessary expense of enforcement of the declaration. Because the District Court erred by awarding defendants all legal costs without making an effort to ascertain the specific source of the costs, the issue was remanded for a proper determination of fees, particularly fees-for-fees, that defendants could recover. Chase v. Bearpaw Ranch Ass'n, 2006 MT 67, 331 M 421, 133 P3d 190 (2006).

No Reciprocal Right to Attorney Fees When Issue Not Contained in Pretrial Order or Raised at Trial: Plaintiff sought $900,000 in attorney fees, posttrial, based on a request for attorney fees by defendant in its pleading, arguing that under this section, the award of attorney fees should be reciprocal. The District Court did not abuse its discretion in denying the request because it was not contained in the pretrial order or raised at trial and thus was not properly before the court. Simmons Oil Corp. v. Wells Fargo Bank, N.A., 1998 MT 129, 289 M 119, 960 P2d 291, 55 St. Rep. 508 (1998), distinguished in In re Estate of Lande, 1999 MT 179, 295 M 277, 983 P2d 316, 56 St. Rep. 701 (1999).

Inapplication of Attorney Fee Provision of Buy-Sell Agreement Held to Mean Inapplication of Reciprocal Right Under Statute: Gainey sold real property located on Flathead Lake to Garrison, and Garrison later sued Gainey, alleging constructive fraud and failure of consideration, and sought rescission of the buy-sell agreement. The Supreme Court noted that the provisions of the buy-sell agreement provide for payment of attorney fees only in the instance of default, breach of contract, and specific performance. The Supreme Court held that because Gainey was not sued for default or breach of contract and specific performance was not sought, the attorney fee provisions of the buy-sell agreement were inapplicable and, therefore, the reciprocal fee provisions of this section do not apply. Gainey was therefore not entitled to recover his attorney fees. Garrison v. Averill, 282 M 508, 938 P2d 702, 54 St. Rep. 454 (1997).

Water Supply Company Not Entitled to Attorney Fees if Successful Defending Against Class Action: Certain residents of Butte brought a class action against the local water company alleging that the water was polluted and was a health problem. The company argued that the lower court should have included in the notice sent to residents concerning the class action a statement that if the residents chose to join in the action, they might be liable for the water company's attorney fees if the company was successful in defending against the suit. The Supreme Court held that the contract between the company and the residents for the supply of water did not contain an express provision providing for attorney fees and therefore the prevailing party had no contractual right to fees and further held that the lower court had properly excluded any reference to attorney fees from the notice. McDonald v. Washington, 261 M 392, 862 P2d 1150, 50 St. Rep. 1374 (1993).

Attorney Fees Not Recoverable Under Contract — Failure of Either Party to Raise Issue of Attorney Fees in Pretrial Order as Precluding Reciprocal Award: Although both parties claimed attorney fees in the pleadings, the final pretrial order did not include any reference to attorney fees, the fees were not listed as a contention at trial, and the amount to be awarded to the prevailing party was not listed as a fact to be considered at trial. Because attorney fees were not recoverable by defendant under the contract language and no evidence was presented on the issue at trial, failure by either party to raise the issue in the pretrial order placed the issue outside the record of the District Court and it was error for the court to amend the judgment to grant fees to defendant on grounds of reciprocity. Naftco Leasing Ltd. Partnership 301 v. Finalco, Inc., 254 M 89, 835 P2d 729, 49 St. Rep. 644 (1992), distinguishing Bell v. Richards, 228 M 215, 741 P2d 788 (1987).

Debtors Entitled to Attorney Fees on Reciprocity — Bank Entitled to Fees on Foreclosure: In the trial court and on appeal, the debtors in an action to foreclose on a deed of trust on residential real property were entitled to attorney fees on the basis of reciprocity under this section; on foreclosure, the bank was entitled to attorney and trustee fees granted by 71-1-320. First Fed. S&L Ass'n of Missoula v. Anderson, 238 M 296, 777 P2d 1281, 46 St. Rep. 1280 (1989), distinguished in Valeo v. Tabish, 1999 MT 146, 295 M 34, 983 P2d 334, 56 St. Rep. 579 (1999).

Reciprocal Award of Contractual Attorney Fees — Not Subject to Contingent Fee Agreement: Since one purpose for a contractual provision for attorney fees is to make the successful party whole, it should be clear that the attorney fees, when finally fixed by the court, belong to the party and are not subject to a contingent fee agreement. Weinberg v. Farmers St. Bank of Worden, 231 M 10, 752 P2d 719, 45 St. Rep. 391 (1988).

Reciprocal Right: A clause in a contract for sale that provides that the seller is entitled to reasonable attorney fees in any subsequent litigation also gives a similar right to the buyer and includes fees incurred on appeal. Magers v. The Shining Mtns., 230 M 373, 750 P2d 449, 45 St. Rep. 283 (1988).

Failure to Mention Attorney Fee Issue on Pretrial Order — Reciprocal Right Not Abandoned: Defendants did not abandon their right to attorney fees by failing to mention the issue under "defendants' contentions" on the pretrial order. The right is reciprocal. Under this section, plaintiffs had a contractual right to attorney fees and so did defendants. Bell v. Richards, 228 M 215, 741 P2d 788, 44 St. Rep. 1467 (1987).

Reciprocal Fee Allowance Under Unenforceable Contract: Even though note and mortgage were unenforceable for lack of consideration, "mortgagor" was entitled to attorney's fee under this section for defending suit on mortgage, which provided for attorney's fee for mortgagee in event of foreclosure. Bartmess v. Bourassa, 196 M 231, 639 P2d 1147, 39 St. Rep. 56 (1982).

Contract for Deed Providing for Attorney Fees: Attorney fees were properly granted sellers under a contract for deed where buyer defaulted and the contract specifically provided for them. Hares v. Nelson, 195 M 463, 637 P2d 19, 38 St. Rep. 2036 (1981).

Indemnity Suit — No Reciprocal Right to Attorney Fees: This section grants a reciprocal right to attorney fees only when the party from whom one is requesting fees has an express right to attorney fees. Thus when plaintiff in a suit for indemnity did not have an express right to attorney fees and no agreement existed between plaintiff and defendant, the alleged indemnitor, defendant, even though a successful party, had no right to recover attorney fees under this section. Town Pump v. Diteman, 191 M 98, 622 P2d 212, 38 St. Rep. 54 (1981), followed in Lasar v. Bechtel Power Corp., 223 M 491, 727 P2d 526, 43 St. Rep. 1938 (1986).

Broker's Commission: In an action involving a broker's commission in which the contract to sell the real estate gave plaintiff the express right to collect attorney fees, this statute made the right reciprocal as to defendant. As the prevailing party defendant is entitled to an award of reasonable attorney fees. Diehl & Associates, Inc. v. Houtchens, 180 M 48, 588 P2d 1014 (1979). See also Fields v. Wells, 239 M 392, 780 P2d 1141, 46 St. Rep. 1775 (1989).

Tortious Conversion: When a complaint alleged a tortious conversion against some defendants in a foreclosure action against another defendant, 30-9-511 (now repealed) was not applicable to the former. However defendants in the alleged tortious conversion were entitled to attorney fees by virtue of this section even though such action arose out of events that occurred prior to that section's effective date. Belgrade St. Bank v. Swainson, 172 M 350, 564 P2d 174 (1977).

Right Exists Regardless of Who Instituted Action: A reciprocal right to attorney fees does not exist only when the party having the contractual right institutes the action. Compton v. Alcorn, 171 M 230, 557 P2d 292 (1976), followed in Rauch v. Michel, 221 M 1, 716 P2d 617, 43 St. Rep. 587 (1986), and in Carey v. Wallner, 223 M 260, 725 P2d 557, 43 St. Rep. 1706 (1986), affirmed, 229 M 57, 744 P2d 881, 44 St. Rep. 1778 (1987).

PREVAILING PARTY

Attorney Fees Awarded Pursuant to Contract — No Discretion to Not Award Fees to Prevailing Party: The parties entered into a contract that provided that if litigation occurred, the prevailing party would be awarded its attorney fees. The plaintiff sued the defendants for faulty design and construction of a roof, and the defendants were granted summary judgment. The District Court also ordered the plaintiff to pay the attorney fees of one of the defendants pursuant to the parties' contract. On appeal, the Supreme Court affirmed, ruling that the District Court did not have discretion to deny the attorney fees, given the language of the contract. Hill County High School District No. A. v. Dick Anderson Constr., 2017 MT 20, 386 Mont. 223, 390 P.3d 602.

Award of Attorney Fees on Appeal: If a contract includes a provision stating that the prevailing party is entitled to reasonable attorney fees arising from litigation under the contract, appellate attorney fees are included under the provision. Boyne USA, Inc. v. Lone Moose Meadows, LLC, 2010 MT 133, 356 Mont. 408, 235 P.3d 1269.

Payment of Actual Costs and Discretionary Attorney Fees Under Contract: A real estate contract provided that the award of reasonable attorney fees to the prevailing party was discretionary with the court and also provided that the prevailing party was entitled to actual costs. The District Court deducted fees and costs related to actions in which plaintiff did not prevail, resulting in a reduction of both attorney fees and costs. On appeal, the Supreme Court affirmed the attorney fee award as an appropriate exercise of the District Court's discretion, but reversed the reduced award of costs because plaintiff was entitled to actual costs under the contract. Gullett v. Van Dyke Constr. Co., 2005 MT 105, 327 M 30, 111 P3d 220 (2005).

No Award of Attorney Fees on Appeal When None Granted at Trial: As the prevailing party on appeal, defendant contended that attorney fees should be awarded. Citing Gen. Motors Acceptance Corp. v. Finch, 246 M 359, 805 P2d 1331 (1990), the Supreme Court declined to award attorney fees on appeal because the District Court did not award defendant attorney fees in the first place and defendant failed to appeal the District Court's determination not to award attorney fees to any party upon summary judgment. R.C. Hobbs Enterprises, LLC v. J.G.L. Distrib., Inc., 2004 MT 396, 325 M 277, 104 P3d 503 (2004).

No Reciprocal Right to Attorney Fees When No Contract Formed — Prevailing Party Under Wrongful Discharge From Employment Act Not Entitled to Attorney Fees Absent Written Offer to Arbitrate: Under 39-2-915, a party is not entitled to attorney fees under the Wrongful Discharge From Employment Act unless that party makes a written offer to arbitrate that is refused and that party prevails in the action. Here, a probationary law enforcement officer made an offer to arbitrate with the town on a wrongful discharge claim, but the town prevailed in the action without making an arbitration offer. The town subsequently claimed a reciprocal right to attorney fees under this section, asserting that the officer's request to arbitrate qualified as an obligation in the nature of a contract that granted the town the same rights as the officer. The Supreme Court disagreed. To hold that 39-2-915 provided the town a reciprocal right to attorney fees would defeat the statutory element that rewards the making of an arbitration offer and allow a party that refuses to arbitrate to claim attorney fees. Further, if an offer to arbitrate is not accepted and no arbitration occurs, no contract is formed upon which a right to reciprocal fees can be based under this section. Denial of the town's request for reciprocal fees was properly denied. Ritchie v. Ennis, 2004 MT 43, 320 M 94, 86 P3d 11 (2004).

Recovery of Attorney Fees, Including Appeal Costs, Based on Indemnification Provision in Underlying Contract: Four people decided to start a business, but ultimately three decided to opt out and exchange their respective corporate shares of stock for cash. The release agreement also held the three harmless from all causes of action relating to the incorporation and provided an indemnification clause that held each party harmless from and against all liability, claim, loss, damage, or expense, including attorney fees, incurred or required to be paid by the other parties by reason of any breach or failure of observance or performance of any representation, warranty, or covenant or other provision of the agreement. Nevertheless, the corporation subsequently sued one of the three resigning members for breach of fiduciary duty, conversion, actual and constructive fraud, and negligent misrepresentation, seeking $110,000 in general damages and also punitive damages. Defendant counterclaimed that by filing a claim that was barred by the release agreement, the corporation had breached its contract. Following trial, the District Court awarded only $3,673.53 for constructive fraud, but also concluded that all claims based on the parties' contractual relationship were barred. Each party then requested attorney fees as the prevailing party pursuant to the indemnification clause, but the court denied the motions, holding that there was no prevailing party because each party had gained a victory but also suffered a loss. The corporation appealed, seeking attorney fees. The Supreme Court held that pursuant to the reciprocal right under 28-3-704, the corporation had the statutory right to recover attorney fees, but only the fees incurred in defending the breach of contract counterclaim as the prevailing party, pursuant to the contractual indemnification provision. Under the same reasoning, the Supreme Court awarded attorney fees for costs of appeal as well, remanding for a determination of fees. Transaction Network, Inc. v. Wellington Technologies, Inc., 2000 MT 223, 301 M 212, 7 P3d 409, 57 St. Rep. 920 (2000), followed in Peschel Family Trust v. Colonna, 2003 MT 216, 317 M 127, 75 P3d 793 (2003).

Assignment of Retail Installment Contract — Breach of Warranty — Abrogation of Waiver of Recourse: Arcadia Financial, Ltd. (Arcadia), is a Minnesota corporation that purchases retail installment contracts from automobile dealers, including Prestige Toyota (Prestige) in Billings, after the dealers have entered into installment contracts with automobile buyers. Knight purchased a Toyota from Prestige, and Knight's contract contained a provision assigning the contract to Arcadia under one of four options. The same day that Knight purchased the automobile, Prestige assigned the contract to Arcadia "without recourse", which meant that only the contract warranties applied, one of which was that Prestige had a valid certificate of title and would send it to the appropriate officials within 10 days of sale to ensure Arcadia's interest in the vehicle. The contract also provided that Prestige unconditionally guaranteed full performance of the contract in the event that it breached any of the warranties. Prestige failed to send a valid certificate of title as required. Knight later defaulted and filed for bankruptcy protection. Arcadia demanded that Prestige repurchase the Knight contract. Prestige admitted breaching the warranty but claimed that it was not required to repurchase the contract and refused to do so, asserting that Arcadia's damages were limited to the amount that the bankruptcy trustee received from sale of the automobile. The District Court awarded Arcadia the principal amount due on the Knight contract, plus interest, attorney fees, and costs, concluding that under the clear language of the contract assignment provisions, Prestige had guaranteed payment of all sums due when it failed to deliver the valid title within the time required. The Supreme Court agreed, noting that the contract was converted into a full recourse contract when Prestige failed to deliver the valid title, so Prestige was required to repurchase the contract for the amount of principal remaining due. The detriment proximately caused by Prestige's failure to repurchase the contract was the principal amount owing on the contract. Further, the District Court properly awarded attorney fees to Arcadia as the prevailing party pursuant to 28-3-704. Arcadia Financial, Ltd. v. Prestige Toyota, 1999 MT 273, 296 M 494, 989 P2d 831, 56 St. Rep. 1111 (1999).

Award of Attorney Fees and Costs on Appeal of Contract Action: Under former Rule 33, M.R.App.P. (now superseded), costs in civil actions were automatically awarded to the prevailing party and, additionally, when an award of attorney fees was based on a contract, the prevailing party was also entitled to an award of reasonable attorney fees incurred on appeal. Chamberlin v. Puckett Constr., 277 M 198, 921 P2d 1237, 53 St. Rep. 593 (1996).

Verdict That Neither Party Breached — Party That Made Higher Monetary Claim Owes Costs and Attorney Fees: Inn sued for $15,556 in damages for breach of a remodeling contract, claiming incomplete performance by the contractor. The contractor counterclaimed for failure to pay the total of the monthly payments due him, alleging that $1,609 was still owed. The contract provided that the prevailing party in a suit would be entitled to costs and attorney fees. The jury found that neither party was in breach. Because the contractor prevailed on the main issue in controversy, Inn's claim for $15,556 in damages, the contractor was the prevailing party and was entitled to costs and attorney fees. Rod & Rifle Inn, Inc. v. Giltrap, 273 M 232, 902 P2d 38, 52 St. Rep. 945 (1995).

Right to Attorney Fees When Defendant Files for Entry of Judgment After Originally Denying Allegations: The parties, Gandy and Eschler, entered into an agreement releasing each other from the performance of a real estate purchase contract upon the payment of $20,000 by Eschler to Gandy. Eschler defaulted on the payments, and Gandy brought an action seeking specific performance requiring Eschler to pay the underlying contract price of $258,640 or in the alternative the $20,000. After originally denying the allegations in Gandy's complaint, Eschler moved the District Court to enter a judgment against him for the balance of the $20,000 owed to Gandy. The Supreme Court held that Gandy was a prevailing party entitled to attorney fees under the provisions of the contract between the parties because Eschler had initially denied the allegations in Gandy's complaint. Gandy v. Eschler, 261 M 355, 862 P2d 1116, 50 St. Rep. 1357 (1993).

No Prevailing Party When All Parties Prevail in Part on Some but Not All Issues: There are some cases when, at the close of litigation, there is no actual prevailing party entitled to attorney fees because both parties gain a victory but also suffer a loss. Such was the case at bar when even though all parties prevailed in part and were entitled to part of a judgment award, none prevailed on all issues or recovered the total of what was individually sought. Failure of the trial court to award attorney fees to any of the parties was not error. Nyquist v. Nyquist, 255 M 149, 841 P2d 515, 49 St. Rep. 927 (1992), followed in Marias Healthcare Serv., Inc. v. Turenne, 2001 MT 127, 305 M 419, 28 P3d 491 (2001).

Attorney Fees to Successful Litigants — Voluntary Dismissal of Moot Counterclaim Not Trial Loss: Attorney fees were properly granted sellers of property under a contract for deed provision that awarded fees to successful litigants. Seller's voluntary dismissal of a moot counterclaim does not constitute a trial loss invalidating the contract provision. Lauderdale v. Grauman, 223 M 357, 725 P2d 1199, 43 St. Rep. 1785 (1986), followed in Gen. Motors Acceptance Corp. v. Finch, 246 M 359, 805 P2d 1331, 47 St. Rep. 2154 (1990), and in Wise v. Sebena, 248 M 32, 808 P2d 494, 48 St. Rep. 309 (1991).

Prevailing Party: While no one factor should be considered in determining the prevailing party, the party that survives an action involving a counterclaim with the net judgment should generally be considered the successful party. Rustics of Lindbergh Lake, Inc. v. Lease, 213 M 246, 690 P2d 440, 41 St. Rep. 2092 (1984).

"Prevailing Party" When Usury Penalty Assessed Against Party Exceeds That Party's Recovery: Appellants filed an action to recover money due on a promissory note that was usurious on its face. The District Court assessed a usury penalty against appellants which exceeded the balance due on the note. Thus, the net judgment was in favor of respondents. The court then assessed attorney fees against the appellants. On appeal, the Supreme Court affirmed, ruling that respondents had been properly found to be the prevailing party. E.C.A. Envtl. Management Serv., Inc. v. Toenyes, 208 M 336, 679 P2d 213, 41 St. Rep. 388 (1984).

Attorney Fees — Not Costs — Timeliness: The defendants signed a contract to purchase a tract of land from plaintiffs. The contract provided for attorney fees to the prevailing party in an action commenced on the contract. Plaintiffs filed suit alleging that under the contract and various oral agreements, defendants had agreed to pay a real estate commission to plaintiffs. The trial court granted summary judgment to defendants, holding that written evidence of an agreement to pay a commission did not exist. No notice of entry of judgment was ever filed. Defendants later moved to set an attorney fee award. The trial court ruled that under Title 25, ch. 10, attorney fees were not recoverable costs and that the motion for costs was not timely, as it was not filed within 5 days of judgment. On appeal, the Supreme Court held that attorney fees were awardable under the contract and that defendants' motion was essentially a motion to amend judgment under former Rule 59(g), M.R.Civ.P. (now superseded). The motion was timely made since no notice of entry of judgment was ever filed. Cook v. Harrington, 203 M 479, 661 P2d 1287, 40 St. Rep. 580 (1983), followed in In re Estate of Lande, 1999 MT 179, 295 M 277, 983 P2d 316, 56 St. Rep. 701 (1999).

Action for Rescission of Contract: Contention that contract provision allowing attorney fees and costs to the prevailing party applied only to actions to enforce the contract and not to the instant action for rescission of the contract lacked merit, particularly when parties making that claim amended their complaint to seek attorney fees and only objected to such an award after the other party prevailed in the action and was granted attorney fees and costs. Preston v. McDonnell, 203 M 64, 659 P2d 276, 40 St. Rep. 297 (1983), affirmed in Carey v. Wallner 229 M 57, 744 P2d 881, 44 St. Rep. 1778 (1987). See also Carey v. Wallner, 223 M 260, 725 P2d 557, 43 St. Rep. 1706 (1986), Norwood v. Serv. Distrib., Inc., 2000 MT 4, 297 M 473, 994 P2d 25, 57 St. Rep. 8 (2000) (citing Mackintosh v. Calif. Sav. Fed'n, 935 P2d 1154 (Nev. 1997)), and Jorgensen v. Trademark Woodworks, LLC, 2018 MT 291, 393 Mont. 381, 431 P.3d 29.

Persons Not Parties to Contract — Right to Attorney Fees Under Contract Granting Them: When suit is brought under a contract providing for attorney fees to the prevailing party, persons who are not parties to the contract are not entitled to attorney fees, either under the contract or a statutory attorney fees provision. Where persons who were not parties to a contract by which a business was sold guaranteed payment of the purchase price, a guarantee which they had no intention of honoring, it was error to award them attorney fees upon finding that they were not liable under the guarantee because they received no consideration from plaintiff seller of the business for their guarantee. Rudio v. Yellowstone Merchandising Corp., 200 M 537, 652 P2d 1163, 39 St. Rep. 1923 (1982).

District Court to Award Attorney Fees if Contract Provided: If a contract provides for attorney fees to the prevailing party, the District Court should have awarded attorney fees to the prevailing party. Wortman v. Griff, 200 M 528, 651 P2d 998, 39 St. Rep. 1916 (1982).

Determination of Validity of Lease: The tenant was forced to sue to determine the validity of the lease. The tenant prevailed in his suit and is therefore entitled to attorney's fees under this section. Kosena v. Eck, 195 M 12, 635 P2d 1287, 38 St. Rep. 1736 (1981).

Attorney's Fees for Action to Compel Forfeiture: The defendants defaulted on a contract for deed in October 1977, but in March 1978, tendered to the plaintiffs the full amount due under the contract, plus the plaintiffs' personal expenses and attorney's fees. The plaintiffs brought suit to enforce forfeiture of the defendant's payments made under the contract, but the court refused to enforce the forfeiture. Under these circumstances, the court erred in granting the plaintiffs their attorney's fees under a contract provision which entitled the prevailing party to his attorney's fees in the event of suit. The defendants have been ready, willing, and able to perform the contract since March 1978. Because the defendants were not relieved from their default but only from forfeiture, the defendants should pay the plaintiffs their reasonable attorney's fees until the time of tender of payment in March 1978. Sharp v. Holthusen, 189 M 469, 616 P2d 374, 37 St. Rep. 1651 (1980).

Losing Party Not Awarded Attorney Fees: Appellant's request for attorney fees pursuant to a contract provision was dismissed since it was not the successful party in litigation. Mont. Williams Double Diamond v. Royal Village, Inc., 186 M 359, 607 P2d 1120 (1980).

Prevailing Party in Real Estate Contract: By virtue of this section the contractual right to attorney fees contained in a real estate broker's contract was reciprocal and entitled the defendant, as the prevailing party, to an award of his attorney fees. Lyle v. Moore, 183 M 274, 599 P2d 336 (1979).

GENERAL

Only Contractual Attorney Fees Reciprocal Under 28-3-704, Not Statutory Attorney Fees. Rafes v. McMillan, 2022 MT 13, 407 Mont. 254, 502 P.3d 674.

Challenge to Award of Attorney Fees Based on Contract — Failure to Argue that Claim Was Not Based on Contract Before District Court — Supreme Court Refusal to Review Argument: The District Court awarded the prevailing hospital attorney fees pursuant to its signed Patient Service Agreement contract with the plaintiff estate. On appeal, the estate argued that the hospital was not entitled to recover attorney fees under the contract because it did not bring an action on the contract. Citing In re Parenting of N.S., 2011 MT 98, 360 Mont. 288, 253 P.3d 863, the Supreme Court declined to address the estate's argument because it had not been presented to the District Court. Estate of Donald v. Kalispell Regional Medical Center, 2011 MT 166, 361 Mont. 179, 258 P.3d 395.

Attorney Fees Owing Despite Choice of Enforcement Alternative Provided in Contract: A real estate sale contract provided three enforcement alternatives for the seller to apply in case of a default by the buyers. Two of the three alternatives expressly provided for payment of attorney fees, but one did not. The seller chose the alternative remedy that did not expressly provide for attorney fees, and the buyers contended that attorney fees were thus not owing. However, a later provision in the contract provided that the seller was entitled to attorney fees regardless of which alternative the seller elected, so the District Court properly awarded attorney fees under the clear language of the more comprehensive contract provision. Weter v. Archambault, 2002 MT 336, 313 M 284, 61 P3d 771 (2002).

Verdict That Neither Party Breached — Party That Made Higher Monetary Claim Owes Costs and Attorney Fees: Inn sued for $15,556 in damages for breach of a remodeling contract, claiming incomplete performance by the contractor. The contractor counterclaimed for failure to pay the total of the monthly payments due him, alleging that $1,609 was still owed. The contract provided that the prevailing party in a suit would be entitled to costs and attorney fees. The jury found that neither party was in breach. Because the contractor prevailed on the main issue in controversy, Inn's claim for $15,556 in damages, the contractor was the prevailing party and was entitled to costs and attorney fees. Rod & Rifle Inn, Inc. v. Giltrap, 273 M 232, 902 P2d 38, 52 St. Rep. 945 (1995).

What Constitute Reasonable Attorney Fees: In determining what constitute reasonable attorney fees, the following factors should be used as guidelines: (1) the amount and character of the services rendered; (2) the labor, time, and trouble involved; (3) the character and importance of the litigation in which the services were rendered; (4) the amount of money or the value of the property to be affected; (5) the professional skill and experience called for; (6) the character and standing in their profession of the attorneys; and (7) the result secured by the services of the attorneys. Morning Star Enterprises, Inc. v. R.H. Grover, Inc., 247 M 105, 805 P2d 553, 48 St. Rep. 112 (1991); Majers v. The Shining Mtns., 230 M 373, 750 P2d 449, 45 St. Rep. 283 (1988); Carkeek v. Ayer, 188 M 345, 613 P2d 1013 (1980); First Sec. Bank of Bozeman v. Tholkes, 169 M 422, 547 P2d 1328 (1976); Crncevich v. Georgetown Recreation Corp., 168 M 113, 541 P2d 56 (1975); Forrester & MacGinniss v. Boston & Mont. Consol. Copper & Silver Min. Co., 29 M 397, 74 P 1088 (1904).

Attorney Fees Proper When Provided in Assignment, Release, and Indemnity Agreement: The Supreme Court reversed a denial of attorney fees when an assignment, release, and indemnity agreement executed by the parties contained the substance of the parties' accord and satisfaction and specifically provided for award of attorney fees to the prevailing party in the event of litigation. Bohnsack v. Hi-Noon Petroleum, Inc., 243 M 190, 793 P2d 815, 47 St. Rep. 1125 (1990).

Contract Provision That Attorney Fees May Be Awarded — Court Need Not Award Fees: The parties entered into a water well use agreement that provided that in the case of litigation between the parties, reasonable attorney fees could be provided. The Supreme Court affirmed the lower court's refusal to award either party attorney fees on the basis that when the contract states that reasonable fees may be awarded, it is within the trial court's discretion to grant or deny either or both parties attorney fees. Baker v. Bailey, 240 M 139, 782 P2d 1286, 46 St. Rep. 2005 (1989).

Attorney Fees and Costs Award Not Abuse of Discretion: The plaintiff purchased a motorcycle dealership from the defendant. The plaintiff changed the business's name, location, and product line. The business ceased making a profit, and the plaintiff sued the defendant for fraud and negligent misrepresentation. The suit was dismissed on summary judgment. The Supreme Court affirmed the award of fees and costs, stating that the sales contract between the parties provided for attorney fees and costs. Although the award was high, it did not constitute an abuse of discretion by the lower court and could not be set aside on appeal. Batten v. Watts Cycle & Marine, Inc., 240 M 113, 783 P2d 378, 46 St. Rep. 1984 (1989).

Failure of Attorney to Read Findings, Conclusions, and Order Not Excusable Neglect: Defendant prevailed in a case regarding a real estate transaction. The trial court addressed reciprocal award of attorney fees in its findings, conclusions, and order and set a hearing to determine fees. Plaintiff's attorney failed to read the findings, to notice the date of the hearing, or to appear at the hearing. Defendant was subsequently allowed to present his claim for fees and costs. The District Court properly found that the attorney's failure to carefully read the findings, conclusions, and order was not excusable neglect. Watson v. Fultz, 239 M 364, 782 P2d 361, 46 St. Rep. 1751 (1989).

Prevailing Party — Net Judgment on Counterclaim No Justification of Attorney Fees: Although lessor received a net judgment on a counterclaim, it was within the lower court's discretion to not award attorney fees when both parties had breached the contract. The award of money was only one factor in determining the prevailing party. Empire Dev. Co. v. Johnson, 236 M 433, 770 P2d 525, 46 St. Rep. 487 (1989).

Attorney Fees Not Awardable on Affidavit of Counsel — Hearing Required: Even though a contract may provide for the award of reasonable attorney fees, it is improper to award attorney fees solely on the affidavit of counsel without holding an evidentiary hearing on the matter. Stark v. Borner, 234 M 254, 762 P2d 857, 45 St. Rep. 1885 (1988), followed in Rothing v. Kallestad, 2007 MT 109, 337 M 193, 159 P3d 222 (2007).

Denial of Attorney Fees When Both Parties Breach Contract: Seller of real property breached a contract by not providing mortgage releases, while buyer breached by not making contract payments when obligated to do so. In light of the breach of contract by both parties, a District Court award of attorney fees based on this section was reversed. Sjoberg v. Kravik, 233 M 33, 759 P2d 966, 45 St. Rep. 1270 (1988).

Provision for Fees by Contract or Statute: Attorney fees are allowed when they are provided for by statute or contractual provision. Poulsen's, Inc. v. Wood, 232 M 411, 756 P2d 1162, 45 St. Rep. 1154 (1988), followed in Wise v. Sebena, 248 M 32, 808 P2d 494, 48 St. Rep. 309 (1991), and in Farm Credit Bank of Spokane v. Hill, 266 M 258, 879 P2d 1158, 50 St. Rep. 726 (1993).

Costs Provided by Contract Allowable Despite Tortious Nature of Claim: In an action by plaintiff to rescind a contract for sale of real property because of alleged fraud, misrepresentation, undue influence, and unconscionability, the award of attorney fees and costs that the contract provided to the successful defendant, relating to his defense and counterclaim of wrongful occupation by the plaintiff, was proper notwithstanding the contention that the action sounded in tort and not in contract (citing Winer v. Jonal Corp., 169 M 247, 545 P2d 1094 (1976)). The underlying action was based on a contract dispute. Westlake v. Osborne, 230 M 364, 750 P2d 444, 45 St. Rep. 277 (1988).

Reversal of Award of Attorney Fees — Applicability of Specific Statutes: Respondents contended that under 27-1-316, 28-3-704, and 30-14-222 they were entitled to attorney fees. The court considered each statute and decided: (1) since the issue of unlawful restraint of trade was reversed, no damages were allowable under 30-14-222; (2) because there was no allowance for attorney fees where the covenantor brings an action for breach of contract against the covenantee, 27-1-316 was inapplicable; and (3) since an agreement with an attorney fee provision was entered into prior to the July 1, 1971, effective date enumerated in 28-3-704 and was found to have been merged in the deeds that contained no such provision, 28-3-704 was also not applicable. The award of attorney fees to respondents was reversed. Haggerty v. Gallatin County, 221 M 109, 717 P2d 550, 43 St. Rep. 674 (1986).

Contractual Attorney Fees — "At Fault" Party Offering to Pay Prior to Trial Prevailing on Appeal: The parties entered into a 5-year lease for office space. Defendant failed to make a monthly rental payment, and plaintiff sent a notice of default followed by a notice to quit. An unlawful detainer action followed. The lease contained a clause providing that in the event of breach, the party "at fault" was liable for the other party's reasonable costs and attorney fees. Defendant admitted fault and, on September 14, offered to pay back rent, interest, attorney fees, and costs. Plaintiff refused and proceeded to trial. Plaintiff prevailed at the District Court, but defendant prevailed on appeal to the extent that it was found entitled to access to the protective statutes. The Supreme Court held that under these circumstances, defendant was "at fault" only until September 14 and was liable only for attorney fees through that date. The Grand Co. v. Jim Slack & Assoc., Inc., 212 M 149, 687 P2d 683, 41 St. Rep. 1654 (1984).

No Provision in Property Settlement for Attorney Fees — Fees Improperly Awarded: Where the parties to a dissolution proceeding agreed to a property settlement that did not provide for payment of attorney fees and the District Court later issued an order providing for the attorney fees to be paid by the husband if he did not comply with the agreement, the Supreme Court held that the District Court erred in issuing the order for the payment of fees by the husband. The property settlement agreement was approved by the District Court but never incorporated by reference into the decree and therefore has the status of a private contract, and the remedies for enforcement of a judgment are unavailable. Absent a statute or contractual provision, attorney fees are generally not recoverable, and since neither is involved here, there was no right to those fees. Lorge v. Lorge, 207 M 423, 675 P2d 115, 41 St. Rep. 50 (1984).

Payee-Assignor's Right to Attorney Fees Provided for by Note: Maker gave payee a promissory note which provided that maker would pay reasonable attorney fees incurred in collection of the note. Payee assigned it to corporation which sued maker on the note, maker in turn filing a third-party complaint against payee-assignor for fraudulent inducement for the note, wrongful assignment of it, and lack of consideration for it. Payee-assignor had no right to attorney fees as against maker, either under this section or the note. He had assigned all his rights under the note, and the complaint against him was not a collection action under the note. Sliter's v. Lee, 197 M 182, 641 P2d 475, 39 St. Rep. 453 (1982), followed in Shull v. First Interstate Bank of Great Falls, 269 M 32, 887 P2d 193, 51 St. Rep. 1345 (1994).

Recovery of Fees Absent Contract or Statute: Attorney fees are not generally recoverable in the absence of a contractual or statutory provision for recovery. Sliter's v. Lee, 197 M 182, 641 P2d 475, 39 St. Rep. 453 (1982), followed in Shull v. First Interstate Bank of Great Falls, 269 M 32, 887 P2d 193, 51 St. Rep. 1345 (1994).

Attorney Fees — Procedure for Determining Amount: Defendant leased a truck from plaintiff. Defendant defaulted on the lease. Plaintiff sued for amounts owing and prevailed. The lease agreement provided for attorney fees. A motion for fees was filed along with a supporting affidavit. A hearing was held, and the District Court reduced the amount awarded from what was requested. The Supreme Court found nothing improper in the award of attorney fees on appeal. R & W Leasing v. Mosher, 195 M 285, 636 P2d 832, 38 St. Rep. 1857 (1981).

"Parties to the Contract": When the plaintiff bank sued upon its contract with one defendant, codefendants who had an interest in the object of the contract but who were not "parties to the contract" could in no event become entitled to attorney fees under this section. First Westside Nat'l Bank v. Llera, 176 M 481, 580 P2d 100 (1978).

Law of the Case: The argument raised by appellant concerning the award of attorney fees in relation to the effective date of this section was the precise issue in a prior appeal of this case and was plainly and unequivocally resolved in favor of the propriety of such award. The general rule in Montana is that when a decision has been rendered by the Supreme Court on a particular issue between the same parties in the same case, whether that decision is right or wrong, it is binding and cannot be relitigated. Belgrade St. Bank v. Swainson, 176 M 444, 578 P2d 1166 (1978), followed in In re Marriage of Gies, 218 M 433, 709 P2d 635, 42 St. Rep. 1715 (1985).

Retail Installment Contract — No Award of Attorney Fees: The provision for attorney fees in the retail installment contract could not be made a basis for an award of attorney fees under this section when the contract had been fully executed and was separable from the purchase contract which was the basis of plaintiff's action. Brabender v. Kit Mfg. Co., 174 M 63, 568 P2d 547 (1977).

Proof of Costs Required: Proof of costs for reasonable attorneys' fees is required when services are contracted for or appear on a note. A determination of reasonableness is made to insure efficient administration of justice and maintain public confidence in bench and bar. Crncevich

v. Georgetown Recreation Corp., 168 M 113, 541 P2d 56 (1975). See also Stark v. Borner, 234 M 254, 762 P2d 857, 45 St. Rep. 1885 (1988), and Krone v. McCann, 205 M 190, 666 P2d 766, 40 St. Rep. 1207 (1983).

Real Estate Listings Agreement: Seller who successfully defended suit by real estate broker for payment of sales commission was entitled to recover attorney's fees. Flaherty v. Hensley, 165 M 434, 529 P2d 1389 (1975).

CHAPTER 10
AGENCY

Part 1
General Provisions

Part Case Notes

Agency — Issue Raised for First Time on Appeal Not Considered: The Supreme Court will not determine the existence of an agency relationship for the first time on appeal. Serv. Funding, Inc. v. Craft, 234 M 431, 763 P2d 1131, 45 St. Rep. 2030 (1988).

Power of Attorney — General Rules of Interpretation: A power of attorney is nothing more than an instrument in writing authorizing another to act as one's agent. The rules governing the interpretation of written instruments generally govern the construction of powers of attorney. First and foremost the intention of the parties as it existed at the time the powers were granted is to be ascertained. Next and when ascertained, that intention is to be given effect. The intention is to be ascertained from the writing alone, if possible. The words used in the writing are to be understood in their ordinary and popular sense, rather than according to their strict legal meaning, unless used by the parties in a technical sense or unless a special meaning is given to them by usage, in which case the latter must be followed. Technical words are to be interpreted as usually understood by persons in the profession or business to which they relate, unless clearly used in a different sense. The whole of the writing is to be taken together, so as to give effect to every part, if reasonably practicable, each clause helping to interpret the other. While the powers granted must be strictly pursued by the agent, where the language permits, a power must be construed so as to carry out the purposes of the appointment. Where the words used are ambiguous in themselves, they are to be taken most strictly against the principal, and the agent in his dealings with a third person may bind his principal in accordance with usage or by any construction of the ambiguous words that is reasonable. The grant of powers is not to be frittered away by very nice and metaphysical distinctions when the general tenor of the instrument is in favor of what was done under the power and when the principal has reaped the benefit of it. A strained interpretation of the powers granted should never be given. McLaren Gold Mines Co. v. Morton, 124 M 382, 224 P2d 975 (1951), distinguished in In re Trust of Jameison v. Bolich, 2000 MT 190, 300 M 418, 8 P3d 83, 57 St. Rep. 753 (2000).

Part Law Review Articles

Presumptions Concerning Agency, Clarke, 37 Mont. L. Rev. 116 (1976).

Principal-Agency Relationships as Applied to the Custody of Children, Aune, 9 Mont. L. Rev. 46 (1948).

28-10-101. Definitions of agent and agency.

Case Notes

Son of Sole Shareholder Signed for Purchases — Ostensible Agent — Binding Contract Formed: A fertilizer company sued the defendants, a Montana corporation and its sole shareholder, for a past due account on the purchase of its goods. The shareholder's son had signed for the goods, and the defendants alleged there was no binding contract between the parties because the son did not have the authority to bind the corporation. The District Court disagreed and issued an order in favor of the plaintiff. On appeal, the Supreme Court affirmed, agreeing that the son was the ostensible agent of the defendant corporation and that a binding contract therefore existed between the parties. Fitterer Sales Montana, Inc. v. Mullin, 2015 MT 272, 381 Mont. 107, 358 P.3d 885.

Establishment of Existence of Joint Venture — Plaintiff to Show Equal Right of Control of Venture: The plaintiff sued the doctor who delivered her baby for malpractice and the hospital where the baby was delivered on the basis that the hospital was liable for the doctor's negligence as the doctor and hospital were operating as a joint venture. The Supreme Court upheld the

District Court's granting of summary judgment to the hospital on the basis that the plaintiff had failed to show that the doctor and hospital had an equal right of control over the alleged joint venture, which is a necessary element of a joint venture. Brookins v. Mote, 2012 MT 283, 367 Mont. 193, 292 P.3d 347.

Deficiency Judgment Not Barred by Alleged Misrepresentations Absent Evidence of Agency: A partnership sought to bar a deficiency judgment by imputing to the lender on agency grounds responsibility for alleged misrepresentations made by a partnership member in securing signatures of borrowers to the promissory note and the trust indenture. However, absent any evidence that the partner was either an actual or ostensible agent of the lender, no imputations could be made that the lender was responsible for the misrepresentations. Trustees of the Wash.-Idaho-Mont. Carpenters-Employers Retirement Trust Fund v. Galleria Partnership, 239 M 250, 780 P2d 608, 46 St. Rep. 1661 (1989).

Control Necessary for Agency: Wolfes' tavern was destroyed in a fire caused by wires leading to a refrigeration unit serviced by the defendant, Schulz Refrigeration. The jury was instructed that the action of the Wolfes' insurance company in inspecting the tavern for fire hazards could be imputed to the Wolfes. This instruction was improperly given. Merely contacting an owner and obtaining permission to inspect his premises is not sufficient control in such owner to establish an agency relationship. The judgment was affirmed however because the grounds for objection at the trial level are different from the argument made on appeal. Wolfe v. Schulz Refrigeration, 188 M 511, 614 P2d 1015, 36 St. Rep. 2091 (1979), followed in Weingart v. C&W Taylor Partnership, 248 M 76, 809 P2d 576, 48 St. Rep. 332 (1991).

Joint Ventures: The members of a joint venture are principals for themselves and are agents as to the other members. Murphy v. Redland, 178 M 296, 583 P2d 1049 (1978).

Determination of Agency Status — Burden of Proof: Appellant failed to sustain burden of proof to establish that third party was agent of respondent when respondent never claimed there was an agency relationship, negotiations were between appellant and respondent, and information gathered by third party was at the request of the respondent. Schulz v. Peake, 178 M 261, 583 P2d 425 (1978).

Factors Determining Existence of Agency: Where service station proprietor was not required to file any written reports to oil company, proprietor could stock any merchandise of his choosing, oil company did not inspect service station and did not require proprietor to wear any particular uniform or to operate station during any particular hours, and only written agreements between oil company and proprietor were equipment leases and truck rental, oil company was not liable for injury sustained by third person on service station premises due to gasoline fire since relationship between oil company and proprietor was not one of actual agency under this section. Elkins v. Husky Oil Co., 153 M 159, 455 P2d 329 (1969).

Insurance Adjuster as Agent of Vehicle Owner: Where after automobile collision plaintiff wrote to owner of other vehicle respecting damage to his automobile and was referred to adjuster of insurance company, and after meeting with adjuster such adjuster agreed to pay a certain sum as damages, which sum was never paid, owner of such other vehicle was liable on such agreement in suit brought by plaintiff. Selby v. Victoria Mines, Inc., 124 M 321, 221 P2d 423 (1950), explained in Jensen v. O'Daniel, 210 F. Supp. 317 (D.C. Mont. 1962).

28-10-102. General versus special agents.

Case Notes

No Notice Imputed to Escrow Party by Knowledge of Escrow Officer: In action by bank to recover on a promissory note and set aside a conveyance of property securing payment of the note, the Supreme Court held that a third party did not have notice of an assignment of a promissory note and refused to impute such notice to him through a special agent, the escrow officer. First Fidelity Bank v. Matthews, 214 M 323, 692 P2d 1255, 41 St. Rep. 2502 (1984).

Peril of Person Dealing With Special Agent:

One dealing with a special agent without acquainting himself with the strict extent of the agent's authority and governing himself accordingly acts at his peril; he is not justified in relying upon any appearance of authority except that which is directly deductible from the nature of the authority actually conferred. Phelps v. Union Cent. Life Ins. Co., 105 M 195, 71 P2d 887 (1937), followed in Estate of Pruyn v. Axmen Propane, Inc., 2009 MT 448, 354 M 208, 223 P3d 845 (2009).

Rule that one dealing with a special agent is bound at his peril to ascertain the scope of the agent's authority applies not only to special agents employed for a single transaction but to agents who have only special authority. Barrett v. McHattie, 102 M 473, 59 P2d 794 (1936).

A person dealing with a special agent is bound at his peril to ascertain the scope of the agent's authority. Benema v. Union Cent. Life Ins. Co., 94 M 138, 21 P2d 69 (1933); NW. Elec. Equip. Co. v. Leighton, 66 M 529, 213 P 1094 (1923); Schaeffer v. Mut. Benefit Life Ins. Co., 38 M 459, 100 P 225 (1909); Moore v. Skyles, 33 M 135, 82 P 799 (1905).

If a person in negotiating for the purchase of land deals with an agent whom he knows to be a special one and makes a partial payment to him which the agent has no right to receive, after which the deal falls through, the receipt of the agent for the money is not the receipt of the principal and the payer cannot recover such payment from the principal. Schaeffer v. Mut. Benefit Life Ins. Co., 38 M 459, 100 P 225 (1909).

General Agent — Who Is: A local agent of a fire insurance company who had authority to accept risks, issue policies and cancel the same, collect premiums, and consent to assignments of policies and to a change of title on foreclosure, unrestricted or hedged about with limitations, will be held to have possessed the powers of a general agent of the insurer. Baker v. Union Assurance Soc'y of London, Ltd., 81 M 281, 264 P 132 (1928).

Special Agent — Who Is:

Where one not in the general employment of the owner of an automobile was directed by the latter to take the car to a prospective purchaser for the purpose of demonstration and then take it to the garage, he was the special agent of the owner for that and no other purpose. Susser v. Delovage, 73 M 354, 236 P 1082 (1925).

One to whom a money order was given by another, with instructions to see if it was all right, and if so, to get it cashed, was a special agent of the latter within the meaning of this section. Moore v. Skyles, 33 M 135, 82 P 799 (1905).

28-10-103. Actual versus ostensible agency — limitation.

Compiler's Comments

2023 Amendment: See 2023 Session Law for amendment made by sec. 1, Ch. 381, L. 2023. Amendment effective October 1, 2023.

2009 Amendment: Chapter 158 inserted (3)(b) providing that failure of a health care provider to require that independent professional service providers are appropriately insured constitutes unprofessional conduct; and made minor changes in style. Amendment effective April 3, 2009.

2007 Amendment: Chapter 440 in (3) inserted second sentence requiring that the insurance be in effect during the time that a medical malpractice action must be brought. Amendment effective October 1, 2007.

2005 Amendment: Chapter 44 inserted (2) and (3) limiting liability of a health care provider for the act or omission by an ostensible agent of the health care provider if the health care provider ensures that the agent has appropriate insurance; and made minor changes in style. Amendment effective July 1, 2005.

Saving Clause: Section 2, Ch. 44, L. 2005, was a saving clause.

Applicability: Section 4, Ch. 44, L. 2005, provided: "[This act] applies to malpractice claims that arise after [the effective date of this act]." Effective July 1, 2005.

Case Notes

No Evidence of Ostensible Agency in Livestock Transaction: Semenza sold cattle to Kniss, and the sale was paid through a wire transfer from Stockman's Livestock Order Buying, Inc. (Stockman's), an Oklahoma corporation. Semenza sold a second lot of cattle to Kniss and received another wire transfer from Stockman's, but the amount was $52,000 less than the price that was orally agreed on between Semenza and Kniss. Semenza brought a breach of contract action against Kniss and Stockman's, arguing that Kniss acted as Stockman's ostensible agent. The District Court found that no agency relationship existed between Kniss and Stockman's, and on appeal, the Supreme Court affirmed. The only evidence that suggested an ostensible agency was the wire transfers and Semenza's affidavit that he believed that Kniss worked for Stockman's. The evidence was insufficient to support a reasonable belief that an ostensible agency relationship existed, and the District Court did not err in so holding. Semenza v. Kniss, 2008 MT 238, 344 M 427, 189 P3d 1188 (2008).

Failure to Prove Agency — Summary Judgment on Nonliability for Constructive Discharge by Alleged Agent Improper: Plaintiff sued defendant corporation American Music Co. (AMC) for constructive discharge based on individual defendant Kelman's tortious interference with plaintiff and AMC's business relationship. Kelman founded AMC and then transferred ownership to his daughters but remained a creditor of AMC and owned the building where the business was located. Plaintiff cited numerous instances of Kelman's intimidating and threatening behavior in the office, contending that Kelman's actions and AMC's failure to control Kelman impaired plaintiff's ability to function normally at work and resulted in plaintiff's constructive discharge. Kelman moved for summary judgment on grounds that Kelman was an agent of AMC and thus was privileged from claims of tortious interference. The District Court agreed and granted summary judgment to Kelman and AMC. On appeal, the Supreme Court reversed. Kelman was not employed by AMC and thus was not an actual agent, nor did ostensible agency exist because AMC never caused any third person to believe that Kelman was an AMC agent. Absent an agency relationship between Kelman and AMC, Kelman's claimed privilege from suit failed. In addition, constructive discharge is usually a question of fact for the trier of fact to decide and is not subject to summary judgment. Plaintiff presented sufficient evidence to create a question of fact whether a reasonable person would have felt forced to resign, so the grant of summary judgment to AMC was also reversible error. Bellanger v. Am. Music Co., 2004 MT 392, 325 M 221, 104 P3d 1075 (2004).

Insufficient Notice of Employment Relationship Between Hospital and Anesthesiologist — Question of Fact Regarding Patient's Belief of Agency Relationship — Summary Judgment for Hospital Improper: Following two epidural injections for back pain by different anesthesiologists, Butler developed a spinal infection that was likely caused by one of the two injections. Subsequently, Butler filed a medical malpractice case against the two anesthesiologists and St. Patrick Hospital, alleging that each was negligent in breaching the standard of care and causing his infection by failing to provide a sterile environment prior to performing the injections. The District Court granted summary judgment in favor of St. Patrick Hospital, concluding that Butler failed to raise genuine issues of material fact as to whether the hospital intentionally or negligently led Butler to reasonably believe that one of the anesthesiologists was its employee. In reversing the District Court's ruling, the Supreme Court adopted the rationale of a Supreme Court of Indiana decision in Sword v. NKC Hosp., Inc., 714 NE 2d 142 (Ind. 1999), agreeing with its conclusion that "a hospital will be deemed to have held itself out as a provider of care unless it gives notice to the patient that it is not the provider of care and that the care is provided by a physician who is an independent contractor and not subject to the control and supervision of the hospital". In its ruling, the court cited the following three facts in Sword to be of particular relevance: (1) the record contained no evidence that would have indicated that the hospital did anything to put the patient on notice that the physician, an independent contractor, and not the hospital, was responsible for medical care; (2) the patient did not select an anesthesiologist prior to admission, and the record did not contain any evidence that would have indicated that the patient had any special knowledge with regard to the hospital's employment arrangements; and (3) the hospital held itself out as a full service hospital. Applying these factors, the court ruled that the evidence was sufficient to raise a genuine issue of material fact as to whether the hospital caused Butler to believe that the anesthesiologist who administered the injection at the hospital was its agent because Butler received no notice of the employment relationship between the anesthesiologist and St. Patrick Hospital and did not select the particular anesthesiologist to perform the procedure and because the record contained no evidence indicating that Butler did not believe that the anesthesiologist was not the hospital's employee. Butler v. Domin, 2000 MT 312, 302 M 452, 15 P3d 1189, 57 St. Rep. 1320 (2000). However, see Brookins v. Mote, 2012 MT 283, 367 Mont. 193, 292 P.3d 347, granting summary judgment to a hospital on the basis that facts clearly showed no agency or ostensible agency relationship.

Failure of Stucco Product — No Agency Relationship Between Contractor-Applicator and Manufacturer — No Negligence or Strict Liability Found — Leave to Amend Complaint Denied: Sunset Point Partnership (Sunset), a condominium developer, sued Wolstein, d/b/a Stuc-O-Flex Systems; Stuc-O-Flex International, Inc.; and Melton and Fischer, d/b/a Melton Fischer Construction (Melton/Fischer). Sunset's complaint alleged breach of contract, breach of warranty, indemnity, negligence, and strict liability in tort because a stucco-like product that Wolstein, as a subcontractor with Melton/Fischer, applied to the exterior of condominium buildings developed problems. The District Court granted summary judgment in favor of Stuc-O-Flex International, Inc., on each of the five counts in Sunset's complaint, holding that there was no evidence of negligence or breach of contract or warranty by Stuc-O-Flex International, Inc., and no evidence of agency between Stuc-O-Flex International, Inc., and Melton/Fischer. Sunset appealed. Citing previous decisions by it to the effect that in order for there to be ostensible agency the principal and not the agent must have taken steps to lead a third party to the belief that an agency relationship existed, the Supreme Court held that there was no evidence of actual or ostensible agency between Melton/Fischer and Stuc-O-Flex International, Inc., As to Sunset's claim of negligence, the Supreme Court answered Sunset's argument that Stuc-O-Flex International, Inc., was negligent in failing to provide adequate training, supervision, and instruction to Wolstein by pointing out that Sunset's complaint only alleged negligence against the defendants in the "manner in which they applied" Stuc-O-Flex and that there was no record evidence indicating a duty on the part of Stuc-O-Flex International, Inc., to train and supervise Wolstein. Concerning Sunset's claim for strict liability, the Supreme Court noted that Sunset had only alleged defective application of Stuc-O-Flex and had not alleged a defective product. Moreover, the Supreme Court pointed out that Sunset's own expert testified that: (1) there was nothing inherently defective about Stuc-O-Flex; (2) Stuc-O-Flex International, Inc., did not sell a "system" consisting of the material on which the product was applied and the product, but only sold the product itself; and (3) therefore only that product was guaranteed. In its review of the District Court's denial of Sunset's motion to amend its complaint to add the seller of the product as a defendant, the Supreme Court affirmed the District Court's decision, pointing out that the litigation was 2 years old by the time that Sunset made its untimely motion to amend. Sunset Point Partnership v. Stuc-O-Flex Int'l, Inc., 1998 MT 42, 287 M 388, 954 P2d 1156, 55 St. Rep. 141 (1998).

Insufficient Evidence:

Plaintiffs relied on Kober v. Billings Deaconess Hosp., 148 M 117, 417 P2d 476 (1966), in maintaining that the provision of office space by a small rural hospital to a radiologist who rotated between several small hospitals constituted sufficient material fact to establish an ostensible agency relationship. However, the allegations did not demonstrate intentional conduct on the part of the hospital to cause plaintiffs to believe the radiologist was an agent of the hospital, nor were there any acts amounting to want of ordinary care by the hospital to indicate an agency relationship existed. The Supreme Court distinguished Kober in affirming the trial court's grant of summary judgment based on plaintiff's failure to present sufficient evidence that would give rise to a genuine issue of material fact regarding ostensible agency. Estates of Milliron v. Francke, 243 M 200, 793 P2d 824, 47 St. Rep. 1134 (1990), following Elkins v. Husky Oil, 153 M 159, 455 P2d 329 (1969). See also Sunset Point Partnership v. Stuc-O-Flex Int'l, Inc., 1998 MT 42, 287 M 388, 954 P2d 1156, 55 St. Rep. 141 (1998). However, see Butler v. Domin, 2000 MT 312, 302 M 452, 15 P3d 1189, 57 St. Rep. 1320 (2000), distinguishing Milliron in ruling that the District Court erred in granting summary judgment to St. Patrick Hospital because testimony raised a genuine issue of material fact as to whether the hospital caused the patient to reasonably believe that the anesthesiologist was an agent of the hospital.

In a dispute over a machine lease transaction, the lessee Doll claimed that the supply company's representative, Walth, was the ostensible agent of a second company, the leasing company, Colonial Pacific. The Supreme Court ruled that there was no ostensible agency created since the undisputed record showed that neither Walth nor Colonial Pacific represented that Walth was Colonial Pacific's agent and further showed that Doll did not believe that Walth was the agent of Colonial Pacific. Doll v. Major Muffler Centers, Inc., 208 M 401, 687 P2d 48, 41 St. Rep. 429 (1984).

Pilot was not ostensible agent of aviation service where owner of plane made own arrangements with pilot and plaintiff's decedent did not rely on aviation service's responsibility, even though aviation service had introduced pilot to plane owner, had previously supplied its own employees as pilots, furnished weather information for flight plans, and organized recovery activities after plane had gone down. Calkins v. Oxbow Ranch, Inc., 159 M 120, 495 P2d 1124 (1972).

Fact that service station proprietor displayed signs advertising oil company's products and honored oil company's credit cards was not sufficient to make proprietor ostensible agent of oil company under this section or 28-10-403, and therefore oil company was not liable for injury sustained by third person on service station premises. Elkins v. Husky Oil Co., 153 M 159, 455 P2d 329 (1969). See also Sunset Point Partnership v. Stuc-O-Flex Int'l, Inc., 1998 MT 42, 287 M 388, 954 P2d 1156, 55 St. Rep. 141 (1998).

The facts that plaintiff in a letter to a bank enclosed with the deed, notes and mortgage to be executed by defendant the supplemental contract between G. and defendant, that it was delivered to him with the deed and that plaintiff did not thereafter repudiate the contract, did not under the circumstances amount to a holding out of G. as his agent so as to make it binding upon himself. Hartt v. Jahn, 59 M 173, 196 P 153 (1921).

Agency Relationship of National Realty Organization With Locally Owned Franchisee as Question of Fact: Summary judgment was improper where a genuine issue as to a material fact existed regarding home buyers' reliance on the name and reputation of a national realty organization despite an "independently owned and operated" disclaimer displayed on materials furnished by the local franchisee. Burkland v. Electronic Realty Associates, Inc., 228 M 113, 740 P2d 1142, 44 St. Rep. 1384 (1987).

Sales — Guaranty of Buyer's Payment by Guarantor's Agent: Jacobs sold the uniform sales part of his business to K&M Sports, which in turn sold it to another, who defaulted on the sale. Jacobs, as secured party, repossessed the inventory and sold it to Snick Sports. Dirkson, who worked for K&M and then Snick, told Powers that Jacobs would guarantee Snick's payment of goods sold to Snick by Powers. There was disagreement as to whether Dirkson worked for Jacobs. For 2 years Powers mailed merchandise, statements, and invoices to Jacobs, who forwarded them to Snick, who paid the bills. When some bills went unpaid, Powers sued Jacobs when he failed to pay the bills on request. The mailings to Jacobs put him on reasonable notice that something was wrong. His failure to investigate and take action was want of ordinary care that caused or allowed Powers to believe an authorized agency existed between Jacobs and Dirkson. Thus, there was an ostensible agency and ostensible authority. For the same reason, a valid guaranty existed and Jacobs was estopped from defending against it on the basis of the Statute of Frauds. A jury verdict for Powers was affirmed. Powers Mfg. Co. v. Leon Jacobs Enterprises, 216 M 407, 701 P2d 1377, 42 St. Rep. 906 (1985).

Notice of On-Job Injury Through Employer's Agent, a Physician: Employer, a hospital, in a suit to recover workers' compensation benefits may be considered to have actual notice within the meaning of 39-71-603 when claimant, a nurse in the hospital, sought and was given treatment by a physician in the emergency room. The physician is an agent under this section, and the hospital may be considered to have notice under 28-10-604. The purpose of the notice requirement is to enable the employer to protect himself by prompt investigation of the claimed accident and prompt treatment of the injury involved with a view toward minimizing its effects by proper medical care. Where, as here, within 2 hours of the accident, the employer had notice and a diagnosis and its managing agent had prescribed treatment for the injury, the purpose of 39-71-603 is fulfilled. Harmon v. Deaconess Hosp., 191 M 285, 623 P2d 1372, 38 St. Rep 65 (1981).

No Agency — Independent Contractor: The determinative question in this case was whether any type of agency relationship existed between York and Cascade Northern at the time York signed the agreement with Miller such that Miller could enforce the agreement against Cascade Northern. No actual agency existed since York was acting as an independent contractor and no ostensible agency existed since there was no act or conduct on the part of Cascade Northern holding York out as its agent. Miller v. Cascade N. Co., 181 M 66, 592 P2d 156 (1979), followed in Sunset Point Partnership v. Stuc-O-Flex Int'l, Inc., 1998 MT 42, 287 M 388, 954 P2d 1156, 55 St. Rep. 141 (1998).

Acts and Statements Establishing Agency:

Where retailer placed orders through wholesaler but received billings directly from manufacturer, and manufacturer attended sales and promotion meetings arranged by wholesaler, retailer was entitled to rely on the ostensible agency relationship between the manufacturer and the wholesaler. Butler Mfg. Co. v. J & L Implement Co., 167 M 519, 540 P2d 962 (1975), followed in Youderian Constr., Inc. v. Hall, 285 M 1, 945 P2d 909, 54 St. Rep. 1012 (1997).

Where a husband signed a letter employing an attorney and where his wife conferred with the attorney several times and approved his actions with the husband's knowledge and without his expressed disapproval, and where the husband claimed the benefits of the attorney's actions, the wife was the ostensible agent of the husband. Purcell v. Gibbs, 133 M 481, 326 P2d 679 (1958).

In an action against a bank for the conversion of plaintiff's funds deposited in a joint account in her own name and that of her daughter in wrongfully paying practically the entire account to the daughter on checks issued by the latter, evidence that plaintiff in opening the account told the bank cashier that she was placing her affairs in the daughter's hands and wished her to have complete charge of the account without requiring plaintiff's presence, attention, or signature, established the daughter's agency in any transaction had with the bank. Ludwig v. Mont. Bank & Trust Co., 109 M 477, 98 P2d 377 (1939).

Evidence that a lien claimant who performed work on defendant's building dealt with a brother of the attorney-in-fact of the owner, which brother was looking after the building either at the request of the attorney-in-fact or the owner and collected rents and endorsed rent checks received, was sufficient to sustain trial court's finding of agency, since the brother with whom the contract was made was at least the ostensible agent of the owner. Doney v. Ellison, 103 M 591, 64 P2d 348 (1937).

To constitute one an ostensible agent, the party sought to be held as principal must, by reason of some act or want of ordinary care on his part, have led the other party to believe he was his agent even though not actually employed by him. Hartt v. Jahn, 59 M 173, 196 P 153 (1921).

Course of Dealing Establishing an Ostensible Agency: Where principal's conduct led third party to believe he was dealing with an agent and third party returned merchandise to agent under such belief, principal cannot hold third party liable for cost of returned merchandise as principal led third party to believe agent had apparent authority to accept return of merchandise. Butler Mfg. v. J & L Implement Co., 167 M 519, 540 P2d 962 (1975).

Negligence: Where appellant failed to establish a case of negligence against the supposed agent, it would be impossible to impute negligence to the principal. Knowlton v. Sandaker, 150 M 438, 436 P2d 98 (1968).

Service Upon Corporation — Proper Agent: The doctrine of ostensible agency appears to have no application when it becomes involved with the question whether service of process has been legally made upon a "managing or general agent". Further, service upon a former employee of a company was not service upon the company itself and default judgment was vacated and set aside. Kraus v. Treasure Belt Min. Co., 146 M 432, 408 P2d 151 (1965).

Acquiescence in Agency: Where a hotel company had acted as a ski lift company's agent in managing the latter's business, and where the hotel company's principal stockholder had later taken possession of and controlled the ski lift company's office and principal place of business for 2 years, the principal stockholder was the agent of the ski lift company in negotiating an employment contract, and this was further confirmed when the stockholder engaged counsel to defend the ski lift company in the instant litigation. Hamilton v. Lion Head Ski Lift, Inc., 139 M 335, 363 P2d 716 (1961), explained in Kraus v. Treasure Belt Min. Co., 146 M 432, 408 P2d 151 (1965).

Burden of Proof: Where plaintiff in his complaint contended that there was a partnership, he assumed the burden of establishing that there was one in fact, or that the partners had permitted themselves to be represented as such to him and that on the faith of such representations, he had given the credit to the partnership. Hempstead v. Allen, 126 M 578, 255 P2d 342 (1953).

Ratification: In an action to recover oil well driller's wages, and on an assigned claim for supplies furnished at the instance and request of an employee of the operator, evidence held to have warranted a judgment for plaintiff on theory that the persons at whose instance the claims were incurred were agents of defendant operator whose acts the latter had ratified with knowledge of the facts resulting in the claims. Stoican v. Withers, 104 M 173, 65 P2d 604 (1937).

Agency Implied: Agency may be implied from conduct and from all the facts and circumstances in the case and may be shown by circumstantial evidence. Also ratification may be implied from the acts and conduct of the alleged principal. Freeman v. Withers, 104 M 166, 65 P2d 601 (1937).

Estoppel: Where one to whom another is indebted by want of ordinary care causes the debtor to believe that a third person is his agent for the purpose of receiving payment, such latter is the ostensible agent of the creditor, and payment having been received by the agent, the principal is estopped to disavow it. Millious v. Thompson, 94 M 110, 20 P2d 1060 (1933).

28-10-104. Who may appoint an agent, who may be an agent.

Case Notes

Workers' Compensation — Disaffirmation of Settlement Agreement by Minor: A minor was injured while working and filed for workers' compensation benefits. He subsequently signed a settlement agreement after negotiating with a claims adjuster. The claimant's filing of a petition to reopen his claim resulted in a hearing and the conclusion that the case was closed. The claimant appealed, based on his minority status at the time of the settlement and his concomitant right to disaffirm contracts. The Supreme Court held that the close relationship and continuing awareness of the claimant's mother during the claims negotiations were of no avail to the defendants because only the minor claimant had signed the settlement. The defendant should have required the claimant's legal guardian to sign as well as the claimant. Accordingly, the final compromise settlement was set aside. Parrent v. Midway Toyota, 192 M 118, 626 P2d 848, 38 St. Rep. 559 (1981).

Agency — Parents' Neglect to Give Notice Not Imputable to Child — Child Incapable of Appointing Agent: Neglect of parents of injured child to give 60-day notice provided for by Ch. 122, L. 1937, may not be imputed to the child, and since under this section a child is incapable of appointing an agent for any purpose, it is questionable whether the statute can be complied with in that respect by anyone as agent. Child's cause of action for personal injuries is a property right over which under 40-6-232 a parent has no control. Lazich v. Belanger, 111 M 48, 105 P2d 738 (1940).

28-10-105. What acts agent may perform.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Transfer of Property for Creation of Trust Not Included in General Power of Attorney: Jameison appointed her granddaughter, Bolich, as "true and lawful attorney", granting her authority to generally act in Jameison's stead "in all matters affecting my business or property". Bolich created a trust agreement naming Jameison the income beneficiary for life and Bolich as trustee and designating Jameison's two daughters as income beneficiaries during their lives in the event that they survived Jameison. The trust agreement provided for distribution of the trust principal for the health, maintenance, and welfare of the income beneficiaries at the trustee's discretion, and upon the death of the last income beneficiary, the trust was to dissolve, with the remainder distributed to Bolich or her estate. Bolich then conveyed all of Jameison's real property, including over 30 parcels, and personal property, including several certificates of deposit and promissory notes, to herself. Jameison died a few months later, and one daughter died shortly thereafter. Over 7 years later, Bolich distributed $100 in trust income to the remaining daughter, who was unhappy with the accounting and challenged the validity of the trust agreement, moving for summary judgment on grounds that Bolich did not have authority under the power of attorney to create it, citing a lack of evidence of Jameison's intent to create the trust and the fact that the trust agreement and conveyance documents were signed solely by Bolich and not by Jameison. The District Court found that Bolich's assertions regarding Jameison's intent were purely speculative and that Bolich had failed to produce any evidence that Jameison had intended to create the trust. The court concluded that the general power of attorney did not specifically authorize Bolich to create the trust and that Bolich exceeded her authority in doing so. The trust was invalidated and terminated, and the estate was distributed pursuant to the laws of intestacy. Bolich appealed. The Supreme Court affirmed. In this case, the power of attorney was broad and general but did not grant authority to create a trust, reflect Jameison's intent to create a trust, or even mention a trust, so Bolich's transfer of Jameison's property to herself as trustee was not warranted by the terms actually used in the power of attorney or as a means of executing other authority. The trust was not created by one of the methods in 72-33-201 (now repealed) and was invalid. Bolich's argument that the trust was ratified pursuant to 28-10-211 by Jameison's oral authorization also failed because ratification of a trust must be accomplished in writing pursuant to 72-33-208 (now repealed). Absent material facts regarding the validity of the trust, summary judgment invalidating the trust was proper. In re Trust of Jameison v. Bolich, 2000 MT 190, 300 M 418, 8 P3d 83, 57 St. Rep. 753 (2000), distinguishing McLaren Gold Mines Co. v. Morton, 124 M 382, 224 P2d 975 (1951).

Part 2
Creation of Agency

Part Case Notes

Lack of Agency as Negative Defense: Lack of agency is a negative rather than affirmative defense. Sterrett v. Milk River Prod. Credit Ass'n, 234 M 459, 764 P2d 467, 45 St. Rep. 2048 (1988), following Porto v. Peden, 233 F. Supp. 178 (W.D. Pa. 1964). See also Grimsley v. Estate of Spencer, 206 M 184, 670 P2d 85 (1983).

No Agency Created by Supervision of Federal Intermediate Credit Bank Over Production Credit Association: Under 12 U.S.C. 2012(13) and 2072(15) and in accord with Fed. Deposit Ins. Corp. v. Langley, 792 F2d 547 (5th Cir. 1986), the regulatory function exercised by a federal intermediate credit bank over a production credit association creates no agency relationship. The separate corporate nature of the entities under their enabling statutes and the separate functions of the organizations mandate this conclusion. Sterrett v. Milk River Prod. Credit Ass'n, 234 M 459, 764 P2d 467, 45 St. Rep. 2048 (1988).

County Not Acting as State's Agent in Denial of Disposal Permit — Mandamus Erroneously Granted: Where the plaintiff applied to the county health department for a disposal permit but was not informed for a period of 6 years whether the permit would be granted, the District Court erred in holding that the Department of Health and Environmental Sciences (now Department of Environmental Quality) was estopped from denying the permit by the county's failure to act. There were no statutes or decisions that made the county the agent of the Department at the time of the 1971 permit application. Under the rationale of St. v. District Court, 170 M 15, 550 P2d 382 (1976), the record and statutes show that the county did not act as an agent for the state in the denial of the 1971 application. Huttinga v. Pringle, 205 M 482, 668 P2d 1068, 40 St. Rep. 1444 (1983).

28-10-201. How agency may be created.

Case Notes

Ratification of Void Deeds — Authority of Agent to Convey Property — Title Properly Quieted: Defendant third party raised three challenges to a District Court's conclusion that deeds voided by forgery during transfer were nevertheless ratified by subsequent actions of the parties and contended that the court erred by quieting title to plaintiff. The first argument dealt with the fact that one of the parties never received proper written authority to convey the property to plaintiff, so ratification was voided under the statute of frauds. The Supreme Court noted that an agreement to sell an interest in property must be in writing and that an agent's authority to sell property must also be in writing. However, the agency relationship may arise either by precedent authorization or by subsequent ratification. In this case, the warranty deeds constituted subsequent written authority for conveyance of the property, so the statute of frauds was not violated for want of written authorization. The second argument was that the criteria for ratification were not satisfied, but after examining the chain of title, the Supreme Court found that the personal actions of the principal ratified the deed and that the criteria for ratification were satisfied. The third argument was that defendant was prejudiced as a third party by ratification, but that argument did not prevail because defendant could not have been prejudiced since defendant's interest in the property was invalid both prior to and after ratification and defendant could have become aware of the void deeds by conducting a title check and avoiding the problem. Lastly, title was properly quieted in plaintiff because defendants with prior interests in the property stipulated that they no longer claimed any right, title, or interest in the property. Plaintiff's deed was superior because it was the first to be recorded and had been ratified, and plaintiff was therefore entitled to have quiet title to the property. The District Court was affirmed. Erler v. Creative Fin. & Inv., LLC, 2009 MT 36, 349 M 207, 203 P3d 744 (2009). See also U.S. v. Heinszen, 206 US 370 (1907), Audit Serv., Inc. v. Francis Tindall Constr., 183 M 474, 600 P2d 811 (1979), Safeco Ins. Co. v. Lovely Agency, 200 M 447, 652 P2d 1160 (1982), and Moore v. Adolph, 242 M 221, 789 P2d 1239 (1990).

Breach of Contract Action for Failure to Properly Embalm Deceased — Agency — Standing to Sue: Maria handled all funeral arrangements for her deceased mother. The family of the deceased, when viewing the body, observed a stain on the clothing that was determined to be caused by leaking embalming fluid. The lower court dismissed the family's claim for breach of contract and also ruled that Maria was not acting as agent for the other family members and that only she would have been able to sue for breach of contract. The Supreme Court held that a cause of action for breach of contract would exist if Maria could show that the breach had so "damaged" the funeral as to constitute a breach of contract entitling Maria to damages. The Supreme Court did affirm the lower court's ruling that Maria was not acting as an agent for the rest of the family in contracting with the mortuary. Therefore, only she could sue on the contract. Contreraz v. Michelotti-Sawyers & Nordquist Mortuary, Inc., 271 M 300, 896 P2d 1118, 52 St. Rep. 454 (1995).

Agency Question of Fact: In a zoning variance controversy, plaintiffs claimed a city-county planning board and city board of adjustments granted the variance without proper notice, without a hearing, and without considering legal requirements. The District Court dismissed the claim as to defendant and granted summary judgment. The Supreme Court reversed, saying the plaintiff may be able to show the planning board is directly liable to plaintiffs because of its acts through its agent. Borrowing on California precedent, the court held that allegations of agency are questions of fact and should not be decided on a motion for summary judgment. The court noted that in dealing with government entities this is not always true because a principal cannot delegate authority it does not possess. This can be determined by establishing the authority which, as a matter of public record, citizens are charged with knowing. The court also noted that while a government principal's authority may be limited by law, the principal may exceed that authority in its day-to-day activity, thereby existing in fact although precluded by law. The dismissal and summary judgment were reversed. Stillman v. Fergus County, 220 M 315, 715 P2d 43, 43 St. Rep. 396 (1986), followed in Sterrett v. Milk River Prod. Credit Ass'n, 234 M 459, 764 P2d 467, 45 St. Rep. 2048 (1988).

How Authority of Agent to Be Established:

An agency relationship is created only if a purported agent claims to be acting on behalf of a ratifying principal. In a suit involving a lease of machinery, the record was devoid of any claim or understanding by either the lessee or the supplier's representative that the supplier's representative was the agent of a second company, the leasing company. Doll v. Major Muffler Centers, Inc., 208 M 401, 687 P2d 48, 41 St. Rep. 429 (1984).

The authority of an agent and its nature and extent can only be established by tracing it to its source in some word or act of the alleged principal; the agent cannot confer authority upon himself. The relationship of principal and agent cannot be established by the declarations of the agent. Fed. Land Bank of Spokane v. Myhre, 110 M 416, 101 P2d 1017 (1940).

Agency may be created by precedent authorization or subsequent ratification and may be implied from conduct and shown by circumstantial evidence. Ratification may likewise be implied from the acts and conduct of the alleged principal. Freeman v. Withers, 104 M 166, 65 P2d 601 (1937).

Ratification by Payment: Defendant's voluntary contributions to union trust funds ratified the corporate general manager's act of signing the collective bargaining compliance agreements requiring contribution. Audit Serv., Inc. v. Elmo Road Corp., 175 M 533, 575 P2d 77 (1978).

Joint Checking Account: The plaintiff had her daughter look after her business affairs. The plaintiff, by opening a joint account and telling a bank officer she was placing her affairs in her daughter's hands, created an agency relationship. An agency such as that involved here may be granted orally or may be implied from the words and conduct of the parties and the circumstances of the particular case, notwithstanding a later denial by the alleged principal. Ludwig v. Mont. Bank & Trust Co., 109 M 477, 98 P2d 377 (1939).

How Agency Established — Lone Man Apparently in Charge of Elevator: Testimony of a bank cashier that one claimed by the bank in its action for the conversion of mortgaged grain to have been the agent of defendant elevator company was the only man at the elevator when he had an interview with him and that such person was running the elevator and went over the books of the concern with him, together with testimony of a Sheriff stating that such person was apparently in charge, has been held sufficient to establish agency. Exchange St. Bank v. Occident Elev. Co., 95 M 78, 24 P2d 126 (1933).

Attorney as Agent for Client: The rules of law applicable to principal and agent are in general applicable to the relation of attorney and client. An attorney is but the agent of his client for the management and conduct of such matters as are entrusted to him, and if he acts within the scope of his authority the client is bound. Bury v. Bury, 69 M 570, 223 P 502 (1924).

Fraudulent Purpose: An agreement between applicants for public lands, made by one of the parties for his wife and ratified by her, the purpose of the agreement being to stifle competition in bidding, is a fraud on the state and is not enforceable. State ex rel. Danaher v. Miller, 52 M 562, 160 P 513 (1916).

28-10-202. Consideration unnecessary.

Case Notes

Consent Necessary: Agency is founded upon consent, not consideration. St. v. Erlandson, 126 M 316, 249 P2d 794 (1952).

28-10-203. When written authorization necessary.

Case Notes

General Power of Attorney — Authority to Transfer Funds by and to Holder of Power of Attorney Within Scope: The decedent was diagnosed with cancer and given a month to live. A month later, he was admitted to the hospital, where he signed a general durable power of attorney authorizing his longtime companion. She later transferred funds from his bank account to her own account pursuant to the decedent's wishes. The decedent's brother filed suit and argued that the transfers were for her own personal benefit, and therefore she exceeded the authority granted to her in the power of attorney. At trial, however, the District Court examined the plain language of the power of attorney, which did not prohibit or limit the companion's authority to make the transfers of funds, and ruled in her favor. On appeal, the Supreme Court affirmed. In re Estate of Cook, 2020 MT 240, 401 Mont. 374, 472 P.3d 1179.

Ratification of Void Deeds — Authority of Agent to Convey Property — Title Properly Quieted: Defendant third party raised three challenges to a District Court's conclusion that deeds voided by forgery during transfer were nevertheless ratified by subsequent actions of the parties and contended that the court erred by quieting title to plaintiff. The first argument dealt with the fact that one of the parties never received proper written authority to convey the property to plaintiff, so ratification was voided under the statute of frauds. The Supreme Court noted that an agreement to sell an interest in property must be in writing and that an agent's authority to sell property must also be in writing. However, the agency relationship may arise either by precedent authorization or by subsequent ratification. In this case, the warranty deeds constituted subsequent written authority for conveyance of the property, so the statute of frauds was not violated for want of written authorization. The second argument was that the criteria for ratification were not satisfied, but after examining the chain of title, the Supreme Court found that the personal actions of the principal ratified the deed and that the criteria for ratification were satisfied. The third argument was that defendant was prejudiced as a third party by ratification, but that argument did not prevail because defendant could not have been prejudiced since defendant's interest in the property was invalid both prior to and after ratification and defendant could have become aware of the void deeds by conducting a title check and avoiding the problem. Lastly, title was properly quieted in plaintiff because defendants with prior interests in the property stipulated that they no longer claimed any right, title, or interest in the property. Plaintiff's deed was superior because it was the first to be recorded and had been ratified, and plaintiff was therefore entitled to have quiet title to the property. The District Court was affirmed. Erler v. Creative Fin. & Inv., LLC, 2009 MT 36, 349 M 207, 203 P3d 744 (2009). See also U.S. v. Heinszen, 206 US 370 (1907), Audit Serv., Inc. v. Francis Tindall Constr., 183 M 474, 600 P2d 811 (1979), Safeco Ins. Co. v. Lovely Agency, 200 M 447, 652 P2d 1160 (1982), and Moore v. Adolph, 242 M 221, 789 P2d 1239 (1990).

Transfer of Property for Creation of Trust Not Included in General Power of Attorney: Jameison appointed her granddaughter, Bolich, as "true and lawful attorney", granting her authority to generally act in Jameison's stead "in all matters affecting my business or property". Bolich created a trust agreement naming Jameison the income beneficiary for life and Bolich as trustee and designating Jameison's two daughters as income beneficiaries during their lives in the event that they survived Jameison. The trust agreement provided for distribution of the trust principal for the health, maintenance, and welfare of the income beneficiaries at the trustee's discretion, and upon the death of the last income beneficiary, the trust was to dissolve, with the remainder distributed to Bolich or her estate. Bolich then conveyed all of Jameison's real property, including over 30 parcels, and personal property, including several certificates of deposit and promissory notes, to herself. Jameison died a few months later, and one daughter died shortly thereafter. Over 7 years later, Bolich distributed $100 in trust income to the remaining daughter, who was unhappy with the accounting and challenged the validity of the trust agreement, moving for summary judgment on grounds that Bolich did not have authority under the power of attorney to create it, citing a lack of evidence of Jameison's intent to create the trust and the fact that the trust agreement and conveyance documents were signed solely by Bolich and not by Jameison. The District Court found that Bolich's assertions regarding Jameison's intent were purely speculative and that Bolich had failed to produce any evidence that Jameison had intended to create the trust. The court concluded that the general power of attorney did not specifically authorize Bolich to create the trust and that Bolich exceeded her authority in doing so. The trust was invalidated and terminated, and the estate was distributed pursuant to the laws of intestacy. Bolich appealed. The Supreme Court affirmed. In this case, the power of attorney was broad and general but did not grant authority to create a trust, reflect Jameison's intent to create a trust, or even mention a trust, so Bolich's transfer of Jameison's property to herself as trustee was not warranted by the terms actually used in the power of attorney or as a means of executing other authority. The trust was not created by one of the methods in 72-33-201 (now repealed) and was invalid. Bolich's argument that the trust was ratified pursuant to 28-10-211 by Jameison's oral authorization also failed because ratification of a trust must be accomplished in writing pursuant to 72-33-208 (now repealed). Absent material facts regarding the validity of the trust, summary judgment invalidating the trust was proper. In re Trust of Jameison v. Bolich, 2000 MT 190, 300 M 418, 8 P3d 83, 57 St. Rep. 753 (2000), distinguishing McLaren Gold Mines Co. v. Morton, 124 M 382, 224 P2d 975 (1951).

Agency and Ratification to Be in Writing: The plaintiffs initiated a suit to have certain water rights distributed pursuant to the residuary clause of a will. The defendant argued that the rights had previously been assigned to him by a release that he signed as agent of the deceased and that the deceased had subsequently orally affirmed. The Supreme Court held that the original release had to be in writing because it called for payments for 32 years and therefore was subject to the statute of frauds. The court went on to hold that since the release had to be in writing, then the creation of an agency and the subsequent ratification also had to be in writing and that since they were not, the water rights passed under the will. Moore v. Adolph, 242 M 221, 789 P2d 1239, 47 St. Rep. 730 (1990).

Unenforceable Timber Sale by Agent Without Written Authority: Gebert Logging contracted in writing with Palin to remove timber from certain land. This was a contract under 30-2-107 of the U.C.C. for goods to be severed from realty. The contract price was over $500, so under 30-2-201 of the U.C.C., the contract had to be in writing. Under 28-10-203 relating to agency, authority to enter into a contract that the law requires to be written can only be given by an instrument that is itself written. Since Palin did not own the land and did not have written authority from his wife, the owner, to execute the contract as her agent, the contract was unenforceable because it was not signed by or with the written authority of the owner of the land. Gebert Logging was thus entitled to receive back its land damage bond, and Palin was not entitled to damages for alleged unrepaired injury to the land. The court denied Palin's claims that part performance took the contract out of the Statute of Frauds and that the contract should not be invalidated because he had altered his position to his detriment. The court also held that his wife could not retroactively ratify his acts without the consent of Gebert Logging, which was not given. Gebert Logging, Inc. v. Palin, 220 M 405, 716 P2d 200, 43 St. Rep. 481 (1986).

Sales — Guaranty of Buyer's Payment by Guarantor's Agent: Jacobs sold the uniform sales part of his business to K&M Sports, which in turn sold it to another, who defaulted on the sale. Jacobs, as secured party, repossessed the inventory and sold it to Snick Sports. Dirkson, who worked for K&M and then Snick, told Powers that Jacobs would guarantee Snick's payment of goods sold to Snick by Powers. There was disagreement as to whether Dirkson worked for Jacobs. For 2 years Powers mailed merchandise, statements, and invoices to Jacobs, who forwarded them to Snick, who paid the bills. When some bills went unpaid, Powers sued Jacobs when he failed to pay the bills on request. The mailings to Jacobs put him on reasonable notice that something was wrong. His failure to investigate and take action was want of ordinary care that caused or allowed Powers to believe an authorized agency existed between Jacobs and Dirkson. Thus, there was an ostensible agency and ostensible authority. For the same reason, a valid guaranty existed and Jacobs was estopped from defending against it on the basis of the Statute of Frauds. A jury verdict for Powers was affirmed. Powers Mfg. Co. v. Leon Jacobs Enterprises, 216 M 407, 701 P2d 1377, 42 St. Rep. 906 (1985).

Realtor Buying Property — Not Usual Course of Business: As part of a real estate transaction in which the buyers needed to sell a piece of property in order to purchase other property, the realtor acting on behalf of the buyers executed a memorandum stating that if the property was not sold by a set time, she would purchase the property at a stated price. The memorandum was not signed by the realtor's alleged partner. On appeal, he contended he could not be bound by the memorandum under the Statute of Frauds. The Supreme Court held that the realtor could not bind her ostensible partner since there was no written authority of agency and because the purchase of real estate was not the realtor's usual way of doing business. The alleged partner could not be bound to the contract evidenced by the memo absent his authorization thereunto in writing. McNabb v. Norine, 204 M 330, 664 P2d 927, 40 St. Rep. 878 (1983).

Breach of Contractual Warranties — Proper Parties — Statute of Frauds: Plaintiffs in an action for breach of express and implied warranties were farmers. Defendants manufactured farm implements. One of the plaintiffs had an arm severed in an accident involving the defendants' machinery. On appeal, the defendants argued that the injured plaintiff was not a party to the purchase contract. The plaintiff alleged the salesman knew that he and the party who actually signed the purchase order were to be co-owners of the hay baler in question. The signature was for the one co-owner for himself and as agent for the plaintiff as well. Because principal and agent law supplement the Montana U.C.C., which covers the purchase of the baler, the court considered applying this section, which prevents oral authorization to contract when the contract itself must be written, as here. It noted exceptions to the Statute of Frauds, however. The question of whether payment of the purchase price took this contract out of the Statute of Frauds was a genuine issue of material fact preventing a summary judgment for the defendants under the Federal Rules of Civil Procedure. Holding the question one of law, the court said it had to hold an evidentiary hearing on the issues. Schlenz v. John Deere Co., 511 F. Supp. 224, 38 St. Rep. 579 (D.C. Mont. 1981).

Power of Attorney: A power of attorney is nothing more than an instrument in writing authorizing another to act as one's agent. The intention of the parties as it existed at the time of granting the power of attorney is to be ascertained from the writing alone, if possible, and that intention is to be given effect. McLaren Gold Mines v. Morton, 124 M 382, 224 P2d 975 (1950).

Authority Granted Orally or Implied From Words and Conduct: Where mother opened joint bank account in both her own and daughter's names and told the cashier she was placing her affairs in the daughter's hands and wished her to have complete charge of the account without requiring the mother's presence, attention, or signature, the mother established the daughter's agency, under the rule that such authority may be granted orally or implied from the words and conduct of the parties and the circumstances of the particular case though denied by the alleged principal under this section. Ludwig v. Mont. Bank & Trust Co., 109 M 477, 98 P2d 377 (1939).

Corporation Agent Acting Without Written Authorization:
To make the rule that a corporation may be bound by an act of its agent in entering into a written contract not to be performed within 1 year without specific written authority on the part of the agent to act, required by this section, applicable, the evidence must show that such agent was the managing official of the corporation or that it had theretofore ratified the agent's acts in similar transactions. Elec. Prod. Consol. v. El Campo, Inc., 105 M 386, 73 P2d 199 (1937).

In an action for breach of a written contract entered into between an agent of defendant corporation and plaintiff, running over 3 years where agent's authority was not in writing as required by this section, it was held that trial court erred in directing a verdict for plaintiff in the absence of such written authority, the record, on the contrary, disclosing that the management of the corporation was vested in the board of directors—ratification or estoppel not entering into the case. Elec. Prod. Consol. v. El Campo, Inc., 105 M 386, 73 P2d 199 (1937).

Contract to Sell Land: The authority of an agent to contract to sell land before the adoption of this section was not required to be in writing, and could be shown by oral testimony, or any evidence tending to prove agency. Cobban v. Hecklen, 27 M 245, 70 P 805 (1902).

28-10-211. How agent's act ratified.

Case Notes

Implicit Ratification — Effect of Acquiescence: Implicit ratification is usually shown where the principal voluntarily recognizes an act of an agent as binding and proceeds to perform the obligations imposed by that act. When a principal with knowledge of the material facts voluntarily continued performing on a contract that had been entered into by an agent, the Supreme Court noted that this was presumptive proof of ratification considering that the principal's subsequent performance and payment were inconsistent with any other intention. Assoc. Management Serv., Inc. v. Ruff, 2018 MT 182, 392 Mont. 139, 424 P.3d 571.

Ratification of Forged Deed Considered in Equity: Commercial property in Hamilton was transferred to multiple parties in successive transactions, resulting in competing claims to the property. Some of the transactions involved fraud or forgery. Plaintiff filed a complaint against numerous parties that were involved in the transactions and sought to quiet title to the property. The District Court concluded that the documents of conveyance to three of the parties were forged and therefore void ab initio and that no rights were transferred to any of those parties. The court found that two of the parties had ratified the forged conveyances by their subsequent actions and that because plaintiff was the first to record a document of transfer, plaintiff was entitled to quiet title. One defendant appealed on grounds that a forged deed cannot be ratified, but the Supreme Court affirmed. A forged deed is void and transfers no rights, even if the subsequent purchaser is bona fide. Thus, the three deeds were void ab initio and plaintiff's interest in the property was not saved by 70-20-404, even though plaintiff parted with value, had no notice of the forgery, and duly recorded the appropriate transfer documents. However, in order to provide a legal remedy in the appropriate case, principles of equity and justice compel recognition of ratification, so a forged deed may be considered in equity. Erler v. Creative Fin. & Inv., LLC, 2009 MT 36, 349 M 207, 203 P3d 744 (2009), distinguishing Hames v. Polson, 123 M 469, 215 P2d 950 (1950), and In re Estate of Griffin, 248 M 472, 812 P2d 1256 (1991).

Transfer of Property for Creation of Trust Not Included in General Power of Attorney: Jameison appointed her granddaughter, Bolich, as "true and lawful attorney", granting her authority to generally act in Jameison's stead "in all matters affecting my business or property". Bolich created a trust agreement naming Jameison the income beneficiary for life and Bolich as trustee and designating Jameison's two daughters as income beneficiaries during their lives in the event that they survived Jameison. The trust agreement provided for distribution of the trust principal for the health, maintenance, and welfare of the income beneficiaries at the trustee's discretion, and upon the death of the last income beneficiary, the trust was to dissolve, with the remainder distributed to Bolich or her estate. Bolich then conveyed all of Jameison's real property, including over 30 parcels, and personal property, including several certificates of deposit and promissory notes, to herself. Jameison died a few months later, and one daughter died shortly thereafter. Over 7 years later, Bolich distributed $100 in trust income to the remaining daughter, who was unhappy with the accounting and challenged the validity of the trust agreement, moving for summary judgment on grounds that Bolich did not have authority under the power of attorney to create it, citing a lack of evidence of Jameison's intent to create the trust and the fact that the trust agreement and conveyance documents were signed solely by Bolich and not by Jameison. The District Court found that Bolich's assertions regarding Jameison's intent were purely speculative and that Bolich had failed to produce any evidence that Jameison had intended to create the trust. The court concluded that the general power of attorney did not specifically authorize Bolich to create the trust and that Bolich exceeded her authority in doing so. The trust was invalidated and terminated, and the estate was distributed pursuant to the laws of intestacy. Bolich appealed. The Supreme Court affirmed. In this case, the power of attorney was broad and general but did not grant authority to create a trust, reflect Jameison's intent to create a trust, or even mention a trust, so Bolich's transfer of Jameison's property to herself as trustee was not warranted by the terms actually used in the power of attorney or as a means of executing other authority. The trust was not created by one of the methods in 72-33-201 (now repealed) and was invalid. Bolich's argument that the trust was ratified pursuant to this section by Jameison's oral authorization also failed because ratification of a trust must be accomplished in writing pursuant to 72-33-208 (now repealed). Absent material facts regarding the validity of the trust, summary judgment invalidating the trust was proper. In re Trust of Jameison v. Bolich, 2000 MT 190, 300 M 418, 8 P3d 83, 57 St. Rep. 753 (2000), distinguishing McLaren Gold Mines Co. v. Morton, 124 M 382, 224 P2d 975 (1951).

Principal Estopped From Denying Agency Relationship Because of Ratification of Ostensible Agent's Actions by Retention of Benefit of Third Party's Act: Hall argued that he did not have to pay for a road constructed by Youderian at Hill's direction because Hill was not his agent. The Supreme Court stated that Youderian had acted reasonably in assuming that Hill was Hall's agent based upon prior dealings among the three parties. The Supreme Court held that as a matter of law, an agency relationship had been created because Hall had ratified Hill's employment of Youderian by retaining the benefit of the improved road and that therefore Hall was estopped from denying Hill's ostensible authority. Youderian Constr., Inc. v. Hall, 285 M 1, 945 P2d 909, 54 St. Rep. 1012 (1997).

Agency and Ratification to Be in Writing: The plaintiffs initiated a suit to have certain water rights distributed pursuant to the residuary clause of a will. The defendant argued that the rights had previously been assigned to him by a release that he signed as agent of the deceased and that the deceased had subsequently orally affirmed. The Supreme Court held that the original release had to be in writing because it called for payments for 32 years and therefore was subject to the statute of frauds. The court went on to hold that since the release had to be in writing, then the creation of an agency and the subsequent ratification also had to be in writing and that since they were not, the water rights passed under the will. Moore v. Adolph, 242 M 221, 789 P2d 1239, 47 St. Rep. 730 (1990).

Contract for Deed — Notifying Escrow Agent of Default: Seller under contract for deed did not have to notify the escrow agent as well as the buyers that payments were in default and the contract was terminated, because the contract only provided for notice to buyers and did not require notice to the escrow agent. More important, the contract gave buyers the right to pay the accelerated balance due within 90 days of receipt of the notice of default, the deed and other documents were held by and the payments were made to the escrow agent, and notice of default to the escrow agent would have prematurely closed the escrow account and denied the buyers the opportunity to pay off the contract within 90 days. Boles v. Ler, 222 M 28, 719 P2d 793, 43 St. Rep. 1035 (1986).

Contract for Deed — Seller's Right to Cancel After Accepting Late Payments to Escrow Agent: Buyers under contract for deed made three late payments to the escrow agent. The escrow agent's acceptance of the three checks was not acceptance by the seller under the theory that the escrow agent was the seller's agent and acceptance by the agent was acceptance by the principal, nor did seller's acceptance of the payments from the escrow agent ratify the agent's acceptance. Failure to promptly return the payments did not waive seller's right to cancel the contract. The contract gave buyers 90 days from notice of default to pay the balance due under the contract, and they could do so in more than one installment. Seller decided the three payments might be installments in an attempt to pay the balance due and decided to hold the checks until it became apparent that the buyers were either going to pay off the balance due or were attempting to induce seller to waive her right to cancel the contract. Seller returned the checks when she realized the latter was the motive. In addition, seller sent a second cancellation notice, making it clear what her intent was. Boles v. Ler, 222 M 28, 719 P2d 793, 43 St. Rep. 1035 (1986).

Attorney as Agent: Under the rulings of McGinley v. Md. Cas. of Baltimore, 85 M 1, 277 P 414 (1929), and Harris v. Root, 28 M 159, 72 P 429 (1903), appellant's knowledge of the terms of a settlement agreement and his acquiescence in the agreement for a period of nearly 2 years constitutes a ratification of the settlement. Webb v. First Nat'l Bank of Hinsdale, 219 M 160, 711 P2d 1352, 42 St. Rep. 1919 (1985).

Elements of Ratification: Ratification exists upon the concurrence of three elements: (1) acceptance by the principal of the benefit of the agent's act; (2) full knowledge of the facts; and (3) circumstances or an affirmative election indicating an intention to adopt the unauthorized arrangement. Safeco Ins. Co. v. Lovely Agency, 200 M 447, 652 P2d 1160, 39 St. Rep. 1861 (1982), followed in Daniels v. Dean, 253 M 465, 833 P2d 1078, 49 St. Rep. 535 (1992), and in Erler v. Creative Fin. & Inv., LLC, 2009 MT 36, 349 M 207, 203 P3d 744 (2009).

Estopped From Applying Section: Where defendant's wife signed an agreement with the plaintiff concerning property covered by the Statute of Frauds and the defendant did not ratify the agreement in writing, he cannot rely on this section to avoid the agreement for equitable reasons in that the plaintiff made an irretrievable change in position or the defendant secured an unconscionable advantage or inflicted an unjust and unconscionable loss upon the plaintiff. Bolz v. Myers, 200 M 286, 651 P2d 606, 39 St. Rep. 1747 (1982).

Alleged Agent Taking No Action: When an alleged agent takes no action, there is nothing that can be ratified. Schulz v. Peake, 178 M 261, 583 P2d 425 (1978).

Ratification by Payment: Defendant's voluntary contributions to union trust funds ratified the corporate general manager's act of signing the collective bargaining compliance agreements requiring contribution. Audit Serv., Inc. v. Elmo Road Corp., 175 M 533, 575 P2d 77 (1978).

Sale of State Property by Employee — No Ratification: Ratification does not result from affirmance by alleged principal of a transaction had by an alleged agent with a third person unless the supposed agent purported to act on account of the reputed principal. Thus where an employee of the State Park Commission neither sold nor purported to sell a state road roller in the name of the state as principal or by himself as agent, the state did not ratify the sale, because the Attorney General had sued the employee and demanded that he account for the disposal of the roller as well as the proceeds and profits from the sale. State ex rel. Olsen v. Sundling, 128 M 596, 281 P2d 499 (1955).

Acceptance by Principal of Results of Act:

A conviction may be had of the owner of a tavern for the sale of beer to a minor although such sale was made by a barmaid who was not on the defendant's payroll but acted at times as bartender when the manager was gone. The owner by her silence and by accepting and retaining the benefits of the sales by the barmaid whom she knew was acting as a substitute bartender for her manager did ratify said acts. St. v. Erlandson, 126 M 316, 249 P2d 794 (1952).

Where a principal accepts a contract made by his agent he takes it as the agent made it and subject to all equities and defenses arising out of the conditions thereof, and the means and instrumentalities by which the agent procured it, even though the agent acted without authority or in excess of his powers. Bell v. Grimstad, 82 M 185, 266 P 394 (1928).

A principal who with knowledge accepts the benefits of a transaction conducted by an assumed agent is deemed to have ratified it in toto. Bell v. Grimstad, 82 M 185, 266 P 394 (1928).

Before a principal may be said to have ratified an unauthorized act of his agent, it must be shown that the former accepted the results of the act of the latter with the intent to ratify and with full knowledge of all the material circumstances. Outlook Farmers' Elev. Co. v. Am. Sur. Co., 70 M 8, 233 P 905 (1924). See also Renland v. First Nat'l Bank, 90 M 424, 4 P2d 488 (1931).

To constitute ratification of an agent's act there must be an acceptance by the principal of the results of the act with an intent to ratify and with full knowledge of all the material circumstances. Pew v. McLeish, 62 M 437, 205 P 235 (1922).

Disavowal of Agent's Acts: A principal who neglects promptly to disavow an act of his agent, by which the latter has transcended his authority, makes the act his own, since principal is bound to disavow act at the first moment that the act comes to his knowledge. McLaren Gold Mines v. Morton, 124 M 382, 224 P2d 975 (1950).

Gambling Transactions: In an action by an elevator company against its former manager and his surety to recover for funds misappropriated by him in grain gambling transactions, refusal of the court to submit the question of ratification of the manager's acts by the company was proper, where it appeared that the gambling transactions were carried on under fictitious names with a commission house in Minneapolis which made reports to the manager so drawn as to conceal their real character, and that the directors of the company did not know of their existence until after the termination of the employment of the manager, who had informed them that he was not gambling. Outlook Farmers' Elev. Co. v. Am. Sur. Co., 70 M 8, 233 P 905 (1924).

Purchase of Lumber: In an action to recover for lumber furnished in the erection of a building the purchase of which was claimed by plaintiff to have been ratified by the defendant owner, by his subsequent promise to pay for it if it had actually been delivered, evidence tending to show ratification was held insufficient to meet the requirements of the rule above. Pew v. McLeish, 62 M 437, 205 P 235 (1922).

Knowledge of Facts: Ratification generally depends upon the intent of the principal. It is an essential element of ratification that the principal has full knowledge of all material facts unless he intentionally and deliberately ratifies knowing that he is not aware of all the facts. Carlson v. Stone-Ordean-Wells Co., 40 M 434, 107 P 419 (1909). See also Arnold v. Genzberger, 96 M 358, 31 P2d 296 (1934) (mechanics' lien, now construction lien); Alward v. Broadway Gold Min. Co., 94 M 45, 20 P2d 647 (1933) (stockholders); First St. Bank of Hilger v. Lang, 55 M 146, 174 P 597 (1918) (bank cashier).

28-10-212. Ratification of part of indivisible transaction.

Case Notes

No Wrongful Discharge Claim When Employment for Specific Term: Plaintiff physician signed a 1-year employment contract with defendant medical center that provided that the employment terms could be extended or renewed by mutual agreement in writing. Although the initial contract expired, plaintiff continued to work by oral agreement for 2 more years. The parties then signed an addendum to the initial contract that set an employment expiration date 6 months later. Plaintiff received a letter 5 days before the expiration date, terminating the employment on the expiration date. Plaintiff filed a wrongful discharge suit, alleging that the termination was unlawful. Defendant moved for summary judgment on grounds that because the addendum provided a specific term of employment, plaintiff had no wrongful discharge claim. The District Court granted summary judgment for defendant, and plaintiff appealed, but the Supreme Court affirmed. A claim for relief that is predicated on discharge from employment is barred if the employment is for a specific term under a written contract and that term has expired. In this case, the addendum constituted a ratification of the original agreement that constituted a contract for a specific term of employment, and by executing the addendum, the parties ratified the original agreement calling for employment for a specific term. The fact that the termination date was stated in the contract recitals did not void the date, because the recitals were consideration for the agreement and the parties intended that the recitals be part of the agreement. Plaintiff's argument that because he did not read the addendum he should not be held to its terms was also without merit because one who executes a contract is presumed to know its contents. Stowers v. Community Medical Center, Inc., 2007 MT 309, 340 M 116, 172 P3d 1252 (2007).

Acceptance of Benefits:

Where a landowner claimed the benefit of an attorney's action in clearing title by paying part of a tax claim as part of a settlement, the landowner ratified other stipulations entered into by the attorney as a part of the same settlement and embodied in the same decree. Purcell v. Gibbs, 133 M 481, 326 P2d 679 (1958).

Where a manufacturer accepts a contract containing ambiguous terms executed by his agent for the sale of goods and acts upon it by shipping them to the dealer, he is not in position to urge that the agent was without authority to make it; ratification by him of a part of an indivisible contract is ratification of the whole. New Home Sewing Mach. Co. v. Songer, 91 M 127, 7 P2d 238 (1931).

Where at the solicitation of the agent of a bank defendant executed a promissory note, transferred personal property as collateral, and then entered into a written agreement with the agent that the maker should not be held liable on the note, the three contracts constituted but a single transaction, by accepting the benefits flowing from a portion of which the bank under this section ratified the whole thereof and was not in a position to assert that in agreeing to relieve defendant from liability on the note the agent exceeded his authority. U.S. Nat'l Bank of Red Lodge v. Chappell, 71 M 553, 230 P 1084 (1924).

Unauthorized Act: If a principal ratifies a part of his agent's unauthorized act he ratifies it in its entirety. Arnold v. Genzberger, 96 M 358, 31 P2d 296 (1934).

28-10-213. Ratification not to prejudice third persons.

Case Notes

Ratification of Void Deeds — Authority of Agent to Convey Property — Title Properly Quieted: Defendant third party raised three challenges to a District Court's conclusion that deeds voided by forgery during transfer were nevertheless ratified by subsequent actions of the parties and contended that the court erred by quieting title to plaintiff. The first argument dealt with the fact that one of the parties never received proper written authority to convey the property to plaintiff, so ratification was voided under the statute of frauds. The Supreme Court noted that an agreement to sell an interest in property must be in writing and that an agent's authority to sell property must also be in writing. However, the agency relationship may arise either by precedent authorization or by subsequent ratification. In this case, the warranty deeds constituted subsequent written authority for conveyance of the property, so the statute of frauds was not violated for want of written authorization. The second argument was that the criteria for ratification were not satisfied, but after examining the chain of title, the Supreme Court found that the personal actions of the principal ratified the deed and that the criteria for ratification were satisfied. The third argument was that defendant was prejudiced as a third party by ratification, but that argument did not prevail because defendant could not have been prejudiced since defendant's interest in the property was invalid both prior to and after ratification and defendant could have become aware of the void deeds by conducting a title check and avoiding the problem. Lastly, title was properly quieted in plaintiff because defendants with prior interests in the property stipulated that they no longer claimed any right, title, or interest in the property. Plaintiff's deed was superior because it was the first to be recorded and had been ratified, and plaintiff was therefore entitled to have quiet title to the property. The District Court was affirmed. Erler v. Creative Fin. & Inv., LLC, 2009 MT 36, 349 M 207, 203 P3d 744 (2009). See also U.S. v. Heinszen, 206 US 370 (1907), Audit Serv., Inc. v. Francis Tindall Constr., 183 M 474, 600 P2d 811 (1979), Safeco Ins. Co. v. Lovely Agency, 200 M 447, 652 P2d 1160 (1982), and Moore v. Adolph, 242 M 221, 789 P2d 1239 (1990).

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28-10-214. When ratification void.

Case Notes

Contract Between Promoters: A contract between promoters under the terms of which one of them agreed to sell, at par less a certain commission, expenses, etc., shares of stock to be issued by a corporation after its organization did not ipso facto by its incorporation become the contract of the company since, to bind it, formal action by its board of directors looking to its assumption or adoption was necessary, and a corporation cannot be bound by contracts made in its behalf before it comes into existence. Kirkup v. Anaconda Amusement Co., 59 M 469, 197 P 1005, 17 ALR 441 (1921).

Deposit of County Funds Without Security: A county, not having authority to empower its Treasurer to make a general deposit of its funds without requiring security as provided by statute, cannot ratify the Treasurer's wrongful act in doing so. Yellowstone County v. First Trust & Sav. Bank, 46 M 439, 128 P 596 (1912).

28-10-215. When ratification may be rescinded.

Case Notes

Unauthorized Act: By the terms of this section it is essential, in order that the ratification of an unauthorized act of an agent be valid, that the principal have full knowledge of all material facts relative to the transaction at the time of the ratification. First St. Bank v. Lang, 55 M 146, 174 P 597, 9 ALR 1139 (1918).

Part 3
Duties of Agent

28-10-301. Agent not to exceed actual authority.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

28-10-302. Duty to keep principal informed.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Broker-Buyer's Duty to Disclose: Plaintiff employed defendant to sell his ranch. Defendant produced some willing buyers who were rejected by the plaintiff. Defendant then found a purchaser willing to buy the machinery and cattle but not the land. Defendant contacted several neighbors, each of whom were willing to buy a portion of the ranch. Defendant did not disclose this to plaintiff. Defendant then made an offer in conjunction with the buyer of the machinery and cattle in anticipation of selling the ranch, in parcels, to the neighbors. Defendant did not disclose that he was one of the offerors. The court held that the defendant had a duty of full disclosure until he was legally bound to buy the property, the day on which the offer was accepted. It was improper to grant defendant summary judgment in this situation. First Trust Co. of Mont. v. McKenna, 188 M 534, 614 P2d 1027, 37 St. Rep. 1026 (1980).

Part 4
Authority of Agent

Part Case Notes

How Authority Shown: The acts or declarations of an agent testified to by third persons are not admissible against his principal to prove the authority of the agent or the scope or extent thereof, unless they were done or made in the presence of the principal or were within his knowledge, or authorized or ratified by him, or there is other evidence of such authority. The direct testimony of an agent on the witness stand is however admissible to prove his authority where his powers and duties have not been reduced to writing. Phelps v. Union Cent. Life Ins. Co., 105 M 195, 71 P2d 887 (1937), followed in Estate of Pruyn v. Axmen Propane, Inc., 2009 MT 448, 354 M 208, 223 P3d 845 (2009).

Agent's Testimony on Authority: The testimony of one who had general supervision of mine guards during a strike prior to their being sworn in as a posse comitatus to suppress a riot, as to what orders he gave the men under him, what his purpose was in giving them, in what capacity the men under him acted and the nature of their duties, was properly admitted over the objection that the questions called for conclusions by the witness, since an agent is a competent witness on the question of his authority as such. McCarthy v. Anaconda Copper Min. Co., 70 M 309, 225 P 391 (1924).

28-10-401. What authority agent has.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Physical Proximity of Principal and Agent at Mediation Session — Agent Authorized to Act in Real Estate Transaction: The Kluvers and McRaes commenced a lawsuit alleging that several power companies had contaminated their ground water. A mediation session between the parties ended with an e-mail detailing a memorandum of understanding for a settlement agreement from the Kluvers' attorney to an attorney for the power companies, including the transfer of real estate between the parties. Although Karson Kluver expressed relief to the McRaes that the case was over, the Kluvers later claimed that the settlement agreement was tentative and invalid. Although there was no signed writing to show the Kluvers assented to the agreement prepared by their attorney at the mediation conference, their physical proximity at the mediation and the text of the memorandum properly authorized the attorney to sign the contract on their behalf, and the later oral representations to the McRaes confirmed that authorization. Kluver v. PPL Montana, LLC, 2012 MT 321, 368 Mont. 101, 293 P.3d 817, following Videau v. Griffin, 21 Cal. 389 (Cal. 1863).

Obligations of Escrow Holder — Strict Adherence to Agreement: A bank acted as escrow agent in an agreement for the purchase of property. The escrow agreement provided that upon default, the seller was "entitled to the immediate return from the escrow agent of the contract for deed, warranty deeds and abstracts" in order to facilitate foreclosure. The agreement further held the escrow agent "liable only to account for the money received by it and for the delivery of the instruments and documents escrowed". The only obligation of the bank was to adhere strictly to the instructions in the agreement. The bank was not obligated to ascertain whether: (1) the demand for return of the documents was technically correct; (2) the notice of default to the buyer was legally sufficient; (3) performance of the contract was impossible; or (4) the contract and default notice were void for vagueness. Turbiville v. Hansen, 233 M 487, 761 P2d 389, 45 St. Rep. 1665 (1988).

No Authority to Contract — Contract Not to Be Ratified or Enforced: Defendants entered into an installment contract to buy land from plaintiffs. The contract was entered by directors of the corporation acting without authority who were defrauding the corporation at the time. When the rightful stockholders came into control, they brought an action to nullify the contract and were awarded summary judgment. Defendant contends that by its actions, plaintiff ratified the contract. A contract entered into without the power to contract cannot be ratified or enforced, and the incapacity to contract cannot be removed by estoppel. Larry C. Iverson, Inc. v. Bouma, 195 M 351, 639 P2d 47, 38 St. Rep. 1911 (1981).

Ostensible Authority: Retailer was entitled to rely on the ostensible authority of wholesaler to grant credit for return of steel grain bins, where wholesaler was the apparent agent of manufacturer, and representatives of the manufacturer had been present when wholesaler had agreed on the return of the bins, and manufacturer had previously given credit for return of other bins. Butler Mfg. Co. v. J & L Implement Co., 167 M 519, 540 P2d 962 (1975).

Failure to Make Authority Known: Authority of bank to apply funds from check endorsed in blank by debtor and delivered to bank by his wife was not measurable in terms of authority that debtor conferred upon his wife without regard to whether that authority or its limitations were made known to bank. Baker Nat'l Bank v. Lestar, 153 M 45, 453 P2d 774 (1969).

Conduct of Business: Employee of used car dealer who had been left on the sales lot with authority to show, demonstrate, quote prices, and make trade-in deals was clothed with sufficient power to conduct the business in the absence of his employer and was agent of the employer in dealing with the public and promoting sale of used cars on the sales lot of his employer. White v. Sorenson, 141 M 318, 377 P2d 364 (1963).

Waiver of Notice of Proof of Loss: Where the certificate of authority of a local fire insurance agent did not show that the agent was empowered to waive notice and proof of loss, and there was no proof of ostensible authority in him so to do, the agent was without authority to waive the conditions. Careve v. Phoenix Ins. Co., 67 M 236, 215 P 235 (1923).

Incur Obligations: It is not essential to the existence of the relationship of principal and agent that the agent be clothed with authority to incur obligations in the name of the principal. St. v. Tuffs, 54 M 20, 165 P 1107 (1917).

28-10-402. Actual authority defined.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Claims Examiner Not Authorized to Make Final Workers' Compensation Settlement for State Fund: Claimant was injured at work in 1973. Her employer was enrolled under Workers' Compensation Plan No. 3. State fund accepted liability and paid some compensation to claimant. For 1½ years state fund negotiated with claimant to reach a final settlement of claimant's disability benefits. Claimant was represented by counsel, and the negotiations were conducted through a claims examiner with state fund who was supervised by the state fund bureau chief. In March 1981, the parties reached a tentative settlement. Claimant and her lawyer signed a petition for full and final compromise settlement. When the petition was presented to the state fund bureau chief, he rejected it as being excessive and beyond the liability of the state as an insurer. Claimant brought the matter to the Workers' Compensation Court where she claimed that she had entered into a binding final agreement with state fund. The Supreme Court affirmed the Workers' Compensation Court ruling that no binding contract was created because the state fund bureau chief had not consented to the terms and the claims examiner had neither actual nor ostensible authority to bind the state fund to a settlement contract. Christenson v. Billings Livestock Comm'n Co., 201 M 207, 653 P2d 492, 39 St. Rep. 2060 (1982).

28-10-403. Ostensible authority defined.

Case Notes

Ostensible Authority Not Provable by Alleged Agent's Statements to Third Party Can Be Proved by Direct Evidence of Alleged Agent as to Relationship With Purported Principal: Hall argued that he did not have to pay for a road constructed by a third party at the direction of Hill because Hill was not his agent and that Hill could not attempt to prove ostensible agency by testifying as to his statements to the third party, which may have been construed by the third party as establishing that Hill was acting as Hall's agent in ordering the road work. The Supreme Court held that although Hill could not establish ostensible agency by testifying as to his statements to the third party, he could establish agency by demonstrating the existence of the agency based on the conduct of the parties, notwithstanding a denial by the alleged principal. Youderian Constr., Inc. v. Hall, 285 M 1, 945 P2d 909, 54 St. Rep. 1012 (1997).

Reasonable Basis for Third Person's Belief That Agency Relationship Existed With Respect to Road Construction — No Basis to Believe Agency Relationship Existed With Respect to Other Construction: Hall argued that he did not have to pay for a road constructed by Youderian at Hill's direction because Hill was not his agent. The Supreme Court ruled that Youderian had acted reasonably in assuming that Hill was Hall's agent based upon prior dealings among the three parties. Hall also argued that another party, Klind, was the general contractor as to the construction of a cabin on the property and that Youderian's only recourse for other construction costs was against the general contractor. The Supreme Court agreed, holding that Klind was the general contractor with respect to the cabin's construction and that because Youderian had not filed a construction lien, his only recourse for reimbursement was against Klind. Youderian Constr., Inc. v. Hall, 285 M 1, 945 P2d 909, 54 St. Rep. 1012 (1997).

Establishment of Implied Agency by Principal's Omissions or Commissions: Ostensible agency may be established by principal's omissions as well as commissions, but failure to disclaim authority asserted by an agent usually concerns attempts of an agent to extend existing authority by his representations to a third party. NW. Polymeric, Inc. v. Farmers St. Bank, 236 M 175, 768 P2d 873, 46 St. Rep. 275 (1989).

Reliance Solely on Alleged Agent's Statements: A manufacturing company received a government contract to supply combat helmets based in part upon a letter supplied to the Department of Defense by Farmers State Bank stating that Farmers Bank, with the participation of First National Bank of Missoula, would provide financing. Neither bank funded the project, and the company brought suit for tort and contract damages. The Supreme Court affirmed a summary judgment in First National Bank's favor, ruling that Farmers Bank could not be construed to be First National's agent solely on the basis of statements made by Farmers Bank in its letter to the Department of Defense. NW. Polymeric, Inc. v. Farmers St. Bank, 236 M 175, 768 P2d 873 46 St. Rep. 275 (1989), followed in Estate of Pruyn v. Axmen Propane, Inc., 2009 MT 448, 354 M 208, 223 P3d 845 (2009).

Sales — Guaranty of Buyer's Payment by Guarantor's Agent: Jacobs sold the uniform sales part of his business to K&M Sports, which in turn sold it to another, who defaulted on the sale. Jacobs, as secured party, repossessed the inventory and sold it to Snick Sports. Dirkson, who worked for K&M and then Snick, told Powers that Jacobs would guarantee Snick's payment of goods sold to Snick by Powers. There was disagreement as to whether Dirkson worked for Jacobs. For 2 years Powers mailed merchandise, statements, and invoices to Jacobs, who forwarded them to Snick, who paid the bills. When some bills went unpaid, Powers sued Jacobs when he failed to pay the bills on request. The mailings to Jacobs put him on reasonable notice that something was wrong. His failure to investigate and take action was want of ordinary care that caused or allowed Powers to believe an authorized agency existed between Jacobs and Dirkson. Thus, there was an ostensible agency and ostensible authority. For the same reason, a valid guaranty existed and Jacobs was estopped from defending against it on the basis of the Statute of Frauds. A jury verdict for Powers was affirmed. Powers Mfg. Co. v. Leon Jacobs Enterprises, 216 M 407, 701 P2d 1377, 42 St. Rep. 906 (1985).

Claims Examiner Not Authorized to Make Final Workers' Compensation Settlement for State Fund: Claimant was injured at work in 1973. Her employer was enrolled under Workers' Compensation Plan No. 3. State fund accepted liability and paid some compensation to claimant. For 1½ years state fund negotiated with claimant to reach a final settlement of claimant's disability benefits. Claimant was represented by counsel, and the negotiations were conducted through a claims examiner with state fund who was supervised by the state fund bureau chief. In March 1981, the parties reached a tentative settlement. Claimant and her lawyer signed a petition for full and final compromise settlement. When the petition was presented to the state fund bureau chief, he rejected it as being excessive and beyond the liability of the state as an insurer. Claimant brought the matter to the Workers' Compensation Court where she claimed that she had entered into a binding final agreement with state fund. The Supreme Court affirmed the Workers' Compensation Court ruling that no binding contract was created because the state fund bureau chief had not consented to the terms and the claims examiner had neither actual nor ostensible authority to bind the state fund to a settlement contract. Christenson v. Billings Livestock Comm'n Co., 201 M 207, 653 P2d 492, 39 St. Rep. 2060 (1982).

Waiver of Time Limit by Superintendent: Because the board allowed plaintiff to believe that the superintendent had the authority to waive the statutory time limit of 20-4-204 for a hearing request, plaintiff was entitled to a hearing before the board concerning the termination of his contract, even though his request came after expiration of the time limit. Yanzick v. Bd. of Trustees, 177 M 459, 582 P2d 338 (1978).

Authority of General Manager to Contract: In an action to recover employer's contributions to union trust funds under collective bargaining compliance agreements, the court erred in finding that defendant's general manager had no authority to enter into such agreements, when the record showed that the general manager had implied an ostensible authority which was not affected by limitations contained in the regulations and bylaws of the defendant. Audit Serv., Inc. v. Elmo Road Corp., 175 M 533, 575 P2d 77 (1978).

Course of Dealing Establishing an Ostensible Agency: Where principal's conduct led third party to believe he was dealing with an agent and third party returned merchandise to agent under such belief, principal cannot hold third party liable for cost of returned merchandise as principal led third party to believe agent had apparent authority to accept return of merchandise. Butler Mfg. v. J & L Implement Co., 167 M 519, 540 P2d 962 (1975).

Service Upon Corporation — Proper Agent: The doctrine of ostensible agency appears to have no application when it becomes involved with the question whether service of process has been legally made upon a "managing or general agent". Further, service upon a former employee of a company was not service upon the company itself and default judgment was vacated and set aside. Kraus v. Treasure Belt Min. Co., 146 M 432, 408 P2d 151 (1965).

Permissive Use of Vehicle by Employee: The mere permissive use by a truck driver of his employer's truck for personal purposes did not make the owner of the truck liable for the driver's negligence under the doctrine of ostensible authority. Searle v. Great N. Ry., 189 F. Supp. 423 (D.C. Mont. 1960).

Acts and Statements Establishing Agency:

Ostensible authority of an agent to do an act may be created by written or spoken words or any other conduct of the principal which reasonably interpreted causes a third person to believe that the principal consents to the doing of the act on his behalf by the person purporting to act for him. Coover v. Davis, 112 M 605, 121 P2d 985 (1941).

Evidence that a lien claimant who performed work on a defendant's building dealt with a brother of the attorney in fact of the owner, which brother was looking after the building at the request of the attorney in fact or of the owner and collected rents and endorsed rent checks received, was sufficient to sustain trial court's finding of agency, since the brother with whom the contract was made was at least the ostensible agent of the owner. Doney v. Elison, 103 M 591, 64 P2d 348 (1937).

Where a person is shown to have been the agent of another in a particular business and continues to act within the apparent scope of his prior authority it will be presumed that his authority still continues and his acts will bind his former principal even though the agent's authority has been revoked, if the persons dealing with him had no notice of the revocation and relied upon the continued existence of his agency. Eastman Kodak Co. v. Sibley, 72 M 338, 233 P 613 (1925).

To constitute one an ostensible agent, the party sought to be held as principal must by reason of some act or want of ordinary care on his part have led the other party to believe he was his agent even though not actually employed by him. Hartt v. Jahn, 59 M 173, 196 P 153 (1921).

Ostensible Versus Implied Agency: Where an ostensible agency is sought to be proved by other like prior transactions, knowledge of them by plaintiff is necessary, but in the case of an implied agency such knowledge is immaterial. Phelps v. Union Cent. Life Ins. Co., 105 M 195, 71 P2d 887 (1937).

Estoppel: Under the doctrine of ostensible authority, where a principal makes it possible by his conduct for his agent to inflict injury upon a third person who dealt with him in good faith under his apparent authority, he is bound by the acts of the agent and estopped from denying the authority of the latter to act. Lindblom v. Employers' Liab. Assurance Corp., 88 M 488, 295 P 1007 (1930).

Knowledge of Extent of Authority: The president of a corporation is chargeable with knowledge of the extent of the authority of its secretary and therefore may not rely upon ostensible authority in the latter to enter into a contract with him (the president) for the performance of an act in behalf of the corporation which he knew the secretary had no power to make. Stanton v. Occidental Life Ins. Co., 81 M 44, 261 P 620 (1927).

Question of Fact: The apparent authority of an agent to act as the representative of his principal must be gathered from all facts and circumstances in evidence and is ordinarily a question of fact. Campbell v. Oriental Trading Co., 58 M 520, 193 P 1112 (1920).

Acquiescence in Conduct: The directors of a bank allowed the cashier to conduct the affairs of the bank. This pattern gave the cashier the ostensible authority to renew a promissory note, at least as regards an innocent third party, even though the bank was defrauded by the act. First St. Bank of Hilger v. Lang, 55 M 146, 174 P 597 (1918).

28-10-404. When and as to whom agent's authority restricted.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Constructive Notice: A person who brings suit to recover money paid on a life insurance premium note given before the rejecting of his application must be charged with constructive notice of the restriction placed upon the authority of the insurance agent where by the use of reasonable diligence such authority could have been ascertained. Weidenaar v. New York Life Ins. Co., 36 M 592, 94 P 1 (1908).

28-10-405. Implied powers of agent.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

Case Notes

Authority to Contract: Authority to make a contract is inferred from authority to conduct a transaction if the making of such contract is incidental to the transaction or is reasonably necessary to accomplish it. Hence, where in an action to recover the amount of a premium of fire insurance, covering a store owned by defendants, the manager thereof, the father of one of the defendants, had arranged for the insurance with plaintiff for a given year, defendants paying the premium, the jury was justified in finding that he was their authorized agent in arranging for the insurance for the next year. Coover v. Davis, 112 M 605, 121 P2d 985 (1941).

Extent of Authority: An agent has authority "to do everything necessary and proper and usual, in the ordinary course of business, for effecting the purpose of his agency". Commercial Credit Co. v. Blair, 84 M 314, 275 P 748 (1929).

Implied Power to Pledge Credit: Where it appears that the agent of a telegraph company had full power to manage its business and make all contracts and arrangements to carry on its business, that the principal knew that the monthly receipts of the business were much less than the expenses, and that it was necessary for the agent to maintain a bank account in its name, the agent has the implied authority to borrow for the company an amount of money not disproportionate to the volume of business transacted. Helena Nat'l Bank v. Rocky Mtn. Tel. Co., 20 M 379, 51 P 829 (1898).

28-10-406. Interpretation of authority given partly in general and partly in specific terms.

Case Notes

Interpretation of Agency Agreement: Where the words used to create a principal and agent relationship are ambiguous in themselves, they are to be taken most strictly against the principal, and the agent in his dealings with a third person may bind the principal in accordance with usage or by any construction of the ambiguous words that is reasonable. The grant of powers is not to be frittered away by very nice and metaphysical distinctions when the general tenor of the instruments is in favor of what was done under the power and when the principal has reaped the benefit of it. McLaren Gold Mines v. Morton, 124 M 382, 224 P2d 975 (1950).

When Authority Implied: An agent with general authority to manage his principal's business has no implied authority to bind his principal by a promissory note. Such authority must be expressly conferred, or be necessarily implied from the exigencies and the general course of the particular employment, or the act must be ratified by the principal. Helena Nat'l Bank v. Rocky Mtn. Tel. Co., 20 M 379, 51 P 829 (1898).

28-10-407. Statutory exceptions to general authority.

Compiler's Comments

Code Commissioner Correction: Pursuant to sec. 28, Ch. 123, L. 2013, the Code Commissioner in (3) substituted "Title 72, chapter 38" for "Title 72, chapter 34" to correct reference rendered erroneous when Title 72, chapter 34, was repealed and replaced as part of the Montana Uniform Trust Code enacted by Ch. 264, L. 2013.

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Self-Dealing During Agency Relationship — Proof of Undue Influence and Constructive Fraud — Shift of Burden of Proof — Agent Prohibited From Acting as Trustee Would Have Been Prohibited: Alice, a good friend of Maggie, lived near her and undertook to manage Maggie's financial affairs when Maggie's health began failing. As Maggie became more afflicted with dementia, Alice moved in with Maggie to care for her and began writing all of Maggie's checks for her. Alice also began selling Maggie's securities, depositing the proceeds into her own account, and writing checks to herself for purposes that sometimes involved Maggie. During this time, Maggie's physician found her mental capacity to be steadily diminishing and urged Alice to take Maggie to a nursing home. After Alice had depleted Maggie's financial resources from approximately $200,000 to approximately $20,000, Maggie's sister, Ida, discovered that Maggie had been moved to a nursing home and discovered that her money had been spent by Alice. Maggie died shortly thereafter, and the personal representative brought an action against Alice for an accounting of Maggie's funds. The Supreme Court held that all of the criteria for proof of undue influence established in Christensen v. Britton, 240 M 393, 784 P2d 908 (1989), had been satisfied and that the District Court therefore erred in not shifting the burden of proof to Alice to prove that the financial transactions involving Alice were fair and voluntary. Likewise, the Supreme Court also held, because of the agency or fiduciary relationship between Alice and Maggie, that the District Court erred in placing the burden on the estate to prove constructive fraud. The Supreme Court held that under statutory provisions of agency law, Alice was not authorized to do any act that a trustee would be prohibited by former Title 72, ch. 34 (repealed in part and replaced by Title 72, ch. 38), from doing and found that such a prohibition still existed under subsection (3) of this section, even though 72-20-208 had been repealed. The Supreme Court therefore remanded the case to the District Court for a new trial. Luke v. Gager, 2000 MT 377, 303 M 474, 16 P3d 377, 57 St. Rep. 1599 (2000).

Fiduciary Duty of Union Officers: It was proper to instruct the jury on the duty of fiduciary responsibility owed by union officers by comparing it to a trust relationship; stating that, as fiduciaries, the officers were required to act prudently; and allowing the jury to consider the duties, powers, and obligations in the union constitution and bylaws. Local Union No. 400 v. Bosh, 220 M 304, 715 P2d 36, 43 St. Rep. 388 (1986).

Authority of Real Estate Broker: A real estate broker does not enjoy general authority but is only authorized to do what is specifically assigned in his contract of employment. Martin v. Vincent, 181 M 247, 593 P2d 45 (1979), following Diehl & Assoc., Inc. v. Houtchens, 173 M 372, 567 P2d 930 (1977), and followed in WRB-West Associates, Inc. v. Madison Addition Inv. Ltd. Partnership, 270 M 498, 893 P2d 340, 52 St. Rep. 329 (1995).

Authority of General Manager to Contract: In an action to recover employer's contributions to union trust funds under collective bargaining compliance agreements, the court erred in finding that defendant's general manager had no authority to enter into such agreements, when the record showed that the general manager had implied an ostensible authority which was not affected by limitations contained in the regulations and bylaws of the defendant. Audit Serv., Inc. v. Elmo Road Corp., 175 M 533, 575 P2d 77 (1978).

Fraud and Misrepresentation: Common honesty denies to an agent the right to profit at the expense of his principal by chicanery and misrepresentation. Middlefork Cattle Co. v. Todd, 49 M 259, 141 P 641 (1914).

28-10-408. When agent may disobey instructions.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

28-10-409. No authority to defraud principal.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Fiduciary Duty of Union Officers: It was proper to instruct the jury on the duty of fiduciary responsibility owed by union officers by comparing it to a trust relationship; stating that, as fiduciaries, the officers were required to act prudently; and allowing the jury to consider the duties, powers, and obligations in the union constitution and bylaws. Local Union No. 400 v. Bosh, 220 M 304, 715 P2d 36, 43 St. Rep. 388 (1986).

Sufficient Evidence Supporting Jury Verdict Against Union Officials for Misappropriation of Funds: A union sued former officers and business managers, alleging, among other things, misappropriation and conversion of union funds and constructive fraud. The union prevailed, and money damages were awarded to the union. On appeal, the Supreme Court ruled that the evidence supported the award of money damages even though no one had testified at trial as to the specific amount of money defendants allegedly owed to the union. The jury heard evidence on mismanagement and self-dealing with regard to union property and on the financial losses of the union during defendant Bosh's administration. Testimony of the union indicated that defendants had not kept adequate financial records. The evidence may have contained contradictions, but it was substantial and adequate. Local Union No. 400 v. Bosh, 220 M 304, 715 P2d 36, 43 St. Rep. 388 (1986).

Criminal Liability — Intentional Breach of Fiduciary Duty: Defendant entered a lease agreement with Town Pump, Incorporated to operate a gas station. Defendant was required to make daily deposits to Town Pump's bank account as payment for gasoline sold. A gasoline audit revealed defendant had failed to deposit $6,377 of proceeds due Town Pump. Defendant contended that a debtor-creditor relationship existed and that he only had a contractual duty to repay the debt, and that a breach of this civil obligation could not be the basis for criminal liability. The evidence showed Town Pump entrusted defendant with the gasoline it supplied with the understanding that its share of sale proceeds would be deposited to its account. The jury was presented with the factual question of when title to the gasoline passed. The jury concluded title did not pass upon delivery. Through the course of dealing in the months preceding the audit, defendant demonstrated his understanding of the entrustment and his responsibility. The deviation from this recognized fiduciary duty when he falsified accounting reports to the company clearly indicated an intent to purposely deprive Town Pump of its proceeds. The deliberate attempt to conceal retention of the proceeds is inconsistent with an ordinary debtor-creditor relationship. There was nothing in the record to show the parties' intent to create a debtor-creditor relationship. Defendant could not avoid criminal liability for taking money entrusted to him by calling it a loan. St. v. Frederick, 208 M 112, 676 P2d 213, 41 St. Rep. 207 (1984).

Acting in Dual Capacity: The general rule that knowledge of the agent is imputable to his principal has no application where the agent is acting in a dual capacity, as where he, though formally acting as such, is in reality acting in his own or another's interest and adversely to his principal. Harrison St. Bank v. USF&G Co., 94 M 100, 22 P2d 1061 (1933).

28-10-422. What included in authority to sell real property.

Case Notes

Potential Access Rights Merged With Deeds and Extinguished — Applicability of Contract Law Doctrine of Merger: Prior to Gehring's consent to sell 360 acres to APS Corporation (APS) in 1970, they entered an agreement that included a provision on access rights, whereby Gehring purported to grant future purchasers access to other land owned by Gehring for certain recreational purposes. After being told by the Gehring Ranch Corporation that they would not be allowed access to Gehring's land for recreation, the successors in interest to APS sought to enforce the agreement, alleging that they had been improperly excluded from the land and that the agreement created an easement over Gehring's land. The District Court granted summary judgment for the Gehring Ranch Corporation, noting that the agreement did not identify Gehring's other lands upon which an easement was purportedly created. The court also held that any agreement prior to execution of the deeds was merged with the deeds and that because the deeds transferring title did not provide for access, any access rights promised in the agreement were lost. The decision was appealed, and the Supreme Court affirmed. The clause in the agreement was part of a larger agreement to transfer property in the future, and Gehring did not intend to create an easement, but at most intended to provide for potential access privileges if certain conditions, such as creation of a property owners' association and adoption of rules governing the use of the recreational privileges, were met. The Supreme Court cited Urquhart v. Teller, 1998 MT 119, 288 M 497, 958 P2d 714 (1998), in applying the contract law doctrine of merger, holding that the deeds contained all the rights of the parties and that because no access privileges were mentioned in the deeds, any potential access rights referred to in the agreement merged with the deeds and were lost. Richman v. Gehring Ranch Corp., 2001 MT 293, 307 M 443, 37 P3d 732 (2001).

Contract Provisions Merged Into Deed — Covenants Not Intended to Be Collateral Extinguished by Unrestricted Deed: A contract for the sale of property can contain a valid covenant running with the land, but generally, all provisions in a sale contract are merged into the warranty deed, founding the purchaser's rights in the deed covenants rather than in the executed contract, unless the parties intend for an agreement in a contract for sale to be collateral. Covenants relating to title, quantity, and possession of land are generally not collateral and thus merge into the deed. In the present case, the parties intended for the contract for deed and attendant restrictions to merge into the warranty deed, so the general rule of merger applied. The District Court did not err in refusing to enforce the covenants contained in the contract for deed. Urquhart v. Teller, 1998 MT 119, 288 M 497, 958 P2d 714, 55 St. Rep. 461 (1998), followed in Richman v. Gehring Ranch Corp., 2001 MT 293, 307 M 443, 37 P3d 732 (2001), and Tungsten Holdings, Inc. v. Olson, 2002 MT 158, 310 M 374, 50 P3d 1086 (2002).

Broker-Buyer's Duty to Disclose: Plaintiff employed defendant to sell his ranch. Defendant produced some willing buyers who were rejected by the plaintiff. Defendant then found a purchaser willing to buy the machinery and cattle but not the land. Defendant contacted several neighbors, each of whom were willing to buy a portion of the ranch. Defendant did not disclose this to plaintiff. Defendant then made an offer in conjunction with the buyer of the machinery and cattle in anticipation of selling the ranch, in parcels, to the neighbors. Defendant did not disclose that he was one of the offerors. The court held that the defendant had a duty of full disclosure until he was legally bound to buy the property, the day on which the offer was accepted. It was improper to grant defendant summary judgment in this situation. First Trust Co. of Mont. v. McKenna, 188 M 534, 614 P2d 1027, 37 St. Rep. 1026 (1980).

Power of Attorney — Interests of Principal: An agent, under a general power of attorney, authorized to sell, convey, and mortgage the grantor's property may execute a trust deed conveying the grantor's individual property as security for the payment of a debt due from a firm of which he is partner so long as he acts in the interests of the principal. Muth v. Goddard, 28 M 237, 72 P 621 (1903).

Part 5
Subagents

28-10-501. When agent may delegate powers.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Signing of Insurance Policy:

Where the president of a bank acting as agent for a fire insurance company had determined a particular risk when a policy was first issued to the insured, he had the right to delegate to the cashier of the bank, who had for a considerable period of time handled much of the detail work in connection with issuing policies, the right to countersign a renewal policy. Altermatt v. Rocky Mtn. Fire Ins. Co., 85 M 419, 279 P 243 (1929).

Evidence that it was customary for insurance agents in a certain locality to entrust clerks and assistants with the signing of fire insurance policies in the name of the local agent was admissible under this section. Altermatt v. Rocky Mtn. Fire Ins. Co., 85 M 419, 279 P 243 (1929).

Employment of Medical Assistance: Where an agent was authorized by a master to employ medical assistance for an injured servant, such agent had no authority to delegate to a physician employed authority to employ an assistant. Bond v. Hurd, 31 M 314, 78 P 579 (1904). See also Trenouth v. Mulroney, 124 M 499, 227 P2d 590 (1951).

Responsibility for Subagent's Actions: The ministerial work of a corporation may be delegated by the directors (agents of the corporation) to subordinate agents, and often must be. The details of a corporation's business necessitate this. If the directors act in good faith and with reasonable care and diligence in appointing and supervising such inferior agents, they are not personally responsible for damages occasioned by the agent's negligence, or even crimes. But a director cannot wholly escape his duty of supervision or transfer his authority to represent his principal, at least without the principal's consent. Cameron v. Kenyon-Connell Commercial Co., 22 M 312, 56 P 358 (1899).

28-10-502. Effect of unauthorized employment of subagent.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

28-10-503. Effect of authorized employment of subagent.

Case Notes

Agent of Receiver: An agent of the receiver of the assignee of a promissory note stands in the same position as the receiver, his principal, and a receiver occupies the same position as his insolvent principal prior to the former's appointment. Erlandson v. Erskine, 76 M 537, 248 P 209 (1926).

Part 6
Rights and Liabilities of Principal

Part Case Notes

Former Boss of City Employee Contributed to Termination at New Job — District Court's Summary Judgment for City Improper: A man working for the city of Billings and his boss had a bad professional relationship. When the man moved to a new job, the boss called the man's new employer to anonymously complain about the man and subsequently provided the new employer with a paper trail he had built regarding the man. The man sued the city in District Court, asserting claims for tortious interference with business relations and negligent misrepresentation and asserting that the city was vicariously liable for the boss's tortious conduct under the common-law doctrine of respondeat superior. The record suggested different possible motives for the boss's actions. The District Court granted the city summary judgment on the ground that the boss engaged in alleged tortious conduct outside the scope of his employment. On appeal, the Supreme Court reversed, noting genuine issues of material fact precluding summary judgment on whether the boss's actions were incidental to implicitly authorized conduct and whether this was within the scope of employment. Brenden v. Billings, 2020 MT 72, 399 Mont. 352, 470 P.3d 168.

Sufficient Evidence to Support Jury Verdict That Principal Breached Fiduciary Duty to Its Agent: An insured brought an action against Deonier, an insurance agent, and Paul Revere Life Insurance Company (Revere) to recover benefits and damages after the insured's claim was denied on grounds of a preexisting condition, despite the incontestability clause in the policy. The agent cross-claimed against the company for indemnity and breach of fiduciary duty, contending that there was a significant amount of evidence that Revere planned to assert the Forman defense in Montana (see Mass. Cas. Ins. Co. v. Forman, 516 F2d 425 (5th Cir. 1975), in which an insurer asserted a legal defense to the incontestability clause based on its definition of sickness as excluding disabilities that manifested themselves prior to the date of issue of the policy) and that Revere's failure to inform Deonier of its intention to invoke the defense was a clear breach of Revere's duty to inform its agents of a risk of pecuniary loss from potential lawsuits. Revere asserted that pursuant to Doettl v. Colonial Life & Accident Ins. Co., 505 F. Supp. 127 (D.C. Mont. 1981), in which a Montana federal District Court endorsed the Forman defense, it had no reason to believe that its policy interpretation might be in violation of Montana law and therefore did not breach its duty to inform its agents of risk of pecuniary loss. In the first Deonier case, Deonier & Associates v. Paul Revere Life Ins. Co., 2000 MT 238, 301 M 347, 9 P3d 622 (2000), the Supreme Court reversed the lower court's summary judgment in favor of Revere that held that there had not been a breach of fiduciary duty and remanded the case back to the lower court for a jury trial on the issue of liability and damages. The jury found for Deonier and awarded her $150,000 in compensatory damages and $1 million in punitive damages, which the trial court reduced to $375,000. The trial court denied Revere's motion for judgment as a matter of law that it had not breached its fiduciary duty. The Supreme Court affirmed on the basis that Deonier had presented evidence that Revere knew it would assert the Forman defense and that such an action might lead to pecuniary damages for its agents, and therefore there existed a legally sufficient evidentiary basis for a reasonable jury to find that a breach of fiduciary duty had occurred. Deonier & Associates v. Paul Revere Life Ins. Co., 2004 MT 297, 323 M 387, 101 P3d 742 (2004).

Indemnity of Insurance Agent for Defending Actions Performed on Insurer's Behalf in Solicitation of Application for Insurance: An insured brought a negligent misrepresentation action against Deonier, an insurance agent, and Paul Revere Life Insurance Company (Revere) to recover benefits and damages after the insured's claim was denied on grounds of a preexisting condition, despite the incontestability clause in the policy. Deonier cross-claimed against the company for indemnity, and the District Court required Revere to indemnify for damages that Deonier suffered as a result of the lawsuit. Revere appealed on grounds that Deonier was acting as an agent for the insured when recommending a disability policy, rather than as an agent for Revere, asserting that the fees that Deonier incurred were for defending the insured's claim that Deonier was actively negligent, defeating an indemnity claim. The Supreme Court affirmed, holding that because Revere admitted in its pleadings that there was no basis in law or fact for the negligent misrepresentation claim against Deonier, Revere implicitly conceded that Deonier's liability to the insured arose solely from the agency relationship between Deonier and Revere, a situation in which indemnity was required. Deonier & Associates v. Paul Revere Life Ins. Co., 2000 MT 238, 301 M 347, 9 P3d 622, 57 St. Rep. 989 (2000). See also Tynes v. Bankers Life Co., 224 M 350, 730 P2d 1115 (1986), and Restatement (Second) of Agency 439 (1958).

Receipt of Asking Price and Licensing — Only Requirements for Commission: Defendants decided to sell their ranch and were contacted by plaintiff, a real estate salesperson. Defendants listed the ranch on a nonexclusive basis for $1.6 million and agreed to pay a 5% commission on the sale. Plaintiff presented offers from Semenza, which were rejected. Later, Semenza offered the asking price, and a contract to sell and purchase was executed, reciting that Semenza had paid $50,000 to plaintiff as earnest money. Semenza failed to obtain financing by the closing date, and it was determined he had never paid the earnest money to plaintiff. A new agreement to sell was executed, referencing the obtaining of long-term financing, at a meeting at which defendants were again represented by counsel. The transaction was closed, and defendants refused to pay plaintiff his commission, contending he was not a licensed broker as claimed at the time they entered the agreement and that he had actually represented the buyer. On appeal from a summary judgment, the Supreme Court found that under 37-51-401 a person need only be a licensed salesperson to receive a commission and that plaintiff was a licensed broker at the time the transaction closed. The defendants received their asking price through plaintiff's efforts, even though Semenza had to bring in a partner. There was no evidence defendants were damaged by the claimed conflict of interest. They ratified the entire transaction and were represented by competent counsel throughout. Deimler v. Ostler, 200 M 350, 651 P2d 41, 39 St. Rep. 1797 (1982).

28-10-601. Accrual of rights and liabilities to principal.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Question of Material Fact Regarding Law Firm's Handling of Real Estate Contract — Summary Judgment Improperly Granted: Plaintiff sued its law firm for work performed in writing a contract for a real estate transaction. Plaintiff's expert opined that the firm violated the standard of care when it: (1) had a nonattorney with no contract drafting experience draft the initial agreement and insert an inaccurate legal description of the property obtained from plaintiff's own engineering firm; (2) used the phrase "more or less" to cure defects in the property description when the legal description was clearly deficient; (3) failed to include a provision that required the seller to sign future applications for a final plat; and (4) failed to execute proper escrow documents to prevent the seller from having veto power over any proposed development of the property. The law firm presented its own expert to refute the allegations. The District Court analyzed the allegations of negligence, applying the legal malpractice standards in Lorash v. Epstein, 236 M 21, 767 P2d 1335 (1989), and, finding no issues of material fact, granted the law firm's motion for summary judgment. Plaintiff appealed, and the Supreme Court reversed, finding that summary judgment was improper. The conflicting expert testimony itself raised a material issue of fact regarding the standard of care that required resolution by a trier of fact. Further, material questions remained concerning whether the law firm's independent failure to recognize a problem with the legal description contributed as a cause to plaintiff's damages, whether the firm followed the requisite standard of care in drafting the escrow agreement, and whether the purported terms of the escrow agreement satisfied the requisite standard of care. Babcock Place Ltd. Partnership v. Berg, Lilly, Andriolo, & Tollefsen, P.C., 2003 MT 111, 315 M 364, 69 P3d 1145 (2003).

Contract for Deed — Seller's Right to Cancel After Accepting Late Payments to Escrow Agent: Buyers under contract for deed made three late payments to the escrow agent. The escrow agent's acceptance of the three checks was not acceptance by the seller under the theory that the escrow agent was the seller's agent and acceptance by the agent was acceptance by the principal, nor did seller's acceptance of the payments from the escrow agent ratify the agent's acceptance. Failure to promptly return the payments did not waive seller's right to cancel the contract. The contract gave buyers 90 days from notice of default to pay the balance due under the contract, and they could do so in more than one installment. Seller decided the three payments might be installments in an attempt to pay the balance due and decided to hold the checks until it became apparent that the buyers were either going to pay off the balance due or were attempting to induce seller to waive her right to cancel the contract. Seller returned the checks when she realized the latter was the motive. In addition, seller sent a second cancellation notice, making it clear what her intent was. Boles v. Ler, 222 M 28, 719 P2d 793, 43 St. Rep. 1035 (1986).

Special Agent's Authority: One dealing with a special agent without acquainting himself with the strict extent of the agent's authority and governing himself accordingly, acts at his peril; he is not justified in relying upon any appearance of authority except that which is directly deductible from the nature of the authority actually conferred. Phelps v. Union Cent. Life Ins. Co., 105 M 195, 71 P2d 887 (1937).

Attorney and Client: The rule that a principal is presumed to have notice of that of which the agent has notice and ought in good faith and the exercise of ordinary care to communicate to his principal, as applied to client (principal) and attorney (agent) does not pertain to facts acquired prior to the employment of the attorney or in the transaction of business for another client. Hansen v. Johnson, 90 M 597, 4 P2d 1088 (1931), explained in Cent. Bank & Trust Co. v. Lee C. Nelson, Inc., 221 F. Supp. 721 (D.C. Mont. 1963), which was followed, as to knowledge of the attorney imputed to the client, in Kaeding v. W.R. Grace & Co., 1998 MT 160, 289 M 343, 961 P2d 1256, 55 St. Rep. 640 (1998).

Sale of Land: Where the agency of one who was instrumental in making a sale of land was admitted by the seller (plaintiff), who made no contention that it had ever been terminated, the evidence on the contrary showing that such agent continued making sales of land for his principal in the same vicinity, the presumption obtains that the agency was still in being at a time thereafter when defendant notified the agent to so construct a ditch that water could be brought upon the land as agreed in the contract, and written notice to the agent was notice to the principal. Healy v. Ginoff, 69 M 116, 220 P 539 (1923).

Demonstration of Car: Where an automobile dealer's chauffeur was demonstrating a car for his employer and permitted the prospective buyer's daughter to drive the car and the girl lost control of the car, and the chauffeur then took hold of the wheel and steered the car upon the sidewalk striking a pedestrian, the chauffeur was acting within the scope of his employment and the employer was liable for the injuries suffered by the pedestrian. Hoffman v. Roehl, 61 M 290, 203 P 349, 20 ALR 189 (1921).

Liability of Principal for Goods Purchased: Where the evidence showed that among other things, it was the duty of the agent for a company engaged in furnishing crews for railroad track maintenance work to arrange for the needs of the crews, the principal was liable for goods purchased by him for that purpose. Campbell v. Oriental Trading Co., 58 M 520, 193 P 1112 (1920).

When Principal Bound: A principal is bound only by the authorized acts of his agent, and prior authority or subsequent ratification must be shown in order to render the principal answerable "ex contractu" for the conduct of his agent. Spelman v. Gold Coin Min. & Mill. Co., 26 M 76, 66 P 597 (1901).

Law Review Articles

Liability of Principal for Statements Made by His Agent, Hirst, 3 Mont. L. Rev. 81 (1942).

28-10-602. Principal's responsibility for agent's negligence, omissions, and wrongs.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Certified Question — Respondeat Superior Doctrine — Employer Vicarious Liability — Law Enforcement Officers' Scope of Employment — Use of Authority as On-Duty Officer to Sexually Assault Person Being Investigated for Crime — Sexual Intercourse in Exchange for Not Being

Charged for Crime — Sexual Assault Not Outside Scope of Employment as Matter of Law — Restatement (Second) of Agency 229 Adopted. L.B. v. U.S., 2022 MT 166, 409 Mont. 505, 515 P.3d 818.

Respondeat Superior Applicable to City Council Member Who Severely Criticized City Employee — Criticism Within Scope of Employment for Respondeat Superior but Not for Application of Legislative Immunity: Shoemaker, a member of the Thompson Falls City Council, severely criticized Denke, the city clerk and finance officer, in two letters to the editor and in a City Council meeting for her job performance that Shoemaker alleged caused the city to hire a CPA. Denke charged that Shoemaker's criticism was unlawful retaliatory conduct for her previous filing of a sexual harassment complaint against the Mayor. Following Kenyon v. Stillwater County, 254 M 142, 835 P2d 742 (1992), the Supreme Court held that Shoemaker was a city employee. The Supreme Court held that Shoemaker was acting as a member of the City Council when he signed the letters and that the city had admitted in an administrative hearing that Shoemaker was within the scope of his employment. The court held that: (1) Shoemaker didn't have to be Denke's supervisor for purposes of applying respondeat superior; (2) Shoemaker's unlawful retaliatory conduct was not within the official discharge of Shoemaker's duties for the purposes of legislative immunity under 27-1-804, but the conduct was within the scope of Shoemaker's employment for purposes of respondeat superior; and (3) the statement of the city in the Human Rights Commission administrative hearing that Shoemaker was acting as a member of the City Council constituted a judicial admission, was an "acknowledgment" under 2-9-305, and was binding upon the city for the purposes of its liability for retaliation. Denke v. Shoemaker, 2008 MT 418, 347 M 322, 198 P3d 284 (2008).

Attorney Agent Acting Within Scope of Employment Responsible to Principal and Not Third Party for Actions: Attorney Cresap was employed by Sorenson to prepare auction instructions for the sale of Sorenson's real property. The bidding instructions prepared by Cresap stated that Sorenson could reject all bids below $270,000 but did not disclose that that amount was the minimum acceptable price for the property. Crane Creek Ranch (Crane Creek) bid $248,000 on the property, was outbid by the Goss brothers, and was told that it could not raise its bid because it failed to meet the minimum bid of $270,000. After failing to purchase the property, Crane Creek sued Cresap and Sorenson for specific performance, fraud, negligent misrepresentation, and deceit, and after the District Court held for Cresap, the claims against Sorenson were stipulated to be dismissed with prejudice. The Supreme Court held that the District Court properly granted summary judgment for Cresap on all counts of the complaint. The Supreme Court held that Cresap was known to Crane Creek as acting as Sorenson's attorney and, in that capacity and in accordance with Smith v. Fladstol, 248 M 18, 807 P2d 1361 (1991), and Rhode v. Adams, 1998 MT 73, 288 M 278, 957 P2d 1124 (1998), Cresap's duty of care ran to his principal, Sorenson, and not to any unrelated third party, such as Crane Creek. Any negligence on the part of Cresap is imputed to his principal, and any legal action against Cresap for actions taken by him within the scope of his agency employment must instead be brought against Cresap's principal, Sorenson. However, as the Supreme Court observed, the cause of action against Sorenson had been dismissed with prejudice under the stipulation with Crane Creek. Crane Creek Ranch, Inc. v. Cresap, 2004 MT 351, 324 M 366, 103 P3d 535 (2004). See also Redies v. Attorneys Liability Protection Soc'y, 2007 MT 9, 335 M 233, 150 P3d 930 (2007).

Joint and Several Liability — Corporations Owned by Same Person Acting as Agent: Lloyd Kimble was president of Hobble Diamond Cattle Company (Hobble) and Kimble Properties, Inc. (Kimble Properties), making him an agent of both companies. Hobble sold land to the buyers, and Kimble Properties sold them an irrigation system. The irrigation system was deficient, and part of the land lay in an old river channel. The buyers sued Kimble, Hobble, and Kimble Properties. The District Court assessed damages against Kimble and Hobble. On appeal, Kimble argued that Hobble was responsible for fraud, but he personally was not. The Supreme Court held that at the time that Kimble sold the irrigation equipment, which was subsequently damaged by erosion of the land, he was acting as an agent of Kimble Properties, not Hobble, so the District Court erred in assessing damages against Hobble rather than Kimble Properties. However, a principal is liable for wrongs committed by an agent while acting within the scope of employment, and a director or officer is individually liable for false representations, so Kimble was personally liable regardless of which of his companies was also liable. H-D Irrigating, Inc. v. Kimble Properties, Inc., 2000 MT 212, 301 M 34, 8 P3d 95, 57 St. Rep. 832 (2000).

Respondeat Superior Applicable Only to Agent Acting Within Scope of Duty: The District Court correctly held that defendant employer was not vicariously liable for the negligent activity of an employee who was involved in personal, rather than business, activity at the time that the negligence occurred. The principle of respondeat superior applies only to an employee or agent who is acting within the scope of the duties owed to the employer or principal. Gentry v. Douglas Hereford Ranch, Inc., 1998 MT 182, 290 M 126, 962 P2d 1205, 55 St. Rep. 737 (1998). See also Hoffman v. Roehl, 61 M 290, 203 P 349 (1921), and Kornec v. Mike Horse Min. & Mill Co., 120 M 1, 180 P2d 252 (1947).

Employer Held Vicariously Liable for Damages Through Criminal Acts of Employee: The Blacks, who owned and managed a business selling carpet, sued a competitor, Carpet Barn, for damages, alleging that Carpet Barn was liable for damages arising from acts of vandalism committed by Huggins, a Carpet Barn employee. Carpet Barn argued that there was no evidence that the criminal conduct of Huggins was in furtherance of the employer, Carpet Barn. The Supreme Court reviewed the record and pointed out that Huggins met Susan Black through business, Huggins discussed the Blacks with the owner of Carpet Barn, some of the acts of vandalism occurred during Carpet Barn's business hours, and Huggins understood that his acts could harm the Blacks and their business. For these reasons, the Supreme Court affirmed the holding of the District Court. Rocky Mtn. Enterprises, Inc. v. Pierce Flooring, 286 M 282, 951 P2d 1326, 54 St. Rep. 1410 (1997).

Assault on Third Person:

Roberts was injured by an explosion caused by a passing truck and sued several mining employers, relying upon respondeat superior. The Supreme Court held that workers' compensation cases were inapplicable. Citing Kornec v. Mike Horse Min. Co., 120 M 1, 180 P2d 252 (1947), the Supreme Court also held that because the employer did not authorize or derive benefit from the assault, respondeat superior did not apply. The Supreme Court also noted that the defendants had no duty to provide security on the road where the assault happened. Roberts v. Pegasus Gold Corp., 273 M 266, 903 P2d 782, 52 St. Rep. 967 (1995).

When a servant in carrying out his assigned duties makes an assault on a third person as a result of a quarrel which arose as a consequence of his performance of the task imposed and at the time and place of performance of the duties he was employed to perform, then the master is liable. Kornec v. Mike Horse Min. & Mill. Co., 120 M 1, 180 P2d 252 (1947), followed in Roberts v. Pegasus Gold Corp., 273 M 266, 903 P2d 782, 52 St. Rep. 967 (1995).

Where controversy between plaintiff and defendant mining company was of long standing concerning right of latter to maintain dam and plaintiff had threatened workers at dam on a previous occasion, the company might reasonably have comprehended that servant sent to repair dam might become involved in altercation with plaintiff and servant assaulted plaintiff at the dam, whether servant in so doing was acting within scope of employment was for jury. Kornec v. Mike Horse Min. & Mill. Co., 120 M 1, 180 P2d 252 (1947), followed in Roberts v. Pegasus Gold Corp., 273 M 266, 903 P2d 782, 52 St. Rep. 967 (1995).

Act Within Scope of Employment and Authority — Summary Judgment Improper: Cloutier arranged to have a pickup truck owned by State Medical Oxygen & Supply, a company of which he was an officer and director, used to haul mattresses and employees of Cay Enterprises, a company of which he was also an officer and director. A Cay Enterprises employee who was injured in the move sought damages from State Medical Oxygen & Supply, alleging negligence in supplying the vehicle. The District Court dismissed the claim by summary judgment, improperly applying Restatement (Second) of Torts 390 (1965), which deals with supplying a chattel to a person incompetent to use it safely. The more proper application was Restatement (Second) of Torts 308 (1965), which deals with the use of a thing or engaging in an activity under the control of an actor if the actor knows that the use or activity might create an unreasonable risk of harm to others. Cloutier was operating within the course and scope of his employment with both companies, thus his knowledge as agent was imputed to the company as principal. That knowledge was a question of fact to be determined by a trier of fact. Summary judgment was improper given that issues of negligence remained to be decided. Williams v. St. Medical Oxygen & Supply, Inc., 265 M 111, 874 P2d 1225, 51 St. Rep. 458 (1994).

Limited Application of Nondelegable Duty Exception to Respondeat Superior Doctrine: Application of the nondelegable duty exception to the respondeat superior doctrine is limited to instances of safety in which the subject matter is inherently dangerous. The Supreme Court declined to modify the presently accepted version of the doctrine by adopting the exception, set out in section 214 of Restatement (Second) of Agency, that a master or other principal who is under a duty to provide protection for or to have care used to protect others or their property and who confides the performance or duty to a servant or other person is subject to liability to others for harm caused to them by the failure of the agent to perform the duty. Noting that there are several reasons for and against extending the liability of an employer when an intentional tort is committed only because or by virtue of the employment situation, the court opted to leave adoption of such a major doctrinal change to the Legislature. Maguire v. St., 254 M 178, 835 P2d 755, 49 St. Rep. 688 (1992), followed in Estate of Strever v. Cline, 278 M 165, 924 P2d 666, 53 St. Rep. 576 (1996).

State's Duty to Provide Institutional Care: The state has a duty under 53-20-142, not inconsistent with the theories of negligent hiring, negligent supervision, and agency, to provide proper care for persons admitted to a residential facility, and it was error for the District Court to refuse to instruct on those theories in a case in which that statutory duty was called into question. Maguire v. St., 254 M 178, 835 P2d 755, 49 St. Rep. 688 (1992).

Punitive Damages Not Contingent Upon Showing of Malice on Principal's Part: Defendant, Lake, argued that proving that he had ratified his agent's acts made him liable only for compensatory damages unless the plaintiff proved malice on his part. The Supreme Court held that this section does not limit liability to wrongs other than intentional and malicious acts resulting in an award of punitive damages. Daniels v. Dean, 253 M 465, 833 P2d 1078, 49 St. Rep. 535 (1992).

Neither School nor Adviser Owed Duty to Student Injured in Extracurricular Activity During Summer: The plaintiff, a high school student, sustained injuries while attending a privately sponsored summer cheerleading clinic. She sued her high school district as the party responsible for its students during extracurricular activities and as principal of its agent, the cheerleading adviser, for negligent supervision. In the plaintiff's appeal of summary judgment in favor of the school district, the Supreme Court held that a school does not owe a duty to a student for an extracurricular activity during the summer months when the activity is governed by independent parties. The cheerleading adviser's participation was too limited to owe a duty as a supervisor, and she was not acting as the school's agent. Rollins v. Blair, 235 M 343, 767 P2d 328, 46 St. Rep. 39 (1989).

Negligent Hiring and Negligent Entrustment: Insurer's agent participated in a Dillon rodeo, went to a barbecue at his Dillon home, and then went drinking in Dillon bars. While driving home in a vehicle he leased from a service company that was a wholly owned subsidiary of and had a common board of directors with insurer, he struck plaintiff, who sued insurer for negligent hiring and service company for negligent entrustment of the vehicle to agent. Insurer and service company sought summary judgment. That one to whom a vehicle is entrusted is licensed does not alone negate a finding of negligent entrustment. Since the record showed agent had at least once before been in an accident while intoxicated and it was alleged service company knew or should have known the agent had a propensity to drive while intoxicated, there was a material question of fact whether service company breached the duty not to entrust a vehicle to an incompetent driver, and summary judgment as to the service company was denied. Insurer's motion for summary judgment on the negligent hiring issue was denied, the court stating that it could find no Montana case on the negligent hiring doctrine. The questions of whether insurer should have foreseen that it was hiring a dangerous driver, that it was negligent in hiring the agent, and that the negligence proximately caused plaintiff's injuries were considered to be questions of fact not properly disposed of on summary judgment. The court also indicated that whether agent was acting within the scope of his employment at the time of the accident was not an issue. Vollmer v. Bramlette, 594 F. Supp. 243, 41 St. Rep. 1964 (D.C. Mont. 1984).

Respondeat Superior — Accident Caused by Insurance Agent: Defendant insurance company's agent participated in a Dillon rodeo, went to a barbecue at his Dillon home, and in the evening consumed alcohol at several Dillon bars. On the way home from the bars, he struck plaintiff while driving an auto the agent leased from insurer's wholly owned service company, which had a common board of directors with insurer. Plaintiff sued defendants under respondeat superior. There was evidence agent sold insurance as a result of participating in group recreational and social activities. Summary judgment for insurer was refused because there was a fact question as to whether agent's activities during the night in question were within the course and scope of his work as an insurance agent. However, summary judgment was granted in favor of the service company as there was no evidence that agent was acting as the agent of the service company at the time of the accident. Vollmer v. Bramlette, 594 F. Supp. 243, 41 St. Rep. 1964 (D.C. Mont. 1984).

Independent Investigation Clause Not to Preclude Justifiable Reliance on Representations: Defendants owned property in Flathead County. Water for the property came from a neighbor's well for which they paid him $8 per month. No written agreement existed concerning the water supply. Defendants listed the property for sale with Tri-City Real Estate. Inserted in the listing contract in the printed space following "water" were the words "community $8/mo." Plaintiffs were interested in the land and looked at it. They asked both defendants and the realtor about the water supply and were told it came from a community well. Plaintiffs wanted written verification of the interest in the water system. The realtor told them he would obtain a copy of the register of the well for them. Plaintiffs continued asking for the register but never received it. Plaintiffs signed a contract for deed to buy the property which had been prepared by the realtor's attorney. The contract contained an "independent investigation" clause, which stated that plaintiffs had investigated the property and entered the contract based upon that investigation and that there were no other agreements or representations concerning the property. The neighbor stopped supplying water, and plaintiffs were forced to dig their own well. They sought recovery from defendants. It was held that defendants were responsible for the negligence of their agents in the sale as related to the community water interest. The Supreme Court held that the "independent investigation" clause did not preclude a holding that the plaintiffs justifiably relied on the representations of the realtor. Parkhill v. Fuselier, 194 M 415, 632 P2d 1132, 38 St. Rep. 1424 (1981), followed in Wagner v. Cutler, 232 M 332, 757 P2d 779, 45 St. Rep. 1092 (1988).

Principal Responsible — Agent Involved in Business of Agency: A principal is responsible for the negligence of the agent if the negligence of the agent is involved in the transaction of the business of the agency. Stewart v. Casey, 182 M 185, 595 P2d 1176 (1979).

Demonstration Automobile Used by Salesman in Personal Business: Where an automobile salesman was given use of a demonstrator automobile and was engaged in personal business, the benefit to the dealership of exposure of the automobile to the public was insufficient to warrant holding the dealership responsible for the employee's negligent operation of the vehicle. State ex rel. City Motor Co. v. District Court, 166 M 52, 530 P2d 486 (1975).

Good Faith: The bank contended that because its agency status was special or limited in nature it bore no fiduciary responsibility to defendant. The court held that in all transactions concerning or affecting the subject matter of the agency relationship, it is the duty of the agent to act with utmost good faith and loyalty for the furtherance of the principal's interest. First Nat'l Bank v. Sant, 161 M 376, 506 P2d 835 (1973).

Drunken Driver: United States was not liable for damages occasioned by the negligent driving by an army driver where such driver, in disobedience of his orders, went out of his way to a tavern where he drank, and then while driving an army vehicle back to base became involved in an accident. The deviation from the master's business and orders was so great as to show that the driver was on his own mission. St. Paul Fire & Marine Ins. Co. v. U.S., 116 F. Supp. 51 (D.C. Mont. 1953).

Malicious Acts of Servant: Under the general rule that a master is liable for the torts of his servants if committed within the scope of his employment, willful and malicious acts of the servant are imputable to the master. Kornec v. Mike Horse Min. & Mill. Co., 120 M 1, 180 P2d 252 (1947), followed in Roberts v. Pegasus Gold Corp., 273 M 266, 903 P2d 782, 52 St. Rep. 967 (1995).

When Acting in Scope of Employment Presumed: In an action to recover damages for personal injuries suffered in an automobile collision caused by the negligence of the driver of the car, employed by a motor company as a salesman of secondhand cars working on a commission basis, the rebuttable presumption is that, where the ownership of the car is established and that the driver was in the employ of the owner, the driver was at the time acting within the scope of his employment. Eliason v. Geil, 114 M 97, 132 P2d 158 (1942).

Doctrine of Respondeat Superior: Where, in an action for slander brought by a customer of a chain store who was charged by the manager thereof with passing a bad check, obtaining change, and ordering a sack of flour sent to an address where there was no house, the rule is that the wrongs for which liability attaches to the principal include not only acts of negligence, but malicious, wanton, and willful acts as well, and the agent's deviation from express instructions or even act in utter disobedience thereof does not generally relieve the principal if the acts were in furtherance of or incidental to the agent's employment. Keller v. Safeway Stores, Inc., 111 M 28, 108 P2d 605 (1940).

Customer Tripping Over Crate: In action against foreign corporation and its resident employee, who was joined as John Doe, was not served with process, and did not appear, for injuries sustained by customer who tripped over orange crate which had been allegedly placed in aisle of corporation's store by employee, the test for removal of cause to federal court on diversity of citizenship was whether employee had any real connection with controversy; a resident citizen properly joined is not merely a nominal party who can be ignored because not served or has not appeared; it was held that corporation was not entitled to have action removed on ground of diversity of citizenship. Jensen v. Safeway Stores, Inc., 24 F. Supp. 585 (D.C. Mont. 1938).

Responsibility of Principal for Agent's Wrongs: Under this section where an employer is sought to be held responsible under the doctrine of respondeat superior, the decisive question is whether the agent or employee was acting within the scope of his employment. If he was acting independently of his employer or while on a mission of his own, the employer may not be held accountable in damages. Meinecke v. Intermountain Transp. Co., 101 M 315, 55 P2d 680 (1936).

Demonstration of Car: Where an automobile dealer's chauffeur was demonstrating a car for his employer and permitted the prospective buyer's daughter to drive the car and the girl lost control of the car, and the chauffeur then took hold of the wheel and steered the car upon the sidewalk striking a pedestrian, the chauffeur was acting within the scope of his employment and the employer was liable for the injuries suffered by the pedestrian. Hoffman v. Roehl, 61 M 290, 203 P 349, 20 ALR 189 (1921).

Law Review Articles

Liability of County for Tortious Conduct of Officers and Employees, Kline, 3 Mont. L. Rev. 128 (1942).

Principal's Liability for Slander by Agent, Angstman, 3 Mont. L. Rev. 75 (1942).

28-10-603. When instrument binds principal.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Obligation to Refund Payment for Gas Field Option: Plaintiff corporation rescinded a gas field option upon which it had paid $50,000 to defendant. After defendant failed to refund money due, plaintiff filed suit and was granted summary judgment for $71,320.55. On appeal, the Supreme Court held that, based upon the exhibits, affidavits, and briefs before the lower court, there was no evidence of a genuine issue of material fact. The escrow agreement and release based upon plaintiff's rescission were supported by adequate consideration since release from contract obligations and forbearance to sue are both adequate consideration. Ayers Oil and Gas, Inc., was a party to both the option and the release agreements as evidenced by Ayers' signature as president. Devon Oil & Gas Co., Inc. v. Ayers, 218 M 223, 707 P2d 523, 42 St. Rep. 1536 (1985).

Business Correspondence: Where the evidence showed that it was the intention of the president of a corporation the stock of which, with the exception of three shares for which the holders paid nothing, was owned by himself, to bind the company by letters written by him personally and relied on by plaintiff, it became bound as fully as if a formal contract had thereafter been executed in his name. Edwards v. Plains Light & Water Co., 49 M 535, 143 P 962 (1914).

28-10-604. When notice to principal or agent is notice to the other.

Case Notes

Parol Evidence of Circumstances Under Which Bid Prepared Proper in Interpreting Uncertain Contract Provisions: Bid estimates on a road building project contained vague and ambiguous project requirements, and testimony at trial regarding the height of the finished road was conflicting. Thus, the District Court, in interpreting provisions of the contract that appeared ambiguous or uncertain, properly considered parol evidence of the circumstances under which the bid was prepared. The court found more credible the contractor's testimony that there was not agreement that a subroad would be constructed of pit run gravel 6 inches above field grade, and that determination was affirmed on appeal. DeNiro v. Gasvoda, 1999 MT 129, 294 M 478, 982 P2d 1002, 56 St. Rep. 521 (1999).

Consulting Physician Diagnosis and Notice to Counsel Binding on Plaintiff — Late Claim Properly Dismissed: In 1992, after consulting with several medical doctors, Kaeding hired Baiz as his attorney to pursue a claim for damages from asbestosis against his employer, W.R. Grace & Co. (Grace). Baiz employed Whitehouse as a consulting physician, and Whitehouse, after reviewing several x-rays, sent Baiz a letter stating that the appearance of the x-rays was consistent with asbestosis. In 1996, Kaeding filed suit against Grace, alleging Grace caused his medical condition. After dismissal of the suit by the District Court for failure to commence the action within the statute of limitations, the Supreme Court, distinguishing Hando v. PPG Indus., Inc., 236 M 493, 771 P2d 956 (1989), in which a diagnosis confirming the plaintiff's suspicions as to her medical condition was not received for some time, held that Kaeding had at least a preliminary diagnosis of asbestosis as early as 1983, when Grace sent Kaeding the results of a breathing test. Although Kaeding argued that he was unaware of the contents of the letter sent to Baiz by Dr. Whitehouse, the Supreme Court concluded that because the employment of an attorney creates an agency relationship between the attorney and the attorney's client, Kaeding knew or should have known no later than the time of Dr. Whitehouse's letter to Baiz that he, Kaeding, had contracted asbestosis. Because suit was not brought within the time required by the statute of limitations after the letter from Dr. Whitehouse, the District Court had properly dismissed the claim. Kaeding v. W.R. Grace & Co., 1998 MT 160, 289 M 343, 961 P2d 1256, 55 St. Rep. 640 (1998), followed in Chriske v. State ex rel. Dept. of Corrections, 2010 MT 149, 357 Mont. 28, 235 P.3d 588.

Act Within Scope of Employment and Authority — Summary Judgment Improper: Cloutier arranged to have a pickup truck owned by State Medical Oxygen & Supply, a company of which he was an officer and director, used to haul mattresses and employees of Cay Enterprises, a company of which he was also an officer and director. A Cay Enterprises employee who was injured in the move sought damages from State Medical Oxygen & Supply, alleging negligence in supplying the vehicle. The District Court dismissed the claim by summary judgment, improperly applying Restatement (Second) of Torts 390 (1965), which deals with supplying a chattel to a person incompetent to use it safely. The more proper application was Restatement (Second) of Torts 308 (1965), which deals with the use of a thing or engaging in an activity under the control of an actor if the actor knows that the use or activity might create an unreasonable risk of harm to others. Cloutier was operating within the course and scope of his employment with both companies, thus his knowledge as agent was imputed to the company as principal. That knowledge was a question of fact to be determined by a trier of fact. Summary judgment was improper given that issues of negligence remained to be decided. Williams v. St. Medical Oxygen & Supply, Inc., 265 M 111, 874 P2d 1225, 51 St. Rep. 458 (1994), followed, as to knowledge of the agent imputed to the principal, in Kaeding v. W.R. Grace & Co., 1998 MT 160, 289 M 343, 961 P2d 1256, 55 St. Rep. 640 (1998).

Imputed Notice of False Representations — No Reliance in Claiming Fraud: The District Court held that the first mortgagee, Aetna Life Insurance Company (Aetna), had defrauded the second mortgagee, Shepherds, ruling that Shepherds did not have notice imputed to them through Ranch Mart, a realty agency employed by Shepherds to sell a ranch, and that even if Shepherds had such notice, it would not "serve as a shield for unfair dealing" by Aetna. On appeal, the Supreme Court found that Ranch Mart had notice of the size of the Aetna loan and resulting first mortgage before consummation of the sale, and therefore, under 28-10-604, Shepherds had notice imputed to them. Further, the court held that since the means were at hand for Shepherds to ascertain the truth of the false representations, they could not, as a matter of law, rely on those representations in claiming fraud. Aetna Life Ins. Co. v. McElvain, 221 M 138, 717 P2d 1081, 43 St. Rep. 697 (1986).

Notice of On-Job Injury Through Employer's Agent, a Physician: Employer, a hospital, in a suit to recover workers' compensation benefits may be considered to have actual notice within the meaning of 39-71-603 when claimant, a nurse in the hospital, sought and was given treatment by a physician in the emergency room. The physician is an agent under 28-10-103, and the hospital may be considered to have notice under this section. The purpose of the notice requirement is to enable the employer to protect himself by prompt investigation of the claimed accident and prompt treatment of the injury involved with a view toward minimizing its effects by proper medical care. Where, as here, within 2 hours of the accident, the employer had notice and a diagnosis and its managing agent had prescribed treatment for the injury, the purpose of 39-71-603 is fulfilled. Harmon v. Deaconess Hosp., 191 M 285, 623 P2d 1372, 38 St. Rep 65 (1981).

Intent of Contracting Parties — Parol Evidence Admissible to Show Knowledge of Agent: In an action by the plaintiff contractor against the defendant motor carrier for breach of contract caused by the defendant's refusal to haul fabricated silo sections, the court did not err in finding that a memorandum of the agreement by the defendant's employee was sufficiently clear to form a valid contract. Parol evidence is admissible to apply the memorandum to the subject matter of the contract. The evidence showed that agents of the defendant knew the subject matter of the contract and that knowledge is imputed to the defendant and will be applied to the memorandum to determine the intent of the defendant as to the subject matter of the contract. Empire Steel Mfg. Co. v. Carlson, 191 M 189, 622 P2d 1016, 38 St. Rep. 101 (1981).

Notice or Knowledge of Attorney of Criminal Trial Date Not Conclusive as to Notice or Knowledge of Client in Criminal Prosecution: In the defendant's trial on a charge of bail-jumping, the jury was instructed that notice to an attorney of a trial date is notice to the client employing him and knowledge of an attorney is knowledge of his client. The Supreme Court found that this instruction had the effect of relieving the State of its burden to prove the mental state of the defendant. The case was remanded to the District Court. St. v. Blackbird, 187 M 270, 609 P2d 708 (1980), distinguished in St. v. Wereman, 273 M 245, 902 P2d 1009, 52 St. Rep. 958 (1995).

Insolvent Bank — Notice to Attorney: The Columbus State Bank became insolvent. Attorneys for plaintiff filed a claim with the Superintendent of Banks on some promissory notes. The Superintendent notified the attorneys that the claim would not receive preference. Challenge to the Superintendent's ruling was not brought within the statutory period. Plaintiff claimed it had not received notice. The Supreme Court said the general rule is that notice to an agent as to matters within the scope of his business is notice to the principal. The relation of attorney and client is one of agency. The attorneys were clearly agents acting on the matter of the claim, so that notice was sufficient. Caterpillar Tractor Co. v. Johnson, 99 M 269, 43 P2d 670 (1935).

Waiver of Condition: Where the agent of a fire insurance company knew before writing a policy that the property in question was mortgaged and that foreclosure proceedings were pending, and thereafter knew of its sale and that the insured was to remain in possession during the period of redemption, and upon inquiry by the latter assured him that the policy was all right without an endorsement relative to the sale, his knowledge was imputable to his principal and in an action on the policy to recover for loss under it the insurer must be held to have waived the condition relative to change of title without its consent. Baker v. Union Assurance Soc'y of London, Ltd., 81 M 281, 264 P 132 (1928).

Sale of Land: Where the agency of one who was instrumental in making a sale of land was admitted by the seller (plaintiff), who made no contention that it had ever been terminated, the evidence on the contrary showing that such agent continued making sales of land for his principal in the same vicinity, the presumption obtains that the agency was still in being at a time thereafter when defendant notified the agent to so construct a ditch that water could be brought upon the land as agreed in the contract, and written notice to the agent was notice to the principal. Healy v. Ginoff, 69 M 116, 220 P 539 (1923).

Assignment for Benefit of Creditors: Under this section, plaintiff corporation must be considered to have had notice of the facts known to its manager in entering into an agreement whereby its debtor was released from liabilities by his assignment for the benefit of creditors, and its voluntary acceptance of the benefits of the transactions was equivalent to a consent to it. Stone-Ordean-Wells Co. v. Anderson, 66 M 64, 212 P 853 (1923).

Redemption of Property: One who joins through an agent, in the redemption of property sold at a judicial sale, is charged with all the knowledge that the agent possesses concerning the matter. Coombs v. Barker, 31 M 526, 79 P 1 (1905).

Law Review Articles

Apparent Agent, Notice of Industrial Accident, Thompson, 22 Mont. L. Rev. 199 (1961).

28-10-605. Extent to which principal bound when agent exceeds authority.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

28-10-606. Extent to which principal bound by acts under ostensible authority.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Binding Agreement: Where grain bins were returned to wholesale agency with the knowledge and apparent approval of the manufacturer, manufacturer could not later repudiate the agreement and hold retailer liable for the purchase price. Butler Mfg. Co. v. J & L Implement Co., 167 M 519, 540 P2d 962 (1975).

Notice of Repudiation: Reasonable promptness of the disavowal of ostensible agency was an open question of fact where representatives of the manufacturer were present when wholesale agent arranged with retailer for return of merchandise, but manufacturer did not repudiate agreement until retailer requested credit. Butler Mfg. Co. v. J & L Implement Co., 167 M 519, 540 P2d 962 (1975).

Service Upon Corporation: The doctrine of ostensible agency appears to have no application when it becomes involved with the question whether service of process has been legally made upon a "managing or general agent". Further service upon a former employee of a company was not service upon the company itself and default judgment was vacated and set aside. Kraus v. Treasure Belt Min. Co., 146 M 432, 408 P2d 151 (1965).

Permissive Use of Vehicle by Employee: The mere permissive use by a truck driver of his employer's truck for personal purposes did not make the owner of the truck liable for the driver's negligence under the doctrine of ostensible authority. Searle v. Great N. Ry., 189 F. Supp. 423 (D.C. Mont. 1960).

28-10-608. Rights of person who deals with agent without knowledge of agency.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Description of Property — Filing of Lien as Notice to Third Parties: On September 27, 1977, plaintiff Mountain States Resources, Inc. (MSR) contracted with defendant to have him furnish and erect three steel buildings to be used in connection with the Gypsy-Highview Gathering System (GHGS) for natural gas. Monte Grand Exploration, Inc. (MGE) was an undisclosed principal of MSR. The buildings were completed, and at the request of MSR's supervisory agent, flashing was installed on two buildings, which flashing was not called for in the contract. On January 18, 1978, MSR paid the contract but refused to pay for the additional flashing. On March 8, 1978, defendant filed a lien against the proceeds of any gas MSR sold to Montana Power Company. MSR sued to set aside the lien and to recover for slander of title. Defendant joined MGE and sought to foreclose the lien. MSR claims that one of the leases listed as belonging to MSR actually belonged to MGE, and the lien therefore contained an improper description of the property and is invalid. MSR was the agent and project manager of the building project and is therefore liable to defendant. MGE was an undisclosed principal in the construction project and is therefore also liable. Regardless of which corporation held title at the time of the lien, filing the lien would give notice of the existence of the lien to interested third parties. As the successor in interest to MSR and MGE, GHGS had notice and was liable. The description was adequate to properly identify the property subject to the lien; consequently, the description and the lien are valid. Mtn. States Resources, Inc. v. Ehlert, 195 M 496, 636 P2d 868, 38 St. Rep. 2061 (1981).

Naming Undisclosed Principal in Original Lien: On September 27, 1977, plaintiff Mountain States Resources, Inc. (MSR) contracted with defendant to have him furnish and erect three steel buildings to be used in connection with the Gypsy-Highview Gathering System (GHGS) for natural gas. Monte Grand Exploration, Inc. (MGE) was an undisclosed principal of MSR. The buildings were completed, and at the request of MSR's supervisory agent, flashing was installed on two buildings, which flashing was not called for in the contract. On January 18, 1978, MSR paid the contract but refused to pay for the additional flashing. On March 8, 1978, defendant filed a lien against the proceeds of any gas MSR sold to Montana Power Company. MSR sued to set aside the lien and to recover for slander of title. Defendant joined MGE and sought to foreclose the lien. MGE contended the lien against it was invalid because it was not named in the original lien. MGE was not named in the lien as required by 71-3-1002, but the District Court found that there was an agent-undisclosed principal relationship between MSR and MGE. Defendant was unaware of this relationship until after he filed the lien. Consequently, defendant joined MGE in the suit when he filed his answer and counterclaim. The lien was valid. Mtn. States Resources, Inc. v. Ehlert, 195 M 496, 636 P2d 868, 38 St. Rep. 2061 (1981).

Oil and Gas Lien as Extending to Leaseholds of Undisclosed Principal: On September 27, 1977, plaintiff Mountain States Resources, Inc. (MSR) contracted with defendant to have him furnish and erect three steel buildings to be used in connection with the Gypsy-Highview Gathering System (GHGS) for natural gas. Monte Grand Exploration, Inc. (MGE) was an undisclosed principal of MSR. The buildings were completed, and at the request of MSR's supervisory agent, flashing was installed on two buildings, which flashing was not called for in the contract. On January 18, 1978, MSR paid the contract but refused to pay for the additional flashing. On March 8, 1978, defendant filed a lien against the proceeds of any gas MSR sold to Montana Power Company. MSR sued to set aside the lien and to recover for slander of title. Defendant joined MGE and sought to foreclose the lien. MSR contended the lien on the gathering system did not entitle him to a lien on the leaseholds served by the system. MSR claimed that MSR and MGE, which own the gas leases, are completely independent of GHGS, which owns the gathering system. Defendant contracted with MSR, and MSR served as agent and project manager for the building project. MGE was an undisclosed principal in the building project. GHGS was not an independent entity until after construction of the buildings started and did not obtain a lease for the land on which the buildings sit until after the lien was filed. Defendant contracted with MSR and MGE, and his lien extended to their leases and GHGS. Mtn. States Resources, Inc. v. Ehlert, 195 M 496, 636 P2d 868, 38 St. Rep. 2061 (1981).

Undisclosed Principal — Liability: DeMars entered a contract to sell land to Williams. Williams was acting as agent for defendant and assigned the contract to her. Williams' interest in the contract was attached for a debt. Plaintiff purchased Williams' interest in the land at a sheriff's sale. Plaintiff then brought an ejectment action, contending defendant was a principal for Williams in the land purchase. The Supreme Court quoted section 89 of Pomeroy on contracts, saying: "When the agreement is executed by the agent in his own name, he appearing to be the contracting party, the requisite as to party is complied with. The principal may maintain a suit and enforce the contract, and it is immaterial whether a principal is actually known during the transaction, or whether the other party supposes that he was dealing with the agent personally, entirely on his own behalf. Under the same circumstances, it is now the rule that a suit may be maintained, and the contract enforced against the principal, even though his name nowhere appears on the face of the writing, and even though he was undisclosed and unknown to the other party at the time of entering into the agreement, provided, of course, it was actually made on his behalf." Ejectment was improper, however, as plaintiff had no greater rights than DeMars and the contract was still being performed. Prosper v. Smith, 67 M 308, 215 P 649 (1923).

28-10-609. Principal's liability when agent given exclusive credit.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

Case Notes

Mechanics' Lien (Now Construction Lien): Even assuming that a contractor making real estate improvements was acting as the agent of the property owner in purchasing material for the improvement, this section does not apply so as to require any notice from the materialman to the property owner, other than that required by the mechanics' lien (now construction lien) law, to perfect a materialmen's lien. Monarch Lumber Co. v. Haggard, 139 M 105, 360 P2d 794 (1961).

Part 7
Agent's Responsibility to Third Persons

Part Case Notes

Business Relationship — Sufficient Notice of Agency — Identity of Principal — Agent Not Personally Liable: The longstanding business relationship between the parties provided sufficient notice to the third party to relieve the agent of any personal liability under a contract when the contract's signature line did not specify that the agent was signing as an agent. Empire Office Mach., Inc. v. Aspen Trails Assoc. LLC, 2014 MT 94, 374 Mont. 421, 322 P.3d 424.

Existence of Agency Not Disclosed — Agent Personally Liable: Rhines, an agent of Sound West, entered into an employment contract with Como but then breached the contract. Como brought suit against Rhines and later added Sound West. The Supreme Court affirmed the judgment of the District Court holding Rhines personally liable. In the absence of evidence of a disclosure that Rhines was acting as an agent of Sound West at the time the contract was entered into, the agent is personally liable. Como v. Rhines, 198 M 279, 645 P2d 948, 39 St. Rep. 932 (1982).

28-10-701. Warranty of authority.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Motion to Dismiss a Complaint for Failure to State a Claim in the Face of a Specific Statute: Applying the rule that a complaint should not be dismissed for failure to state a claim unless it appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief, a motion to dismiss a complaint for failure to state a claim was proper where third party plaintiff knew that third party defendant was an agent and that credit was not extended to him personally as 28-10-702 specifies credit must be given to the agent personally to hold him responsible to third persons as a principal. Hasbrouck v. Krsul, 168 M 270, 541 P2d 1197 (1975).

28-10-702. When agent responsible to third persons as principal.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Agent Not Liable for Bills of Identified Principal: The plaintiff sued an agent for the unpaid bills of an identified principal. The District Court ruled on cross-motions that the agent was not liable. The Supreme Court affirmed, finding that the agent had not agreed to be bound to pay bills of the identified principal. Big Sky Civil & Envtl., Inc. v. Dunlavy, 2018 MT 236, 393 Mont. 30, 429 P.3d 258.

Sufficient Evidence to Sustain Claims Against Individual Defendants Acting as Corporate Agents: Plaintiffs presented claims for breach of contract, bad faith breach of contract, tortious interference with contract, abuse of process, and malicious prosecution against defendant corporation and against individual members of the corporation. The individual members moved for their dismissal from the case on grounds that as employees and officers of the corporation they could not be held personally liable for the acts of the corporation. The District Court denied dismissal, and on appeal the Supreme Court affirmed. Review of the record demonstrated that there was sufficient evidence to submit plaintiffs' claims of tortious interference with contract, abuse of process, and malicious prosecution against the individual members. From this evidence the jury could have concluded that the individual members' conduct was tortious and was directed at plaintiffs or that the evidence did not support that conclusion, but in either case the evidence was sufficient to survive the dismissal motion. The fact that the jury found the individual members not liable for tortious interference with contract or punitive damages showed that the jury did not simply lump the individual members in with the acts of the corporate defendant, but instead individually considered the individual members' actions in relation to each claim based on the evidence. The Supreme Court declined to disturb the jury's conclusions. Ammondson v. NW. Corp., 2009 MT 331, 353 M 28, 220 P3d 1 (2009).

Attorney Agent Acting Within Scope of Employment Responsible to Principal and Not Third Party for Actions: Attorney Cresap was employed by Sorenson to prepare auction instructions for the sale of Sorenson's real property. The bidding instructions prepared by Cresap stated that Sorenson could reject all bids below $270,000 but did not disclose that that amount was the minimum acceptable price for the property. Crane Creek Ranch (Crane Creek) bid $248,000 on the property, was outbid by the Goss brothers, and was told that it could not raise its bid because it failed to meet the minimum bid of $270,000. After failing to purchase the property, Crane Creek sued Cresap and Sorenson for specific performance, fraud, negligent misrepresentation, and deceit, and after the District Court held for Cresap, the claims against Sorenson were stipulated to be dismissed with prejudice. The Supreme Court held that the District Court properly granted summary judgment for Cresap on all counts of the complaint. The Supreme Court held that Cresap was known to Crane Creek as acting as Sorenson's attorney and, in that capacity and in accordance with Smith v. Fladstol, 248 M 18, 807 P2d 1361 (1991), and Rhode v. Adams, 1998 MT 73, 288 M 278, 957 P2d 1124 (1998), Cresap's duty of care ran to his principal, Sorenson, and not to any unrelated third party, such as Crane Creek. Any negligence on the part of Cresap is imputed to his principal, and any legal action against Cresap for actions taken by him within the scope of his agency employment must instead be brought against Cresap's principal, Sorenson. However, as the Supreme Court observed, the cause of action against Sorenson had been dismissed with prejudice under the stipulation with Crane Creek. Crane Creek Ranch, Inc. v. Cresap, 2004 MT 351, 324 M 366, 103 P3d 535 (2004). See also Redies v. Attorneys Liability Protection Soc'y, 2007 MT 9, 335 M 233, 150 P3d 930 (2007).

Joint and Several Liability — Corporations Owned by Same Person Acting as Agent: Lloyd Kimble was president of Hobble Diamond Cattle Company (Hobble) and Kimble Properties, Inc. (Kimble Properties), making him an agent of both companies. Hobble sold land to the buyers, and Kimble Properties sold them an irrigation system. The irrigation system was deficient, and part of the land lay in an old river channel. The buyers sued Kimble, Hobble, and Kimble Properties. The District Court assessed damages against Kimble and Hobble. On appeal, Kimble argued that Hobble was responsible for fraud, but he personally was not. The Supreme Court held that at the time that Kimble sold the irrigation equipment, which was subsequently damaged by erosion of the land, he was acting as an agent of Kimble Properties, not Hobble, so the District Court erred in assessing damages against Hobble rather than Kimble Properties. However, a principal is liable for wrongs committed by an agent while acting within the scope of employment, and a director or officer is individually liable for false representations, so Kimble was personally liable regardless of which of his companies was also liable. H-D Irrigating, Inc. v. Kimble Properties, Inc., 2000 MT 212, 301 M 34, 8 P3d 95, 57 St. Rep. 832 (2000).

Ambiguity in Insurance Policy as to Submission of Claims Resolved in Favor of Insured: Golt worked as a civilian employee of the Army and Air Force Exchange Service (AAFES) until he was discharged from employment in 1994 for cause. Thirty days after termination, Golt died of carbon monoxide poisoning. As a benefit of employment, Golt was covered by an accident insurance policy issued by General American Life Insurance Company (General) and also by Aetna Life Insurance Company (Aetna) under a group life and accident and health insurance policy. AAFES transmitted the Aetna claim, but did not transmit the General claim. A subsequent request for benefits from General was denied because the claim was not submitted within 20 days after the covered loss occurred. Golt's wife asserted that by tendering the claim to AAFES within the 20-day period, she satisfied the notice requirements of the General policy, while General contended that the policy plainly informed both Mrs. Golt and her attorneys that notice of claim and proof of loss were to be sent to the National Accident Insurance Underwriters (NAIU) or one of General's agents and that AAFES was the policyholder, not a General agent. The Supreme Court held that the notice provision in the policy was ambiguous because it gave an invalid address for NAIU and did not list any acceptable General agents. However, the notice did allow claims to be submitted through the policyholder/employer. For purposes of this case, when accepting or processing claims, AAFES, with the express permission of General, was performing a function of the insurer and was properly considered an agent of the insurer. Mrs. Golt's claim was thus timely submitted. Golt v. Aetna Life Ins. Co., 2000 MT 155, 300 M 142, 2 P3d 841, 57 St. Rep. 613 (2000).

Salesman Personally Liable for Negligent Misrepresentation: Plaintiffs purchased a subdivision parcel from defendant and subsequently contracted with defendant, a sales agent for a home center, to purchase a modular home to be placed on the parcel. Relying on defendant's advice and assurance that the property would be properly prepared, plaintiffs installed the home on concrete piers instead of a full foundation. Upon learning from engineering reports that extensive water damage to the home was caused by foundation instability, plaintiffs filed an action, alleging that the defendant had falsely misrepresented that the land had been properly prepared prior to installation of the home. Affirming the District Court decision, the Supreme Court ruled that the defendant was personally liable for selling property as appropriate for a modular home and for unreasonably representing to plaintiffs that the home was suitable for the pier-type foundation. Williams v. DeVinney, 259 M 354, 856 P2d 546, 50 St. Rep. 831 (1993).

Duty of Insurance Broker With Respect to Insured or Insurer: The insureds asked First National Insurance, Inc., to cancel the policy that First National had obtained for them from Nautilus Insurance Company. First National informed Nautilus of the cancellation, but the policy was to remain in effect for 3 months because of Nautilus's practice of retaining a portion of the paid premium. During that time, the insureds suffered a loss and Nautilus paid the claim. Nautilus then sued First National, alleging that First National as Nautilus's agent had a duty to take additional steps on Nautilus's behalf. The Supreme Court held that there was no duty because the broker acted as agent with respect to an insured and an insurer on the basis of which party requested an action to be taken. In the present case, the insureds had requested the cancellation and the broker was therefore acting on their behalf. Nautilus Ins. Co. v. First Nat'l Ins., Inc., 254 M 296, 837 P2d 409, 49 St. Rep. 802 (1992).

Negligent Misrepresentation — Agent Jointly and Severally Liable: In case relating to the failure of commercial trout farm, trial court refused to hold agent liable with bank for breach of fiduciary duty and fraudulent misrepresentation. Upon appeal, the Supreme Court reversed, holding that an agent cannot be shielded from personal liability upon a finding that the agent was personally negligent or his actions tortious in nature. An agent is jointly and severally liable with his principal to third parties for wrongful acts committed in the course of his agency. Crystal Springs Trout Co. v. First State Bank of Froid, 225 M 122, 732 P2d 819, 44 St. Rep. 90 (1987), followed in Sherner v. Nat'l Loss Control Serv. Corp., 2005 MT 284, 329 M 247, 124 P3d 150 (2005).

Dismissal of Claim Against Agent for Lack of Evidence: In an action for damages arising from sale of a defective modular home, a motion to dismiss corporate seller's president as a party defendant should have been granted where there was no evidence of negligence or other tortious action on his part. He was not present when the home was installed on the foundation, at which time the defects were apparently caused; he had not been made aware of any errors in the installation; he had a representative of the corporation make a service call each time the buyer made a complaint; and there was no evidence that he knew of any negligent construction or participated in the actual construction process. Little v. Grizzly Mfg., 195 M 419, 636 P2d 839, 38 St. Rep. 1994 (1981).

Piercing Corporate Veil Doctrine — Refusal to Apply: The doctrine of piercing the corporate veil to avoid fraud or injustice was not applied in a suit for damages arising from defects in a modular home manufactured and installed by defendant where there was no evidence that the corporation was defectively formed or formed to avoid personal liability on the part of the officers. Little v. Grizzly Mfg., 195 M 419, 636 P2d 839, 38 St. Rep. 1994 (1981).

Public Policy Against Personal Liability of Agent: As a matter of public policy, the officers and agents of a corporation must be shielded from personal liability for acts they take on behalf of the corporation in furtherance of corporate goals, policies, and business interests. Little v. Grizzly Mfg., 195 M 419, 636 P2d 839, 38 St. Rep. 1994 (1981).

Liability of Seller for Negligent Misrepresentation by Real Estate Agent — Disclaimer in Contract for Deed: Where the buyers and seller of certain real estate executed a contract for deed containing an acknowledgment that the buyers had inspected the property, were familiar with it, and that no representations concerning the property had been made by anyone on behalf of the seller and the buyers later discovered that the real estate agent had shown them and the buyers had executed a contract for deed on a lot other than the one purportedly sold to the buyers, the acknowledgment of the buyers applied to the wrong lot and the seller was responsible for the misrepresentation of the real estate agent because under 28-10-602, a principal is responsible for the negligence of his agent. McCarty v. Lincoln Green, Inc., 190 M 306, 620 P2d 1221, 37 St. Rep. 2007 (1980).

Standard of Care of Real Estate Agent — Improper Identification of Real Property: Where the defendant real estate agent improperly identified certain real estate to prospective purchasers with the result that the buyers purchased property they had not intended to buy and suffered damages for which the seller became liable, it was not error for the court to find that the agent had breached his duty of care even though there was no evidence presented to the court on the standard of care of real estate agents in Montana. No standard of care could be countenanced by the real estate broker's profession, accepting as a reasonable standard of care the showing of the wrong property on behalf of a seller to a prospective purchaser. McCarty v. Lincoln Green, Inc., 190 M 306, 620 P2d 1221, 37 St. Rep. 2007 (1980).

Insurance Agency Not Responsible as Principal: A finance and insurance agency that sells disability insurance as an agent for an insurance company is not precluded from recovering money lent to a customer on the grounds that the insurance company denied coverage to the customer and the agency is a beneficiary because this section contains the only provisions where the agency may be held liable as the principal and none of these conditions were met. Budget Ins. & Fin. v. Leighty, 186 M 368, 607 P2d 1125 (1980).

Attorney: In action by sheriff to recover warehouse storage fees, attorney of judgment creditor was not liable as agent of his client since he was known to be only an agent and credit had not been extended to him personally. Hasbrouck v. Krsul, 168 M 270, 541 P2d 1197 (1975).

Personal Liability on Contract:

Where seller at auction sale required assurances from principal before it would accept the agent's drafts on principal in payment for cattle purchased, the seller could not hold the agent personally liable on the contract even though it permitted the agent to bid in at the auction without disclosing his principal. Yellowstone Livestock Comm'n v. Dupuis, 133 M 454, 325 P2d 691 (1958).

Where plaintiffs, in their suit to foreclose a mechanics' lien (now construction lien), proceeded upon the theory that one of the three defendants was the agent of the other two (owners of the property), and the agent was not shown to have done anything to make himself personally liable (this section) for the work done, entry of judgment against him was error. Arnold v. Genzberger, 96 M 358, 31 P2d 296 (1934).

An agent is not personally liable on a contract entered into by him on behalf of his principal if he disclosed the identity of the latter and made the engagement for him. This section embodies in principle the same rule. Farr v. Stein, 54 M 529, 172 P 135 (1918).

Trust Estate: The effect of 72-23-307 (now repealed) declaring in substance that a trustee is a general agent for the trust property to the same extent as the acts of an agent bind his principal, viewed in connection with this section, is either that the trust estate is to be considered an entity chargeable as a principal for the acts of the trustee, its agent, or that the legal incidents of the trustee's authorized acts, so far as the parties are concerned, are the same as those which would attach to an agent's authorized transactions for his principal. Tuttle v. Union Bank & Trust Co., 112 M 568, 119 P2d 884, 139 ALR 127 (1941).

Proof of Scope: Defendant was manager of an opera company, which was having a dispute with plaintiff. Hirsch, who acted as agent for defendant in some matters, offered to pay plaintiff's expenses to go to Butte to negotiate with defendant. At trial where plaintiff claimed the trip as an item of damages, it was held that there was no proof that Hirsch acted within the scope of his agency or that he attempted to bind anyone other than himself. Defendant was not bound by Hirsch's promise. Ming v. Pratt, 22 M 262, 56 P 279 (1899).

28-10-703. Responsibility of agent when third person claims property received for principal.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

28-10-704. Applicability of laws relating to capacity to contract.

Law Review Articles

Power of Infant to Appoint Agent, Ettien, 2 Mont. L. Rev. 68 (1941).

Part 8
Termination of Agency

Part Case Notes

Burden of Proving Termination: Where the relation of principal and agent is once established it is presumed to have continued, in the absence of a showing of its termination, the burden of proving termination being upon the principal. Exchange St. Bank v. Occident Elev. Co., 95 M 78, 24 P2d 126 (1933).

Part Law Review Articles

Termination of Agency by Death or Incapacity, McCormick, 22 Mont. L. Rev. 74 (1960).

28-10-801. Circumstances that terminate agency.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Construction — Section as Declaring Common Law: This section and 28-10-802 are declaratory of the common law. Nord v. Boston & Mont. Consol. Copper & Silver Min. Co., 33 M 464, 84 P 1116, 89 P 647 (1906).

28-10-802. Circumstances that terminate agency not coupled with interest.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Power Not Coupled With Interest: Power of attorney authorizing physician to perform all future medical services for decedent for which he was to receive $2,000 was not a power coupled with an interest and terminated upon death of decedent. Trenouth v. Mulroney, 124 M 499, 227 P2d 590 (1951).

Agency Revocable at Will: Where in an action to recover a 5% commission on the sale price of real estate under a contract of indefinite duration plaintiff's agency was not coupled with an interest and he had not procured a purchaser ready, able, and willing to buy and his efforts to that end were not approaching success the agency was revocable at the will of the principal. Newman v. Dunleavy, 51 M 149, 149 P 970 (1915).

Attorney and Client: That a party becomes insane while indebted to an attorney who was representing him at the time with respect to his property interests does not give such attorney the right per se to appear as attorney for the party's guardian, who by reason of such appointment becomes responsible for the estate and the proper conduct of the incompetent's affairs. State ex rel. Davis v. District Court, 30 M 8, 75 P 516 (1904).

CHAPTER 11
GUARANTY, INDEMNITY, AND SURETYSHIP

Part 1
Guaranty — General Provisions

28-11-101. Guaranty defined.

Case Notes

Sales — Guaranty of Buyer's Payment by Guarantor's Agent: Jacobs sold the uniform sales part of his business to K&M Sports, which in turn sold it to another, who defaulted on the sale. Jacobs, as secured party, repossessed the inventory and sold it to Snick Sports. Dirkson, who worked for K&M and then Snick, told Powers that Jacobs would guarantee Snick's payment of goods sold to Snick by Powers. There was disagreement as to whether Dirkson worked for Jacobs. For 2 years Powers mailed merchandise, statements, and invoices to Jacobs, who forwarded them to Snick, who paid the bills. When some bills went unpaid, Powers sued Jacobs when he failed to pay the bills on request. The mailings to Jacobs put him on reasonable notice that something was wrong. His failure to investigate and take action was want of ordinary care that caused or allowed Powers to believe an authorized agency existed between Jacobs and Dirkson. Thus, there was an ostensible agency and ostensible authority. For the same reason, a valid guaranty existed and Jacobs was estopped from defending against it on the basis of the Statute of Frauds. A jury verdict for Powers was affirmed. Powers Mfg. Co. v. Leon Jacobs Enterprises, 216 M 407, 701 P2d 1377, 42 St. Rep. 906 (1985).

Corporation Owners' Personal Guarantee of Corporation's Contract Obligation: Defendant corporation purchased plaintiff's business under a contract which provided that the inventory of the business would not be reduced in value below the amount still owed plaintiff under the contract. When plaintiff became worried about corporation's plan to carry out such a reduction, the owners of the corporation personally guaranteed payment of that part of the sale price still due plaintiff. There was consideration for the guarantee, in that plaintiff, in return for the guarantee, relinquished various legal rights of action which he would otherwise have had upon reduction of the value of the inventory. Therefore, the guarantee was not void for lack of consideration. Rudio v. Yellowstone Merchandising Corp., 200 M 537, 652 P2d 1163, 39 St. Rep. 1923 (1982), followed, with regard to sufficiency of mutual promises as valid consideration, in Kephart v. Portmann, 259 M 232, 855 P2d 120, 50 St. Rep. 771 (1993).

Guaranty for Repayment of Money Loaned: A guaranty for repayment of money loaned was not a suretyship within the meaning of 28-11-401. Stensvad v. Miners and Merchants Bank of Roundup, 183 M 160, 598 P2d 1083 (1979).

Letter of Credit: Letter of credit from bank to debtor stating "We are willing to guarantee these funds to whomever you purchase this engine from . . ." constituted a guaranty of the purchase price of the engine. Miller v. Walter, 165 M 221, 527 P2d 240 (1974).

Distinction Between "Special" and "General" Guaranty: A special guaranty is one addressed to a particular person who alone can take advantage of it and to whom only the guarantor can be held responsible; a general guaranty is for acceptance by the public generally. Austin v. New Brunswick Fire Ins. Co., 111 M 192, 108 P2d 1036 (1940).

Stockholder Liability Is in Nature a Guaranty:

The statutory liability imposed upon holders of bank stock by section 6036, R.C.M. 1921 (since repealed), for debts of a bank, is in the nature of a guaranty—not primary, but secondary—and, within the meaning of 27-2-211, providing that actions to recover on such liability must be brought within 3 years after the liability "was created", the liability was created, not when the statute imposing it was enacted, nor when the relation of debtor and creditor between the bank and plaintiff first arose, but when the bank became insolvent; therefore the complaint in such an action showing on its face that it was commenced within the 3-year period was sufficient as against a general demurrer. Mitchell v. Banking Corp. of Mont., 83 M 581, 273 P 1055 (1929).

The double liability to the creditors of an insolvent state bank imposed by section 6036, R.C.M. 1921 (since repealed), as amended by Ch. 9, L. 1923, upon a holder of stock in such bank, is in the nature of a guaranty, and therefore will not support an attachment as upon a contract for the direct payment of money in an action by the receiver to collect an assessment levied upon the stock of a delinquent stockholder. Muri v. Young, 75 M 213, 245 P 956 (1926).

Distinction Between Indemnity and Guaranty: When for the purpose of inducing the purchase of corporate stock the seller gave the buyer a promissory note payable in 3 years, the back of which bore the endorsement that when the stock had paid dividends to the amount of the purchase price, the note should be void, the agreement was one of indemnity and not of guaranty. Peterson v. Nelson, 77 M 539, 252 P 368 (1926).

Distinction Between Surety and Guarantor:

A contract of guaranty "is a promise to answer for the debt, default or miscarriage of another person". But it is distinguishable from one of surety, in that the former is a separate contract whereby the promisor is bound independently of the person for whose benefit it is made, while the latter is a contract whereby the promisor is bound jointly with the principal on the same contract. Anderson v. Border, 75 M 516, 244 P 494 (1926); Emerson-Brantingham Implement Co. v. Raugstad, 65 M 297, 211 P 305 (1922).

Under a contract of guaranty the promisor is bound independently of the person for whose benefit it is made, his engagement being a collateral undertaking; hence there being neither privity of contract, mutuality, nor joint liability between the principal debtor and the guarantor, they cannot be joined as defendants; under that of suretyship the surety is bound as an original promisor and the creditor may bring his action jointly against him and the debtor. Butte Mach. Co. v. Carbonate Hill Mill. Co., 75 M 167, 242 P 956 (1926).

A bond in which the sureties unconditionally agreed to indemnify a County Treasurer for failure of a bank to pay over to him on demand any funds he might have on deposit therein was a contract of surety and not of guaranty. State ex rel. Barnett v. Reynolds, 68 M 572, 220 P 525 (1923).

A surety is bound with the principal as an original promisor on the same contract, while a guarantor makes his own separate contract; a surety makes his contract primarily for the principal, while a guarantor makes his contract mainly for his own benefit. Cole Mfg. Co. v. Morton, 24 M 58, 60 P 587 (1900).

Nature of Contract of Guaranty: Although the contract of guaranty is collateral to the contract of the principal debtor, the two are distinct and independent, there being, as to the contract of guaranty, no privity, mutuality, or joint liability between the principal debtor and his guarantor. Baroch v. Greater Mont. Oil Co., 70 M 93, 225 P 800 (1924).

Distinction Between Accommodation Maker and Guarantor: When defendant signed a renewal note taking the place of a note signed by her husband and another, at the request of the husband for the purpose of lending her name to him as comaker, she was an accommodation maker within the meaning of 30-3-415, and not a guarantor. Mulany v. Murray, 68 M 245, 216 P 1105 (1923).

Law Review Articles

The Standby Letter of Credit: What It Is and How to Use It, Banks, 45 Mont. L. Rev. 71 (1984).

28-11-103. When separate consideration required.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Consideration for Renewal of Guaranty: Where defendants, after executing a contract of guaranty for the payment of merchandise under which goods were furnished but not paid for, upon its expiration entered into a contract of renewal thereof, agreeing to pay not only for future deliveries but reassuming liability for past indebtedness, the promise of the guarantee to furnish more goods was a good consideration for the contract, irrespective of the fact that no more goods were called for. W. T. Rawleigh Co. v. Miller, 105 M 456, 73 P2d 552 (1937).

Sufficiency of Consideration:

Before plaintiff manufacturing company would enter into a renewal contract with a distributor of its goods, it required him to furnish a written contract of guaranty signed by responsible parties agreeing to pay the company on termination of the renewal contract the amount due it from the distributor at the time of the execution of the guaranty or what might become due thereafter; in consideration it promised to furnish the distributor with more goods. The guaranty was furnished, no further goods, however, being thereafter ordered. In an action to recover on the guaranty, extension of time of payment was sufficient consideration. W. T. Rawleigh Co. v. Washburn, 80 M 308, 260 P 1039 (1927).

If a contract of guaranty is made for the benefit of the guarantor at the same time as the original obligation, no other consideration need exist. Lyon v. Featherman, 80 M 504, 261 P 268 (1927).

Forbearance to enforce a legal right is a sufficient consideration to support a contract. Doorly v. Goodman, 71 M 529, 230 P 779 (1924).

Simultaneous Delivery of Instruments: When a promissory note was not accepted until a guaranty was produced and the two instruments were delivered together, plaintiff in an action on the guaranty was not required to show independent consideration for it; a showing of consideration for the note was sufficient. Schauer v. Morgan, 67 M 455, 216 P 347 (1923).

Suretyship Distinguished: The codes preserve the general distinction between suretyship and guaranty, which is that a surety is bound with the principal as an original promisor on the same contract, while the guarantor makes his own separate contract. This section was enacted with regard to this distinction. Cole Mfg. Co. v. Morton, 24 M 58, 60 P 587 (1900).

28-11-104. Guaranty generally to be in writing — form.

Case Notes

Guaranty Imposed by Law Need Not Be in Writing: When a liability in the nature of a guaranty is imposed by law it does not fall within the provision of this section requiring a contract of guaranty to be in writing. Muri v. Young, 75 M 213, 245 P 956 (1926).

28-11-105. When guaranty considered original obligation and need not be in writing.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Sales — Guaranty of Buyer's Payment by Guarantor's Agent: Jacobs sold the uniform sales part of his business to K&M Sports, which in turn sold it to another, who defaulted on the sale. Jacobs, as secured party, repossessed the inventory and sold it to Snick Sports. Dirkson, who worked for K&M and then Snick, told Powers that Jacobs would guarantee Snick's payment of goods sold to Snick by Powers. There was disagreement as to whether Dirkson worked for Jacobs. For 2 years Powers mailed merchandise, statements, and invoices to Jacobs, who forwarded them to Snick, who paid the bills. When some bills went unpaid, Powers sued Jacobs when he failed to pay the bills on request. The mailings to Jacobs put him on reasonable notice that something was wrong. His failure to investigate and take action was want of ordinary care that caused or allowed Powers to believe an authorized agency existed between Jacobs and Dirkson. Thus, there was an ostensible agency and ostensible authority. For the same reason, a valid guaranty existed and Jacobs was estopped from defending against it on the basis of the Statute of Frauds. A jury verdict for Powers was affirmed. Powers Mfg. Co. v. Leon Jacobs Enterprises, 216 M 407, 701 P2d 1377, 42 St. Rep. 906 (1985).

Original Promise Within the Meaning of This Section:

When a merchant would not sell merchandise to a grower unless plaintiff bank promised to pay therefor, its promise to do so made it the principal debtor and constituted an "original obligation" within the meaning of this section, not required to be in writing. First Nat'l Bank v. Hergert, 94 M 197, 22 P2d 169 (1933).

When two directors of a corporation in need of financial aid orally agreed with each other that each would answer to the other for advances made by each to it, provided things could not be so arranged that both should be made whole by the corporation, neither became a principal debtor to the other. Bennighoff v. Robbins, 54 M 66, 166 P 687 (1917).

A promise to answer for the obligation of another is to be deemed the original obligation of the promisor when the creditor parts with value in terms, or under circumstances, such as put the promisor in the attitude of principal debtor, and the person he promises for in the attitude of surety. Such terms or circumstances do not appear when a person introduces strangers to a storekeeper and says, "If they don't pay, I will." Fortman v. Leggerini, 51 M 238, 152 P 33 (1915).

Oral Agreement by Husband to Pay Wife's Attorney to Bring About Reconciliation: An oral agreement between the husband and his wife's attorney to pay for the latter's services was an original undertaking within the meaning of this section, and not a guaranty, and therefore not void under the Statute of Frauds. Walker v. Hill, 90 M 111, 300 P 260 (1931).

Oral Obligation to Pay Antecedent Obligation of Another:

When a promise is made to pay the antecedent obligation of another upon the condition that the party receiving it will cancel the obligation, accepting the new promise in substitution therefor, it is an original undertaking or agreement and not a mere promise to answer for the debt of another within the meaning of the Statute of Frauds, and need not be in writing. Tannhauser v. Shea, 88 M 562, 295 P 268 (1930).

A promise by partners to pay an existing debt of a corporation to another in consideration of such other person giving them an agency for sale of his coal is an original obligation, which, under this section, need not be in writing. McCormick v. Johnson, 31 M 266, 78 P 500 (1904).

Consideration Necessary: The consideration which will convert a promise to answer for the obligation of a third person into an original obligation of the promisor, so as to take it out of the Statute of Frauds, must be one tangible at law. Bennighoff v. Robbins, 54 M 66, 166 P 687 (1917).

Oral Promise to Pay When Promisor Has Received Property: Where upon the winding up of a copartnership of which defendant was a member he retained certain partnership funds and agreed to pay plaintiff a debt due him for wages from the firm, defendant's promise was upon a consideration beneficial to himself and was valid though not in writing. Carlson v. Barker, 36 M 486, 93 P 646 (1907).

Independent Duty to Pay: When the original debt was antecedently contracted and subsists, the promise to pay it is original if founded upon a new consideration moving to the promisor, and beneficial to him, and such that the promisor thereby comes under an independent duty of payment irrespective of the liability of the principal debtor. McCormick v. Johnson, 31 M 266, 78 P 500 (1904).

28-11-106. When notice of acceptance necessary to bind guarantor.

Case Notes

Reasonable Notice of Acceptance: Notice of acceptance of bank's offer of guaranty on price of an engine was reasonable and timely when made at time of bank's repossession of truck (3 months after actual acceptance) and nearly 3 months before truck was resold. Miller v. Walter, 165 M 221, 527 P2d 240 (1974).

Letter: A letter written by plaintiff to defendant was a sufficient acceptance of an offer of guaranty. Davis v. McEwen, 193 F 305 (C.C.A. Mont. 1912).

28-11-107. When guaranty considered unconditional.

Case Notes

Lack of Notice to Guarantor of Alteration of Note — Basis for Release: When a lending bank brought an action to recover under a continuing and unconditional contract of guaranty, the guarantor established that the lender failed to notify the guarantor of changes in the underlying note which materially increased the guarantor's risk. The lending bank has a duty to notify a guarantor that it has not totally discharged a note upon receipt of the collateral. The bank's failure to give such notice releases the guarantor from his obligation. The Supreme Court approved the use of a test from the Restatement of Security sec. 124(1) (1941), for when a creditor has a duty, at the outset of an obligation, to disclose facts it knows about the debtor to the surety to determine whether the surety should be released. Sec. Bank v. Mudd, 215 M 242, 696 P2d 458, 42 St. Rep. 323 (1985).

Conditional Sale Contract: A guaranty on a conditional sale contract, guaranteeing full performance and stating any settlement or compromise with parties would not release guarantor, was an absolute guaranty, and the guarantor was not relieved by plaintiff recovering and selling the mining equipment involved. Gen. Fin. Co. v. Powell, 114 M 473, 138 P2d 255 (1943).

28-11-108. Continuing guaranty — definition — revocation.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Guarantor Owes Pro Rata Share: Appellant and four other shareholders in company executed continuing guaranties for promissory notes on behalf of their shared business. Appellant subsequently signed away his share in company and left the business. Although the court considered appellant's equitable defense that he was not liable for his pro rata share of the notes because the other four guarantors personally profited from the sale of the business after appellant departed, he remains liable for his pro rata share. He signed the guaranty knowing the lender could sue him directly on the notes. All five shareholders shared equal liability on the promissory notes, and appellant is required to contribute his one-fifth pro rata share. Citizens St. Bank v. Bossard, 226 M 75, 733 P2d 1296, 44 St. Rep. 468 (1987).

Part 2
Guaranty — Liability and Exoneration of Guarantor

Part Case Notes

Determination of Reasonable Efforts Made by Creditor Prior to Action Against Guarantor: The plaintiff, a real estate agent, sued the defendant for unpaid commissions. The District Court granted the plaintiff summary judgment. On appeal, the defendant argued that it was improper for the District Court to rule on the issue of whether the plaintiff had reasonably exhausted all remedies against other debtors before attempting to collect from him, the guarantor, in a motion for summary judgment. The Supreme Court agreed and reversed and remanded the matter for further proceedings. Foss v. Melton, 2016 MT 232, 385 Mont. 5, 386 P.3d 553.

Condition Required by Guaranty Held Satisfied by Proceeding Against Debtor in Bankruptcy: Based on a contract executed in 1990, Western supplied material to Chicago Mining Corporation (CMC) for its tailings pond in Pony. CMC failed to make contract payments, and Western filed a construction lien. In 1991, the guarantors individually executed personal guaranties that included language authorizing Western to collect against each guarantor "with the necessity of first proceeding against [CMC]". Later, Western and CMC stipulated to a judgment against CMC, a final judgment was entered, and Western arranged for a Sheriff's sale of certain CMC property, but CMC filed a petition for Chapter 11 bankruptcy. In 1995, Western brought a motion for summary judgment that was granted by the District Court. The Supreme Court held that the guaranty was conditional because it established the necessity for action against CMC as a condition precedent to action against the guarantors to collect CMC's debt. The Supreme Court held that the condition was satisfied because Western had brought an action against CMC, filed a stipulated judgment against CMC, had attempted to enforce the judgment, and had taken various steps to participate in the bankruptcy proceedings, including the conversion of those proceedings from a Chapter 11 proceeding to a Chapter 7 proceeding. W. Indus., Inc. v. Chicago Min. Corp., 279 M 105, 926 P2d 737, 53 St. Rep. 1071 (1996).

28-11-201. Obligation of guarantor not to exceed that of principal.

Case Notes

Stipulated Judgment as Basis for Debt of Guarantors — Vesting Date of Right to Interest — Prejudgment and Postjudgment Interest Awarded: Chicago Mining Corporation (CMC) made a contract with Western for the purchase of mining equipment, and when CMC did not make payments as required by the contract, Western filed a construction lien to collect the amount of $232,730.04. In January 1991, individuals acting as guarantors executed personal guaranties for that amount, and Western promised that it would not institute foreclosure proceedings to enforce its lien until February 1, 1991. In 1994, Western and the guarantors stipulated to entry of judgment in the amount of $196,849.72, and judgment was entered for that amount. Following a bankruptcy proceeding and pursuant to a motion for summary judgment, the District Court awarded Western $232,730.04 and prejudgment interest from February 1, 1991, to February 22, 1996. The Supreme Court held that the stipulated judgment conclusively established CMC's obligation and that because the obligation of guarantors cannot exceed the obligation of the principal debtor, the amount of the stipulated judgment is also the amount owed by the guarantors. The Supreme Court also held that because Western's right to recover from the guarantors vested on February 1, 1991, the day CMC failed to make payments and the date upon which the guarantors agreed to make payment, that date is the date upon which prejudgment interest was due and that postjudgment interest was due from the date of the judgment to the date upon which the judgment is satisfied. W. Indus., Inc. v. Chicago Min. Corp., 279 M 105, 926 P2d 737, 53 St. Rep. 1071 (1996).

Letter of Credit — Guaranty Distinguished: Plaintiff agreed to lend Prospect Associates, Inc. (Prospect) money to finance construction of a subdivision. As part of the security for the loan, Prospect was required to obtain a letter of credit with plaintiff as beneficiary. Prospect defaulted on the promissory note evidencing the loan. Defendant refused payment on the letter of credit, contending it was a guaranty on which it was not primarily liable. The District Court granted summary judgment to plaintiff, and defendant appealed. The Supreme Court affirmed the decision, saying the document was clearly entitled a letter of credit and its intent was to hold the bank primarily liable upon nonperformance of one of the named instruments, as opposed to secondarily liable as under a guaranty. Sherwood & Roberts, Inc. v. First Security Bank, 209 M 402, 682 P2d 149, 41 St. Rep. 787 (1984).

Effect of Impossibility of Performance of Contract by Principal: Although contract was void because the impossibility of performance due to the nature of the thing the contracting company undertook to do, the contractor was entitled to a recovery on the quantum meruit. His bond did not permit recovery of damages. A collateral promise in the contract consisting of warranty was invalid and would not support action for breach of warranty. Contractor's lien was supported by the implied contract. Smith Eng'r Co. v. Rice, 102 F2d 492 (9th Cir. 1938).

28-11-202. Liability under guaranty of incomplete contract.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Accelerated Payments Provision: When a purchase-money mortgage of machinery provided that on default the seller was authorized to take possession of the machinery and sell it at public auction without further demand, or at a private sale, the liability of the guarantors of the notes became fixed when the buyer failed to make payment at maturity of the notes. Minneapolis Thresh. Mach. Co. v. Jameison, 70 M 27, 223 P 893 (1924).

28-11-203. Liability under guaranty of illegal contract or contract void against principal.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

28-11-205. When guarantor of payment or performance becomes liable.

Case Notes

Conditional Sales Contract — No Release by Assignment: A guaranty endorsed on a conditional sales contract by the seller guaranteeing full performance of the contract and prompt payment of all sums due thereunder is a separate and distinct agreement between him and the assignee thereof, and does not give rise to any contractual relation between the assignee and the vendee named in the contract. A guaranty such as this which in addition stated that any settlement or compromise which the holder of the conditional sales contract assigned may make with the parties to it shall not release the guarantor was an absolute guaranty from liability under which he was not relieved by the assignee's recovery and sale of the machinery involved. Gen. Fin. Co. v. Powell, 114 M 473, 138 P2d 255 (1943).

Subrogation of Guarantor: The guarantor of a mortgage debt can be subrogated to the rights of the mortgagee only by payment of the entire debt secured and not merely by payment of the interest coupons of the mortgage as here. NW. Fire & Marine Ins. Co. v. Pollard, 74 M 142, 238 P 594 (1925).

Accelerated Payments Provision: Where a purchase-money mortgage of farm machinery provided that on default of the purchaser in payment of any part of the principal of the notes given by him, the seller was authorized to take possession of the machinery and sell it at public auction without further demand, or at a private sale with or without notice, the liability of the guarantors of the notes became fixed when the buyer failed to make payment at maturity of the notes. Minneapolis Thresh. Mach. Co. v. Jameison, 70 M 27, 223 P 893 (1924).

28-11-206. Liability upon guaranty of conditional obligation — notice of default.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

28-11-211. When guarantor exonerated.

Compiler's Comments

2021 Amendment: Chapter 168 in (1) after "any act of the creditor" substituted "not authorized by the original guaranty instrument or without the separate consent of the guarantor" for "without the consent of the guarantor"; and made minor changes in style. Amendment effective October 1, 2021.

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Alteration of Original Terms of Guaranty — Exoneration From Personal Guaranty: Defendant signed a guaranty for a personal loan from the plaintiff bank. During the period of the loan, the bank materially altered the terms of the original guaranty by changing the underlying obligation from a line of credit to a term loan, which extended defendant's exposure as a guarantor. The jury exonerated the defendant from liability under the guaranty, and the bank appealed, but the Supreme Court affirmed. Defendant presented sufficient evidence of the bank's change in the original obligation to warrant the jury's exoneration of the defendant from the guaranty. First Citizens Bank v. Sullivan, 2008 MT 428, 347 M 452, 200 P3d 39 (2008).

Principal's Impairment or Suspension of Rights of Guarantor — Exoneration of Guarantor Proper: Ace Leasing, Inc. (Ace), funded a lease to O'Neill for $45,000 for business equipment. Boustead was guarantor of the lease agreement. If O'Neill failed to perform, the lease provided that Ace could proceed directly against Boustead. O'Neill failed to make timely payments. Ace canceled the lease. O'Neill and Ace then discussed the matter, and O'Neill explained that the late payments were the result of the late arrival of the ordered equipment. Ace agreed to accept several late payments, but Boustead was not part of the negotiations. O'Neill again missed several payments, and Ace requested that Boustead pay off the lease. Boustead refused to pay on grounds that the cancellation letter and acceptance of late payments without Boustead's knowledge, as well as the method of purchasing the equipment, constituted a material change in the agreement and in Boustead's obligations as guarantor. The District Court agreed and exonerated Boustead as guarantor under this section. The court also held that Boustead's risk was increased because Ace did not own the equipment, so the transaction between Ace and O'Neill constituted a loan rather than a lease. Ace appealed the findings regarding ownership and alteration of the agreement. The Supreme Court affirmed. Under 30-2-401, the title of goods passes to the buyer at the time that and place at which the seller completes performance with reference to physical delivery of the goods, unless the agreement provides otherwise. Here, neither Ace nor O'Neill conformed to the purchase provision of the agreement. Because Ace failed to obtain title, Ace could not assume the role of lessor and, while retaining title and ownership, transfer to O'Neill merely the right of possession and use of the equipment, so the transaction effectively became a loan agreement between the parties with O'Neill holding title to the equipment according to the default provisions of the Uniform Commercial Code. Further, Ace's actions in accepting late payments after canceling the agreement and in failing to comply with the terms of the lease requiring Ace to purchase the equipment and retain ownership to secure its interest were a material alteration in the agreement as affecting Boustead. Ace impaired or suspended its rights and remedies against O'Neill and, without Boustead's consent, impaired or suspended Boustead's rights as well, which was sufficient to exonerate Boustead as guarantor under this section. Ace Leasing, Inc. v. Boustead, 2002 MT 213, 311 M 285, 55 P3d 371 (2002).

Guarantor's Obligation Not Barred by Statute of Limitations as to Obligation of Principal: A creditor's claim against a guarantor is not exonerated by the running of the statute of limitations as against the principal. Mercury Marine v. Monty's Enterprises, Inc., 270 M 413, 892 P2d 568, 52 St. Rep. 255 (1995). See also Dupree v. Jordan, 252 P 67 (Okla. 1927), Bloom v. Bender, 313 P2d 568 (Calif. 1957), and Restatement of Security 130 (1941), Comment a on subsection (1) and illustration 2.

Guarantor Discharged From Guaranty if Bank Impaired Remedy: The Supreme Court remanded for a determination of whether attorneys for the estate knew of bank's claim and represented that a creditor's claim need not be filed. If determined that the bank did indeed fail to file a required creditor's claim, it impaired its remedy against the principal without authorization of the guarantor. Therefore, guarantor would be discharged of any responsibility under her guaranty. NW. Bank of Lewistown v. Estate of Coppedge, 219 M 473, 713 P2d 523, 43 St. Rep. 102 (1986).

Lack of Notice to Guarantor of Alteration of Note — Basis for Release: When a lending bank brought an action to recover under a continuing and unconditional contract of guaranty, the guarantor established that the lender failed to notify the guarantor of changes in the underlying note which materially increased the guarantor's risk. The lending bank has a duty to notify a guarantor that it has not totally discharged a note upon receipt of the collateral. The bank's failure to give such notice releases the guarantor from his obligation. The Supreme Court approved the use of a test from the Restatement of Security sec. 124(1) (1941), for when a creditor has a duty, at the outset of an obligation, to disclose facts it knows about the debtor to the surety to determine whether the surety should be released. Sec. Bank v. Mudd, 215 M 242, 696 P2d 458, 42 St. Rep. 323 (1985).

Exoneration by Death of Surety: Where deceased had previously cosigned a promissory note for the purpose of lending his name to another party, he became an accommodation maker. As such he is primarily responsible for the payment of the note, without necessity of resort to the principal, and it was error for the District Court to disallow the holder's claim against the deceased's estate. In re Estate of Harbaugh, 196 M 274, 639 P2d 495, 39 St. Rep. 84 (1982).

Alteration of Remedies or Rights of Creditor: An alteration or elimination of debtor's remedy did not result in exoneration of the guarantor; elimination of right of redemption of debtor corporations which owned real property subject to security interest by secured party's action in forcing transfer of pledged stock certificates did not exonerate guarantor. Stensvad v. Miners & Merchants Bank of Roundup, 163 M 409, 517 P2d 715 (1973).

Execution and Delivery of Note as Evidence: Debtor's execution and delivery to creditor of note as evidence of debt rather than as payment thereof did not exonerate debtor's surety in the absence of prejudice to the surety. Falls Implement Co. v. Gen. Ins. Co. of Am., 152 M 250, 448 P2d 675 (1968).

Rescission of Contract by Creditor: When vendees of real estate abandoned premises with the knowledge of vendors, who repossessed by permitting another party to occupy and served a notice of cancellation of the contract for sale upon vendees, vendors by such rescission of contract lost their right to bring action against vendees' guarantor for unpaid purchase price. Scott v. Kyhl, 141 M 523, 379 P2d 803 (1963).

Actual Injury to Surety Not Necessary: If a creditor without the consent of the surety does any act which in contemplation of law alters the surety's liability, increases his risk, or deprives him even for a moment of the right to pay the debt and assume the position of the creditor, or of his right to seek indemnity, the surety is discharged and the fact that he may not have been actually injured is immaterial. U.S. Bldg. & Loan Ass'n v. Burns, 90 M 402, 4 P2d 703 (1931).

Alteration of Contract Releasing Surety: Where the grantor of mortgaged real property conveys it, the grantee assuming the mortgage (the grantor thus becoming a surety and the grantee the principal debtor), and thereafter the mortgagee enters into a written agreement with the grantee under which he relinquishes his right to receive the gross revenues from the property as provided for under the mortgage contract, requires the grantee to pay only what is left after paying operating expenses and waives default in the payment of taxes as well as his right to foreclose the mortgage because of defaults in paying monthly installments of rent, the original obligation is so materially altered as to release the surety under 28-11-412 and this section. U.S. Bldg. & Loan Ass'n v. Burns, 90 M 402, 4 P2d 703 (1931).

Extension of Time for Payment as Release: When a mortgagee granted a purchaser of the mortgaged property who had assumed the debt an extension within which to make payment at a higher rate of interest than that originally provided for, without the consent of his grantor, thus materially altering the terms of the obligation to pay debt, the grantor (surety) was released from liability and therefore the mortgagee was not entitled to a deficiency judgment against him in his action to foreclose. Shipman v. Terrill, 84 M 322, 276 P 21 (1929).

Amendment of Complaint as Release: The surety on an undertaking to secure the release of property from attachment enters into the obligation with reference to the cause as it then stands; and if the plaintiff in the action in which the attachment was levied, without the consent of the surety, subsequently changes his pleading so as to state another and different cause of action, it is such a change as will work a release of the surety. Gilna v. Fidelity & Deposit Co., 83 M 231, 272 P 540 (1928).

Compromise of Claim as Release: A guarantor of the payment of a note is relieved from liability when the cashier of the holder, with the knowledge of the holder, accepts as payment from the principal debtor a conveyance of land, cancels the note, and executes a note to the holder for the amount of the debt of the principal debtor. Standford v. Coram, 26 M 285, 67 P 1005 (1902).

Law Review Articles

Suretyship: Defenses of Sureties and Guarantors Under R.C.M. 1935, §§ 8188 and 8201, Browning, 2 Mont. L. Rev. 155 (1941).

28-11-213. Guarantor not exonerated by delay of creditor.

Case Notes

Guarantor's Obligation Not Barred by Statute of Limitations as to Obligation of Principal: A creditor's claim against a guarantor is not exonerated by the running of the statute of limitations as against the principal. Mercury Marine v. Monty's Enterprises, Inc., 270 M 413, 892 P2d 568, 52 St. Rep. 255 (1995). See also Dupree v. Jordan, 252 P 67 (Okla. 1927), Bloom v. Bender, 313 P2d 568 (Calif. 1957), and Restatement of Security 130 (1941), Comment a on subsection (1) and illustration 2.

28-11-214. Guarantor not exonerated by discharge of principal.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

28-11-216. Effect of part performance on guarantor's liability.

Case Notes

Subrogation of Guarantor: The guarantor of a mortgage debt can be subrogated to the rights of the mortgagee only by payment of the entire debt secured and not merely by payment of the interest coupons of the mortgage as here. NW. Fire & Marine Ins. Co. v. Pollard, 74 M 142, 238 P 594 (1925).

Part 3

Indemnity

Part Case Notes

No Error in Granting Summary Judgment Based on Insurer's Duty to Defend: Although an insurer had charged a premium to a pest control producer to add the pest control distributor to an insurance policy, the insurer refused to defend or indemnify the distributor in an underlying action. Because the duty to defend is broader than the duty to indemnify, the Supreme Court found that the insurer should have defended the distributor and could have done so while reserving its rights. The Supreme Court found that due to the insurer's refusal to defend the distributor, it had failed to raise any coverage defenses and was estopped from denying indemnification for the distributor's damages, including the settlement amount and attorney fees. Scentry Biologicals, Inc. v. Mid-Continent Casualty Co., 2014 MT 39, 374 Mont. 18, 319 P.3d 1260.

Sufficient Evidence to Support Jury Verdict That Principal Breached Fiduciary Duty to Its Agent: An insured brought an action against Deonier, an insurance agent, and Paul Revere Life Insurance Company (Revere) to recover benefits and damages after the insured's claim was denied on grounds of a preexisting condition, despite the incontestability clause in the policy. The agent cross-claimed against the company for indemnity and breach of fiduciary duty, contending that there was a significant amount of evidence that Revere planned to assert the Forman defense in Montana (see Mass. Cas. Ins. Co. v. Forman, 516 F2d 425 (5th Cir. 1975), in which an insurer asserted a legal defense to the incontestability clause based on its definition of sickness as excluding disabilities that manifested themselves prior to the date of issue of the policy) and that Revere's failure to inform Deonier of its intention to invoke the defense was a clear breach of Revere's duty to inform its agents of a risk of pecuniary loss from potential lawsuits. Revere asserted that pursuant to Doettl v. Colonial Life & Accident Ins. Co., 505 F. Supp. 127 (D.C. Mont. 1981), in which a Montana federal District Court endorsed the Forman defense, it had no reason to believe that its policy interpretation might be in violation of Montana law and therefore did not breach its duty to inform its agents of risk of pecuniary loss. In the first Deonier case, Deonier & Associates v. Paul Revere Life Ins. Co., 2000 MT 238, 301 M 347, 9 P3d 622 (2000), the Supreme Court reversed the lower court's summary judgment in favor of Revere that held that there had not been a breach of fiduciary duty and remanded the case back to the lower court for a jury trial on the issue of liability and damages. The jury found for Deonier and awarded her $150,000 in compensatory damages and $1 million in punitive damages, which the trial court reduced to $375,000. The trial court denied Revere's motion for judgment as a matter of law that it had not breached its fiduciary duty. The Supreme Court affirmed on the basis that Deonier had presented evidence that Revere knew it would assert the Forman defense and that such an action might lead to pecuniary damages for its agents, and therefore there existed a legally sufficient evidentiary basis for a reasonable jury to find that a breach of fiduciary duty had occurred. Deonier & Associates v. Paul Revere Life Ins. Co., 2004 MT 297, 323 M 387, 101 P3d 742 (2004).

Indemnity of Insurance Agent for Defending Actions Performed on Insurer's Behalf in Solicitation of Application for Insurance: An insured brought a negligent misrepresentation action against Deonier, an insurance agent, and Paul Revere Life Insurance Company (Revere) to recover benefits and damages after the insured's claim was denied on grounds of a preexisting condition, despite the incontestability clause in the policy. Deonier cross-claimed against the company for indemnity, and the District Court required Revere to indemnify for damages that Deonier suffered as a result of the lawsuit. Revere appealed on grounds that Deonier was acting as an agent for the insured when recommending a disability policy, rather than as an agent for Revere, asserting that the fees that Deonier incurred were for defending the insured's claim that Deonier was actively negligent, defeating an indemnity claim. The Supreme Court affirmed, holding that because Revere admitted in its pleadings that there was no basis in law or fact for the negligent misrepresentation claim against Deonier, Revere implicitly conceded that Deonier's liability to the insured arose solely from the agency relationship between Deonier and Revere, a situation in which indemnity was required. Deonier & Associates v. Paul Revere Life Ins. Co., 2000 MT 238, 301 M 347, 9 P3d 622, 57 St. Rep. 989 (2000). See also Tynes v. Bankers Life Co., 224 M 350, 730 P2d 1115 (1986), and Restatement (Second) of Agency 439 (1958).

No Agreement to Indemnify Third Parties in Contract for Sale of Ski Resort: In 1976, Big Sky of Montana, Inc., sold the Big Sky ski resort. The resort eventually came under the ownership of Boyne U.S.A., Inc. Big Sky of Montana, Inc., agreed to indemnify Boyne against liability claims arising out of Big Sky's business affairs prior to the sale. In 1976, structural defects were found in condominiums owned by the plaintiffs, and after a lawsuit, Big Sky's successor in interest, Big Sky of Montana Realty, Inc., made repairs to the buildings. In 1981, the plaintiffs suffered two fires that destroyed parts of their condominiums. The plaintiffs sued Big Sky of Montana Realty, Inc., claiming that the plaintiffs were entitled to indemnity for their loss under the sales contract. The District Court found that no indemnity agreement existed. The Supreme Court found that on the record, Big Sky of Montana Realty, Inc., made no indemnity payment to the plaintiffs for settlement of the structural defects and that there was no other evidence before the Supreme Court of an indemnity agreement. The District Court therefore properly found that the 1976 sale was not an indemnity agreement in favor of the plaintiffs. Ass'n of Unit Owners of Deer Lodge Condominium v. Big Sky of Mont., Inc., 245 M 64, 798 P2d 1018, 47 St. Rep. 1814 (1990).

Accepted Work Rule Doctrine — Contractor Nonliability: The District Court properly granted summary judgment in favor of a contractor on the issue of negligence based on the accepted work rule doctrine. The doctrine, first recognized in Ulmen v. Schwieger, 92 M 331, 12 P2d 856 (1932), is based on the rule that an independent contractor is not liable to third parties for injuries that occur after the work has been completed and turned over to and accepted by the employer. Instead, the person employing the contractor is substituted as the responsible party. The Supreme Court affirmed the doctrine by refusing to extend contractor liability to foreseeable injury caused by negligent construction. Harrington v. LaBelle's of Colo., Inc., 235 M 80, 765 P2d 732, 45 St. Rep. 2176 (1988), overruled in Pierce v. ALSC Architects, P.S., 270 M 97, 890 P2d 1254, 52 St. Rep. 93 (1995).

Products Liability — "Upstream" Indemnification From Manufacturer of Defective Component: The federal District Court, noting the Montana Supreme Court decision in Brandenburger v. Toyota Motor Sales, 162 M 506, 513 P2d 268 (1973), adopted as a general proposition the rule that allows the manufacturer/assembler of a finished product to seek indemnification from the manufacturer of a component part that was defective at the time it left the component manufacturer's hand and that was integrated as part of the finished product. Jones v. Aero-Chem Corp., 680 F. Supp. 338, 45 St. Rep. 360 (D.C. Mont. 1987).

No Right to Third-Party Indemnity or Contribution in RICO Action: In a Racketeer Influenced and Corrupt Organizations Act (RICO) action there is no right to indemnification or contribution from a third party. Jacobson v. W. Mont. Prod. Credit Ass'n, 643 F. Supp. 391, 43 St. Rep. 1598 (D.C. Mont. 1986), citing Seminole Elec. Co-op, Inc. v. Anthony Tanner, No. 85-1286-Civ-T-13 (M.D. Fla. 1986).

Indemnity — Refusal to Instruct on Active/Passive Negligence Not Reversible Error: Where the plaintiff supplier of certain air pollution control equipment brought an action against the defendant manufacturing company for breach of warranty, the District Court did not err in refusing to instruct the jury on the active/passive negligence of the plaintiff. The record in this case shows that there was no active negligence on the part of the plaintiff and he therefore did not lose his right to indemnity under the rationale of Town Pump, Inc. v. Diteman, 191 M 98, 622 P2d 212, 38 St. Rep. 54 (1981). Iowa Mfg. Co. v. Joy Mfg. Co., 206 M 26, 669 P2d 1057, 40 St. Rep. 1479 (1983).

Liability of Indemnitor Upon Settlement of Original Claim — Standard for Liability: Where the plaintiff equipment supplier sued the defendant manufacturing company in a third-party action for breach of warranty, after giving the defendant an opportunity to defend or approve a settlement of the original case, the plaintiff sustained its burden of proof by proving potential liability in the original action. Because the defendant was given the opportunity to either defend the plaintiff or approve a settlement and declined to do either, the plaintiff needed only to show potential rather than actual liability in the original action in order to recover from the defendant, and there was sufficient evidence in the record of potential liability. Iowa Mfg. Co. v. Joy Mfg. Co., 206 M 26, 669 P2d 1057, 40 St. Rep. 1479 (1983).

Indemnification for Amount of Settlement Under Specific Contract Provisions: When under the terms of a contract between two interstate trucking firms the appellant agreed to provide workers' compensation coverage and to save the appellee's carrier harmless from any liability arising out of the relationship between the appellant and his employees, the appellee's carrier was entitled to be indemnified for an amount paid in settlement of a workers' compensation claim. Indus. Indem. Co. v. McIntosh, 185 M 158, 604 P2d 1233 (1980).

Products Liability — Indemnity — Third-Party Actions: Plaintiff was injured when a pickup truck in which he was riding rolled over. Plaintiff sued General Motors and also the manufacturer of the pants he was wearing. Plaintiff alleged the pants were defective and increased the severity of his injuries by melting onto his skin. The pants manufacturer filed a third-party complaint against Burlington Industries who had manufactured the pants material and supplied it to Corbin, Ltd., the maker of the pants. Burlington moved for dismissal of the third-party complaint, saying that indemnity for tort liability cannot be sought in a third-party action when the primary complaint sounds in strict products liability, indemnity being antithetical to and inapplicable in strict liability actions. Corbin argued that such indemnity is permissible through a process of weighing the comparative fault of two potentially liable parties, despite the fact the action was in strict liability, not in negligence. The U.S. District Court agreed with the Burlington arguments, observing that Corbin offered little supporting authority while Burlington cited ample authority. The court also noted that Montana has adopted Section 402A of the Restatement of Torts, including the conclusion that the doctrine of strict liability was evolved to place liability on the party primarily responsible for the injury occurring, that is, the manufacturer of the defective product, a position based on public policy arguments. The question in Montana is the condition of the product in the hands of the injured party, not the ultimate fault of any given defendant arising from such defendant's conduct. Kelly v. Gen. Motors Corp., 487 F. Supp. 1041, 37 St. Rep. 805 (D.C. Mont. 1980), distinguished in Jones v. Aero-Chem Corp., 680 F. Supp. 338, 45 St. Rep 360 (D.C. Mont. 1987).

Implied Right of Indemnity Not Applicable: Plaintiffs sued defendant airline company for injuries sustained by the airline's negligent maintenance of the runway apron, and the defendant's third-party complaint alleging an implied right of indemnity by the city maintaining the airport was dismissed. Because indemnity operates to shift the entire loss from one party compelled to bear it to the shoulders of another who should bear it instead, indemnity is not applicable where active negligence on the part of one party has been proven. The city's motion for summary judgment dismissing the third-party complaint was properly granted. Rogers v. W. Airlines, 184 M 170, 602 P2d 171 (1979).

28-11-301. Indemnity defined.

Case Notes

No Duty to Defend or Indemnify — Claims Outside of Policy Coverage — Summary Judgment in Favor of Insurer Proper. Christian v. United Fire & Cas. Co., 2023 MT 100, 412 Mont. 340, 530 P.3d 456.

Additional Insured Endorsement in Primary Policy — Duty to Defend: An employee of a subcontractor was injured while installing fireproofing in a building. The general contractor's liability insurer (defendant insurer) tendered a defense to the subcontractor under the indemnity clause in the subcontract and to the general contractor's insurer (plaintiff insurer) under the commercial general liability policy, so the question arose whether plaintiff insurer had a duty to defend pursuant to the commercial liability under which the general contractor qualified as an additional insured. Plaintiff insurer argued that because the general contractor could not shift responsibility to the subcontractor for the general contractor's statutory duty to maintain general job site safety, plaintiff insurer had no duty to defend or cover the loss. The District Court disagreed and granted summary judgment to defendant insurer pursuant to the additional insured endorsement. Plaintiff insurer appealed, but the Supreme Court affirmed. The court examined the indemnity provision in the subcontract and determined that the indemnity provision was not sufficiently clear and unequivocal in its intent to indemnify the general contractor for its own negligence, so the court then turned to the language of the additional insured endorsement. The general contractor was clearly named as an additional insured on a primary noncontributing basis, so plaintiff insurer's policy was clearly intended to be primary. Because plaintiff insurer had a duty to defend the general contractor, the District Court did not err in granting defendant insurer's motion for summary judgment and holding that plaintiff insurer breached its duty to defend. United Nat'l Ins. Co. v. St. Paul Fire & Marine Ins. Co., 2009 MT 269, 352 M 105, 214 P3d 1260 (2009), following Slater v. Cent. Plumbing & Heating Co., 275 M 266, 912 P2d 780, 53

St. Rep. 132 (1996). See also Staples v. Farmers Union Mut. Ins. Co., 2004 MT 108, 321 M 99, 90 P3d 381 (2004), and Newman v. Scottsdale Ins. Co., 2013 MT 125, 370 Mont. 133, 301 P.3d 348.

Indemnification Required for Medical Expenses Incurred Through Insurance Lapse — Payment of Expenses Proper Absent Evidence of Expenses Beyond Indemnification: The parties' dissolution decree required the mother to provide medical insurance for their children and to pay uninsured medical expenses, and the father was required to pay child support and dental and ocular expenses. The mother subsequently lost her medical insurance but failed to notify the father. The mother later sought to hold the father in contempt for failing to provide child support and for unpaid medical expenses. The father asserted that because the mother failed to maintain the required insurance or provide written notice, he was entitled to indemnity from the medical care expenses pursuant to 40-5-822(4). The District Court held that indemnity did not apply and ordered the father to pay 4 months of disputed child support and his portion of uncovered medical expenses, plus the mother's attorney fees. The Supreme Court held that the mother was required by 40-5-822(4) to indemnify the father for health care costs unless she satisfied one of the exemptions in subsection (4) because she permitted the insurance to lapse without securing comparable insurance. Because the written notice required by 40-5-822(4)(b) was not given, the District Court erred as a matter of law in concluding that the mother was not required to indemnify the father for expenses incurred as a result of the failure to maintain insurance. However, the father's argument that he was not obligated to pay any medical expenses following the insurance lapse failed. Section 40-5-822(4) did not require that the mother pay all the medical costs, but only that the father be indemnified, or made whole. Upon proof of the amount owed, the mother was required to pay the father for any additional medical costs incurred to the extent that those expenses were in excess of what the father's obligation would have been if the mother had maintained insurance coverage. The father presented no evidence of such expenses, while the mother presented evidence showing to the penny how much the father was obligated to pay. Thus, the District Court had nothing from which to determine an amount that should be deducted, so the court did not err in ordering the father to pay his share of the medical expenses. In re Marriage of Crone, 2003 MT 238, 317 M 256, 77 P3d 167 (2003).

Judgment — Setoff Based on Stipulation: Plaintiff received a judgment against defendant. Defendant appealed, and the appeal was dismissed with prejudice when defendant advised the court that defendant did not wish to proceed with it. Defendant then filed a motion for a setoff of an amount that plaintiff and defendant were both liable to pay to a third party. Defendant's attorney and plaintiff's attorney had entered into a stipulation that plaintiff was primarily liable and defendant secondarily liable for that amount and that if defendant paid it, the payment would be set off against any judgment granted plaintiff against defendant. The lower court properly set off that amount as partial satisfaction of the judgment. Although the motion was not made within the time required by the rules, it was properly considered because the Clerk of Court did not give defendant notice of entry of the judgment against defendant; therefore, the time for filing the motion had not commenced to run, since the motion was to be made within a certain time from the notice of entry of judgment. AAR Constr., Inc. v. Fergus Elec. Co-op., Inc., 215 M 102, 695 P2d 819, 42 St. Rep. 214 (1985).

Subcontractor to Indemnify Contractor: The contract between Wright, the general contractor, and DeBeer, the subcontractor, contained an indemnity provision. An employee of DeBeer's was injured and recovered a judgment against Wright. Wright sued to enforce the indemnity clause. The Supreme Court found that the clause included not only the negligence of DeBeer but also that of Wright. It made no difference whether Wright was actively or passively negligent. Further, a covenant not to sue between the employee and DeBeer had no effect on the operation of the clause. Howard S. Wright Constr. Co. v. DeBeer Mechanical Constr. Co., 185 M 47, 604 P2d 323 (1979), distinguished in Slater v. Cent. Plumbing & Heating Co., 275 M 266, 912 P2d 780, 53 St. Rep. 132 (1996).

Contractor's Indemnity to Subcontractor: When subcontractor was required to perform in accordance to contractor's deficient design and home owners had judgment against him, he had right to indemnification against contractor. Miller v. Melaney, 172 M 74, 560 P2d 902 (1977).

Dividend Guaranty Note: When for the purpose of inducing the purchase of corporate stock the seller gave the buyer a promissory note payable in 3 years, the back of which bore the endorsement that when the stock had paid dividends to the amount of the purchase price the note should be void, the agreement evidenced by the note and endorsement was one of indemnity within the meaning of this section and not of guaranty. Peterson v. Nelson, 77 M 539, 252 P 368 (1926).

28-11-302. Indemnity for future unlawful act void.

Case Notes

Inapplication to Torts: This section applies only to conduct defined as criminal; it does not apply to tortious conduct. First Bank of Billings v. Transamerica Ins. Co., 209 M 93, 679 P2d 1217, 41 St. Rep. 573 (1984).

Insurance Coverage of Punitive Damages — Not Violative of Public Policy: Punitive damages may be insured against in Montana, and insurance coverage of such damages does not violate public policy. First Bank of Billings v. Transamerica Ins. Co., 209 M 93, 679 P2d 1217, 41 St. Rep. 573 (1984).

Indemnity for All Injuries Not in Contravention of Law: Tenant's agreement to save the railroad, the landlord, harmless from all injuries due to the negligence of the railroad or its employees, and to maintain insurance protecting the railroad, did not contravene Montana law that all contracts for exempting anyone from responsibility for his own fraud, willful injury to personalty, or law violation are against public policy. Ryan Mercantile Co. v. Great N. Ry., 294 F2d 629 (9th Cir. 1961), followed in Sweet v. Colborn School Supply, 196 M 367, 639 P2d 521, 39 St. Rep. 168 (1982).

Effect of Trespass: An implied promise to indemnify a Sheriff for making an attachment was not void under this section when the rights of the rival claimants to the attached personalty were not clear. Weir v. Hum Tong, 100 M 1, 46 P2d 45 (1935).

Implied Indemnity Agreement Sustained: A Sheriff attached furniture on instructions of attaching creditor. Later in conversion suit some of the furniture was held exempt and claimant awarded damages against Sheriff for its retention. In Sheriff's action to recover from attaching creditor on implied promise of indemnity the claim of the attaching creditor that officer knew his act was unlawful and the indemnity agreement was therefore void under this section was without merit. Weir v. Hum Tong, 100 M 1, 46 P2d 45 (1935).

28-11-304. Indemnity extended to acts of agents.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

Case Notes

Contractor's Indemnity to Subcontractor: When subcontractor was required to perform in accordance to contractor's deficient design and home owners had judgment against him, he had right to indemnification against contractor. Miller v. Melaney, 172 M 74, 560 P2d 902 (1977).

28-11-305. Indemnification of several persons.

Case Notes

Agreement Determines Scope: An agreement requiring the tenant to save the railroad (the landlord) harmless from any and all injuries, whether due to negligence of the railroad, its contractors, officers, agents, and employees, and to defend the railroad against any action because of such injuries, required the tenant to defend an action for injuries against the railroad based solely on the negligence of railroad employees at a place where the railroad had a duty under Montana law to provide safeguards. Ryan Mercantile Co. v. Great N. Ry., 294 F2d 629 (9th Cir. 1961).

28-11-311. Person indemnifying liable jointly and severally.

Compiler's Comments

1997 Amendment: Chapter 429 in exception clause inserted "and 27-1-705"; and made minor changes in style. Amendment effective on occurrence of contingency.

Preamble: The preamble attached to Ch. 429, L. 1997, provided: "WHEREAS, efforts of the Legislature to amend the comparative negligence statute, which is premised on a modified joint and several liability scheme, have repeatedly been struck down by the Montana Supreme Court; and

WHEREAS, the Montana Supreme Court rulings prohibiting the consideration of fault attributable to nonparties impair the effectiveness of the current modified joint and several liability system in Montana; and

WHEREAS, the Legislature intends that the policy of the state should be a system of comparative fault in which persons are held responsible only to the extent to which they cause or contribute to the harm; and

WHEREAS, the current system of joint and several liability, which apportions all liability only among parties to the action, fails to apportion liability among all tortfeasors according to their equitable share of fault; and

WHEREAS, the Legislature recognizes that public policy favors fair settlements that accurately reflect the liability of settled or released parties; and

WHEREAS, the Legislature is concerned with the present inequitable results of solvent defendants having to pay for the liability of insolvent, immune, or settled parties; and

WHEREAS, the present system of joint and several liability for all tort actions does not reflect the state's policy of liability in proportion to fault; and

WHEREAS, the Legislature recognizes that joint and several liability should be retained for certain situations; and

WHEREAS, at least ten other states have abrogated the doctrine of joint and several liability, except for specific situations; and

WHEREAS, the Legislature has the power to alter tort causes of action to promote legitimate state interests.

THEREFORE, the Legislature declares that the doctrine of joint and several liability is abolished, except for specific causes of action, and is replaced with a comparative fault system utilizing the principles of several liability."

Severability: Section 9, Ch. 429, L. 1997, was a severability clause.

1987 Amendment: At beginning inserted exception clause.

Case Notes

Indemnification Action — Defense of Contributory Negligence Unavailable: Contributory negligence is not available in Montana as a defense in an action for indemnification. Jones v. Aero-Chem Corp., 680 F. Supp. 338, 45 St. Rep. 360 (D.C. Mont. 1987).

Action Against Insurance Company Not Maintainable Until Liability of Insured Adjudicated: This section declaring that the insurer is jointly liable with the indemnitee does not operate prior to an adjudication of liability against the insured. Conley v. USF&G Co., 98 M 31, 37 P2d 565 (1934).

"An Act to Be Done": The phrase "an act to be done", as used in this section, with reference to which the indemnity exists, clearly implied an act the nature of which is known to the parties and one which is yet anticipated. It also strongly implies that the liability contemplated is to accrue from the doing of the act and not upon the contract of indemnity. Conley v. USF&G Co., 98 M 31, 37 P2d 565 (1934); Cummings v. Reins Copper Co., 40 M 599, 107 P 904 (1910).

Declaratory of the Common Law: This section is simply declaratory of the common law and has no application to a case in which one company has contracted to indemnify another employing company for damages to its employees; one of the companies, if answerable at all, is liable for contract; the other for a tort. Cummings v. Reins Copper Co., 40 M 599, 107 P 904 (1910).

General Import of Section: The import of this section is that the indemnitor gives a bond, in consideration of which the indemnitee agrees or is induced to act, or to refrain from acting, to the injury of a third person. Northam v. Cas. Co. of Am., 177 F 981 (9th Cir. 1909).

"To Be Done By": The phrase "to be done by", as used in this section, implies on the part of the indemnitee an agreement or obligation to commit the tort in question, as if the phrase were "an act required (or demanded or requested) to be done by" the indemnitee and, as so construed, the section is merely declaratory of the common law. Northam v. Cas. Co. of Am., 177 F 981 (9th Cir. 1909).

28-11-312. When person indemnifying entitled to reimbursement.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Law Review Articles

Contribution and Indemnity Among Tortfeasors, Franks, 31 Mont. L. Rev. 69 (1969).

28-11-313. Interpretation of contract of indemnity.

Case Notes

Liberal Interpretation: Indemnity clauses in contracts should be liberally construed in favor of the party intended to be indemnified. To indemnify a party against his own negligence, the indemnity must be expressed in clear and unequivocal terms. The indemnity provision in a contract between a highway contractor and the State Highway Commission (now Transportation Commission) holding the contractor solely responsible in areas of high voltage electric cables was not for the benefit of the contractor's deceased employee. The widow of the employee sued the electric company for wrongful death. The company could not bring a third-party action against the contractor under the indemnity provisions of the contract. Lesofski v. Ravalli County Elec. Co-op, 151 M 104, 439 P2d 370 (1968), followed in Slater v. Cent. Plumbing & Heating Co., 1999 MT 257, 297 M 7, 993 P2d 654, 56 St. Rep. 1023 (1999).

Indemnity — Construction of Lease: A clause in an instrument covering the lease of equipment provided that the lessee assumed all liability arising from the use of the equipment and growing out of any cause, including defective equipment. An injury was sustained by one of lessee's employees. Lessee's liability for the injury resulting from defective equipment was not limited to workers' compensation. The measure of damages was whatever lessor might properly pay in settlement of the action against it by the employee, plus interest and reasonable expenses. The indemnity clause was valid. W. Constr. Equip. Co. v. Mosby's, Inc., 146 M 313, 406 P2d 165 (1965), followed in Wash. Water Power Co. v. Morgan Elec. Co., 152 M 126, 448 P2d 683 (1968).

Agreement to Determine Scope: An agreement requiring the tenant to save the railroad (the landlord) harmless from any and all injuries, whether due to negligence of the railroad, its contractors, officers, agents, and employees, and to defend the railroad against any action because of such injuries, required the tenant to defend an action for injuries against the railroad based solely on the negligence of railroad employees at a place where the railroad had a duty under Montana law to provide safeguards. Ryan Mercantile Co. v. Great N. Ry., 294 F2d 629 (9th Cir. 1961).

Liberal Construction: An indemnity contract must be liberally construed in favor of the party intended to be indemnified, and so as to best effectuate and carry into operation the reasonable intention of the parties. The construction of the contract of indemnity here, which in effect permitted the contribution by one tortfeasor from his joint tortfeasor, contrary to the established rule which denied such right, was not contrary to public policy. Union Elec. Co. v. Lovell Livestock Co., 93 M 577, 20 P2d 255 (1933).

28-11-314. When and what person indemnified entitled to recover.

Case Notes

Failure to Notify of Challenge to Right to Indemnification Prior to Settlement — Indemnification for Wage Loss and Medical Benefits Required: Plaintiff's employee Salazar was injured while a passenger on defendant's transportation service, and Salazar's care was managed by plaintiff's federally approved wellness program. Salazar agreed to drop claims against plaintiff and the contractor that provided the transportation service, and plaintiff then cross-claimed for indemnification from the contractor. The contractor was subsequently ordered to indemnify plaintiff for part of the settlement, and the contractor appealed, seeking equitable relief. The Supreme Court affirmed. The program administrator failed to request an independent medical examination to separate the work-related claims from claims related to the accident, which arguably increased the contractor's risk of loss beyond what the contractor agreed to indemnify, but the contractor failed to notify plaintiff prior to settlement that the contractor would challenge plaintiff's right to indemnification, so the contractor did not come to court with clean hands and could not avail itself of the equitable relief of discharge from the obligation to indemnify plaintiff. Mont. Rail Link v. CUSA PRTS, LLC, 2009 MT 432, 354 M 101, 222 P3d 1021 (2009). See also Seifert v. Seifert, 173 M 501, 568 P2d 155 (1977), and Cowan v. Cowan, 2004 MT 68, 320 M 332, 87 P3d 443 (2004).

Indemnification Provisions — "Clear and Unequivocal" Standard: A contract provision that required the subcontractor to indemnify the general contractor for damages arising out of the subcontractor's negligence did not require the subcontractor to indemnify the general contractor for the general contractor's own negligence. Contractual provisions that indemnify a party for its own negligence must be "clear and unequivocal" to be enforceable. The general contractor was found negligent per se under Title 50, ch. 77, part 1, commonly known as the Montana Scaffolding Act. The general contractor could not use the indemnification clause of the contract in order to recover against the subcontractor. Slater v. Cent. Plumbing & Heating Co., 275 M 266, 912 P2d 780, 53 St. Rep. 132 (1996). Following the 1996 decision (Slater I), the general contractor sought contribution from the subcontractor for that portion of liability attributable to the subcontractor. The District Court held that Slater I closed all the general contractor's doors of recovery from the subcontractor under any theory. However, the motion for partial summary judgment that gave rise to Slater I was based on the first claim of the general contractor's amended cross-claim and only precluded indemnification for the general contractor's own negligence under a breach of contract claim, but the general contractor was not precluded by the prohibition against splitting a cause of action or by the doctrine of res judicata from pursuing a separate claim for contribution under the second claim of its amended cross-claim. The issue of indemnity based on the subcontractor's negligence was not the same as the previously decided issues regarding whether there was an indemnity claim based on the general contractor's negligence or a breach of contract in relation to the safety provisions. Thus, the case was remanded for further proceedings on the remaining claims. Slater v. Cent. Plumbing & Heating Co., 1999 MT 257, 297 M 7, 993 P2d 654, 56 St. Rep. 1023 (1999).

Liability Insurance — Recovery on Policy Not Defeated by Negligence of Insured: Insurer brought declaratory judgment action against insured for indemnity on basis that gasoline leakage was not covered by policy. In Town Pump, Inc. v. Diteman, 622 P2d 212, 38 St. Rep. 54 (1981), the insured had been denied indemnity coverage against its contractor for the same gasoline leakage because of the insured's own negligence. The District Court found insured 50% negligent and ordered recovery on that basis. The Supreme Court reversed the District Court decision and ordered full recovery for insured against insurer on the basis that mere negligence of a policyholder is not a defense to enforcement of a policy and full recovery by an insured is in order in the absence of a cooperation clause or allegations of intentional wrongdoing. Gen. Ins. Co. of Am. v. Town Pump, Inc., 214 M 27, 692 P2d 427, 41 St. Rep. 2292 (1984).

Finding a Partnership — Splitting of Profits, Advertising, and Merging of Resources and Talents — Lack of Intent Not Controlling: Father and son shared equipment as needed, stored seed potatoes together in son's warehouse, advertised under the name of "Wilbur Kimm and Son", and split profits in a joint account. Son's insurer sued father's insurer for contribution for claims paid that were filed by buyers against son for crop damages caused by seeds treated by son. District Court found no partnership existed, primarily based on father's and son's testimony that they did not intend for a partnership to exist. The Supreme Court reversed and ordered judgment granting plaintiff insurer's motion for summary judgment. The Supreme Court held that splitting of profits, coupled with advertising under a joint name and the merging of resources and talents for the growing of the potatoes, preponderates against the District Court's finding of no partnership. Truck Ins. Exch. v. Indus. Indem. Co., 212 M 297, 688 P2d 1243, 41 St. Rep. 1835 (1984).

Indemnity for Own Negligent Act: An indemnity agreement for damages caused by negligent acts of the indemnitee must be in clear and unequivocal terms. Sweet v. Colborn School Supply, 196 M 367, 639 P2d 521, 39 St. Rep. 168 (1982), followed in Slater v. Cent. Plumbing & Heating Co., 275 M 266, 912 P2d 780, 53 St. Rep. 132 (1996).

No Right of Indemnity Where Plaintiff Is Negligent: In an indemnity action the negligent conduct of plaintiff precludes recovery from the defendant, a construction contractor hired by plaintiff, of damages paid to a third party. The right of indemnity exists for the benefit of plaintiff if, without wrongful conduct on its part, it was liable to pay damages caused by the negligence of defendant and the liability to pay damages arose from the breach by defendant of an implied contractual duty owed to plaintiff. Town Pump v. Diteman, 180 M 358, 590 P2d 1126, 38 St. Rep. 54 (1981).

Consideration for and Enforcement of Implied Indemnity: Defendant, special administratrix of an estate, had a deposit as such in a bank, and Weisner, claiming to have been appointed special administrator, made demand for payment to him of the sum deposited. The bank notified defendant of this demand, and she requested it to refuse the demand and retain the deposit in her name until it could be ascertained who was entitled to it. The bank relied upon her implied promise to indemnify and save it harmless from all damage by reason of its compliance with her request, and refusal to comply with Weisner's demand. This constituted a good consideration for the implied promise, that is, a benefit conferred on Mrs. Nett and a prejudice suffered by the bank. Mrs. Nett was subsequently removed from her office and, after her removal, Weisner recovered judgment against the bank for the amount of the deposit with interest from the date of his demand. Mrs. Nett was not liable to reimburse the bank for the amount paid as interest, it having been the bank's duty without request to retain the deposit to meet its obligation to her. Murphy v. Nett, 51 M 82, 149 P 713 (1915).

28-11-315. Costs of defense.

Case Notes

No Award of Attorney Fees Absent Basis in Indemnification Provision: The District Court held that defendant was required to indemnify plaintiff for medical care and that plaintiff was entitled to attorney fees and costs pursuant to 28-11-315. Defendant appealed and the Supreme Court reversed in part. The indemnification provision did not specifically provide for an award of attorney fees, and the court declined to adopt an exception to the American Rule that allows attorney fees in contract actions only if specifically allowed by the contract. Additionally, 28-11-315 addresses only costs, not attorney fees, so the section did not provide a statutory basis for the award of attorney fees in the indemnification action. On remand, plaintiff was entitled to costs but not attorney fees. Mont. Rail Link v. CUSA PRTS, LLC, 2009 MT 432, 354 M 101, 222 P3d 1021 (2009).

Contractual Indemnity Clear — Costs and Attorney Fees for Defending Suit: A contract's indemnity provision stated that contractor indemnified client for costs and reasonable attorney fees arising in whole or in part from contractor's negligence and that client indemnified contractor for costs and reasonable attorney fees arising solely from client's negligence. In a suit against both of them, client's request that the contractor defend was refused. Client defended, and contractor was ordered to pay client's costs and reasonable attorney fees. For purposes of appeal, contractor admitted it was at least partially negligent. Contractor's claim that client was not indemnified for client's negligence was denied. If both were negligent or if contractor was solely negligent, client was entitled to recover its costs and reasonable attorney fees under the indemnity agreement. Amazi v. Atl. Richfield Co., 249 M 355, 816 P2d 431, 48 St. Rep. 737 (1991).

Right to Indemnity for Costs and Attorney Fees Incurred in Proving Right to Indemnity: A provision that contractor indemnified client, including indemnity for costs, attorney fees, judgments, settlements, and other similar or dissimilar related expenses, was merely one provision in a contract to perform geophysical exploration. Because client was not expressly indemnified for establishing the right to indemnification, client was not entitled to be indemnified for costs and attorney fees client incurred in proving client's right to indemnity under the contract. The court rejected client's claim that the indemnity provision was similar to a contract of insurance and that therefore client was entitled to costs and attorney fees for proving client's indemnity right. The court also rejected the claim that the "related expenses" clause should be liberally construed to require indemnity for costs and attorney fees incurred in proving the right to indemnity. Amazi v. Atl. Richfield Co., 249 M 355, 816 P2d 431, 48 St. Rep. 737 (1991).

28-11-316. Duty of person indemnifying to defend.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

No Duty to Defend Against Slander Claim When Claim in Underlying Lawsuit Undated — Not Alleged to Have Been Committed During Insurance Policy Periods. Farmers Ins. Exch. v. Minemyer, 2023 MT 138, 413 Mont. 60, 532 P.3d 837.

No Duty to Defend or Indemnify — Claims Outside of Policy Coverage — Summary Judgment in Favor of Insurer Proper. Christian v. United Fire & Cas. Co., 2023 MT 100, 412 Mont. 340, 530 P.3d 456.

Minor Filmed in Shower at Insured's Home — Consent Judgment for Minor's Emotional Damages — District Court Finding That Insurer Properly Rejected Duty to Defend — Claims Expressly Excluded in Policy — Affirmed on Appeal. R.S. v. United Serv. Auto. Ass'n, 2022 MT 68, 408 Mont. 195, 507 P.3d 565.

Delay in Seeking Declaratory Judgment — Breach of Duty to Defend: The plaintiff insurance company provided the defendant, the state of Montana, with a comprehensive general liability policy from 1973 to 1976. In 2000, Libby Mine claimants started suing the state for its regulatory role of the Libby Mine based on the theory that the state had failed to warn them of the danger of asbestos exposure. In 2006, the insurance company offered a tender of a full defense to the state subject to a reservation of rights. The state rejected the offer and continued defending itself against the asbestos claims. Six years after offering to defend subject to a reservation of rights, the plaintiff sought a declaratory judgment over its rights and duties under the liability policy. The District Court held that the plaintiff had breached its duty to defend, not by reserving its rights but by its 6-year delay in seeking judicial resolution of its reserved coverage issues. On appeal, the Supreme Court agreed that the delay constituted a breach and affirmed. Nat'l Indemnity Co. v. St., 2021 MT 300, 406 Mont. 288, 499 P.3d 516.

Offer of Pro Rata Defense — Breach of Duty to Defend — Reservation of Rights, No Breach Proper: The plaintiff insurance company provided the defendant with a comprehensive general liability policy from 1973 to 1976. In 2000, Libby Mine claimants started suing the state for its regulatory role of the Libby Mine based on the theory that the state had failed to warn them of the danger of asbestos exposure. In 2002, the state tendered the claims to the plaintiff while the state was defending against the claims, and ultimately, the plaintiff sought a declaratory judgment over its rights and duties under the liability policy. The District Court concluded that the plaintiff had breached its duty to defend in 2005 when the plaintiff told the state it would pay only a share of defense costs. However, the District Court held that the plaintiff had not breached its duty when it later offered the state a full defense under a reservation of rights. On appeal, the Supreme Court affirmed. Nat'l Indemnity Co. v. St., 2021 MT 300, 406 Mont. 288, 499 P.3d 516.

Declaratory Judgment Action — Duty of Insurer to Defend and Indemnify — District Court Error as Matter of Law: The plaintiff, an insurance company, filed an action for declaratory judgment that it did not have a duty to defend or indemnify the defendants in a wrongful death lawsuit. The District Court denied the motion for summary judgment and held that the plaintiff had a duty to defend one of the defendants as an additional insurer under the policy. On appeal, the Supreme Court reversed, holding that the District Court erred as a matter of law and that the defendant did not meet the contractual requirement to be an automatic additional insured under the policy. Employers Mut. Cas. Co. v. Estate of Buckles, 2019 MT 136, 396 Mont. 153, 443 P.3d 534.

Sexual Harassment Claims by Court Reporter Against State Judge — State Not Obligated to Pay Settlement Made Without Its Consent: A court reporter filed a claim of sexual harassment against the District Court judge for whom she worked. The judge sought the costs of his defense, as well as indemnification, from the state. Eventually, the court reporter and the judge mediated the matter, with the state refusing to participate, and they entered into a settlement agreement. The state then filed a request seeking a judicial declaration that the state was not obligated to pay the settlement because the judge's harassment of the court reporter was not within the course and scope of his employment. The District Court ruled that the state was not obligated to pay the settlement because the judge had settled without the consent of the state as provided in 2-9-305(6)(c). The court reporter appealed and the Supreme Court affirmed, agreeing that the state was not obligated to pay the settlement because it had not agreed to it as required by law. St. v. Berdahl, 2017 MT 26, 386 Mont. 281, 389 P.3d 254.

Amount of Settlement Contested by Insurer — Potential for Windfall for Plaintiff — Error to Deny Reasonableness Hearing and Discovery: The plaintiff sued several defendants related to the alleged defective construction of a building. During the construction, the contractor was insured by two different insurers during different time spans. The defendant contractor attempted to seek coverage and defense from one of its insurers, who denied coverage. The other insurer tendered a defense for the contractor under a reservation of rights. Ultimately, the contractor settled with the plaintiff for more than $5 million and assigned his rights to the plaintiff, who then filed suit against the insurer, alleging it was liable to pay the settlement. The District Court ordered the insurer to pay the settlement. The insurer unsuccessfully requested a hearing on the reasonableness of the amount of the settlement and to conduct discovery related to the reasonableness determination. On appeal, the Supreme Court reversed, holding that the insurer had shown that the plaintiff was possibly receiving a $2 million windfall under the settlement. The court remanded the matter for discovery and a hearing on the reasonableness of the settlement amount. J & C Moodie Properties, LLC v. Deck, 2016 MT 301, 385 Mont. 382, 384 P.3d 466.

Duty to Defend Breached — Insured Represented by Another Insurer Under Reservation of Rights: The plaintiff sued several defendants related to the alleged defective construction of a building. During the construction, the contractor was insured by two different insurers during different time spans. The defendant contractor attempted to seek coverage and defense from one of its insurers, who denied coverage. The other insurer tendered a defense for the contractor under a reservation of rights. Ultimately, the contractor settled with the plaintiff and assigned his rights to the plaintiff, who then filed suit against the insurer who had denied coverage, alleging it had breached its duty to defend and was liable to pay the settlement. The District Court ruled that the insurer had breached its duty to defend and ordered the insurer to pay the settlement. On appeal, the Supreme Court affirmed, holding that the insurer was not absolved of its duty to defend simply because the insured was being represented by another insurer under a reservation of rights. J & C Moodie Properties, LLC v. Deck, 2016 MT 301, 385 Mont. 382, 384 P.3d 466.

Policy Limiting Coverage to Accidents May Include Intentional Acts — Summary Judgment Improper — Remanded to Determine Whether Damages Were Not Objectively Intended or Expected: The plaintiff insurer defended the defendant insured in a negligence case under a reservation of rights and initiated a declaratory action to determine whether the policy provided coverage for the claim under which it had a duty to indemnify the insured. At issue in the declaratory action was the interpretation of the term "occurrence" and, correspondingly, its common policy definition as an "accident," and whether an intentional act could be considered an "accident" for purposes of insurance coverage. The Supreme Court held that the policy language defining "accidents" may have included intentional acts if the damages were not objectively intended or expected by the insured. Given the testimony, the Supreme Court determined there were issues of material fact that precluded summary judgment and that further proceedings were necessary to resolve factual issues related to application of the coverage provisions of the policy. Employers Mut. Cas. Co. v. Fisher Builders, Inc., 2016 MT 91, 383 Mont. 187, 371 P.3d 375, distinguished in Huckins v. United Servs. Auto. Ass'n, 2017 MT 143, 387 Mont. 514, 396 P.3d 121. See also Blair v. Mid-Continent Cas. Co., 2007 MT 208, 339 Mont. 8, 167 P.3d 888, Millers Mut. Ins. Co. v. Strainer, 204 Mont. 162, 663 P.2d 338 (1983), and NW. Nat'l Cas. Co. v. Phalen, 182 Mont. 448, 597 P.2d 720 (1979).

Negligence Claims Related to Breach of Contract by County — No Duty to Defend Pursuant to Policy Exclusions: Beaverhead County was sued by a contractor for breach of contract and negligence in preparing bid documents. The county submitted the lawsuit to its insurer, the Montana Association of Counties, and asked it to indemnify the county and defend it against the suit. The association denied coverage based on the county's insurance policy, which specifically excluded coverage for any claims arising out of a claim for breach of contract. The county filed suit against the association for failing to defend it. The District Court granted summary judgment in favor of the association and the county appealed. The Supreme Court affirmed, agreeing that because the negligence claims arose from the county's alleged breach of contract, no coverage existed under the policy. Beaverhead County v. Mont. Ass'n of Counties, 2014 MT 267, 376 Mont. 413, 335 P.3d 721.

Breach of Duty to Defend — No Analysis of Coverage Under Policy: Shareholders sued two corporate officers for breach of their corporate duties related to a merger. Initially, the carrier of the corporation's corporate liability insurance policy covered the defense costs for the two officers. Later, however, the carrier informed counsel for the officers that it would discontinue paying their defense costs. Shortly thereafter, the officers entered into a stipulation with the shareholders in which the officers assigned their rights to the shareholders and agreed that the shareholders were entitled to $29 million in damages. The carrier argued that there was no coverage under the policy. However, the District Court concluded, and the Supreme Court agreed, that because the carrier unjustifiably refused to defend the officers, it was estopped from denying coverage under the policy. Tidyman's Management Serv. v. Davis, 2014 MT 201, 376 Mont. 72, 330 P.3d 1135.

No Breach of Duty to Defend When Insured Fully Defended — Duplicative Counsel by Coinsurer Unnecessary: The parents of a woman who died in a car accident sought compensation from two different insurers of the driver's parents and his estate. The two insurers worked together to ensure that their insureds were defended, although only one of the insurers paid the costs of counsel. As a part of a consent judgment, the rights of the insureds were assigned to the decedent woman's parents. The parents then argued that the insurer who did not pay the costs of defending had breached its duty to defend and was estopped from denying coverage. The District Court agreed and granted the parents summary judgment. The District Court also ordered the insurer to pay the full amount of the consent judgment as well as attorney fees and costs. On appeal, the Supreme Court reversed, ruling that as long as the insureds were fully defended, the duty to defend did not require both insurers to provide separate counsel when their combined efforts would be duplicative. St. Farm Fire and Cas. Co. v. Schwan, 2013 MT 216, 371 Mont. 192, 308 P.3d 48.

Presence of Insurance Adjuster Rather Than Attorney at Prelitigation Mediation Conference Not Violative of Insurer's Duty to Defend: An insurer sent an insurance adjuster rather than an attorney to a prelitigation mediation conference. Defendant contended that this violated the insurer's statutory duty to defend under the policy. The District Court held that the insurer met its obligation by actively participating in the mediation, and defendant appealed. The Supreme Court noted that the duty to defend encompasses functions that can only be fulfilled by a licensed attorney, but that insurance adjusters play a vital role in the resolution of claims prior to the initiation of litigation and further noted that public policy encourages settlements and avoiding unnecessary litigation. Requiring that counsel be retained for informal settlement conferences could hinder the negotiation process and contravene the policy of encouraging out-of-court settlements. The mediation was not part of any judicial proceeding, and the insurer did not violate its duty to defend by sending an insurance adjuster to mediation. The District Court was affirmed. Farmers Ins. Exch. v. Johnson, 2009 MT 442, 354 M 192, 224 P3d 613 (2009).

Additional Insured Endorsement in Primary Policy — Duty to Defend: An employee of a subcontractor was injured while installing fireproofing in a building. The general contractor's liability insurer (defendant insurer) tendered a defense to the subcontractor under the indemnity clause in the subcontract and to the general contractor's insurer (plaintiff insurer) under the commercial general liability policy, so the question arose whether plaintiff insurer had a duty to defend pursuant to the commercial liability under which the general contractor qualified as an additional insured. Plaintiff insurer argued that because the general contractor could not shift responsibility to the subcontractor for the general contractor's statutory duty to maintain general job site safety, plaintiff insurer had no duty to defend or cover the loss. The District Court disagreed and granted summary judgment to defendant insurer pursuant to the additional insured endorsement. Plaintiff insurer appealed, but the Supreme Court affirmed. The court examined the indemnity provision in the subcontract and determined that the indemnity provision was not sufficiently clear and unequivocal in its intent to indemnify the general contractor for its own negligence, so the court then turned to the language of the additional insured endorsement. The general contractor was clearly named as an additional insured on a primary noncontributing basis, so plaintiff insurer's policy was clearly intended to be primary. Because plaintiff insurer had a duty to defend the general contractor, the District Court did not err in granting defendant insurer's motion for summary judgment and holding that plaintiff insurer breached its duty to defend. United Nat'l Ins. Co. v. St. Paul Fire & Marine Ins. Co., 2009 MT 269, 352 M 105, 214 P3d 1260 (2009), following Slater v. Cent. Plumbing & Heating Co., 275 M 266, 912 P2d 780, 53 St. Rep. 132 (1996). See also Staples v. Farmers Union Mut. Ins. Co., 2004 MT 108, 321 M 99, 90 P3d 381 (2004), and Newman v. Scottsdale Ins. Co., 2013 MT 125, 370 Mont. 133, 301 P.3d 348.

No Duty of Insurer to Defend or Indemnify Contractor Protected From Liability: An employee of a subcontractor sued plaintiff for negligence, but plaintiff's insurers and the contractor's insurer refused to defend and indemnify against the claim. The District Court granted summary judgment to the contractor's insurer, and the employee appealed. The Supreme Court affirmed. The contractor was protected from liability under 39-71-411. Because the contractor was not sued for its own negligence or found liable for any tortious conduct, its insurer had no duty to defend or indemnify plaintiff under the insurance policy or its endorsements. Plum Creek Marketing, Inc. v. Am. Economy Ins. Co., 2009 MT 264, 352 M 56, 214 P3d 1238 (2009), followed in F.H. Stoltze Land & Lumber Co. v. Am. States Ins. Co., 2015 MT 165, 379 Mont. 409, 352 P.3d 612.

Insurer Duty to Defend Against Subcontractor-Caused Damages From Faulty Product Provided by Subcontractor Under Policy Conditions: Defendant insurer contended that it had no duty to defend against subcontractor-caused damages. Generally, an insurer has no duty to defend the insured if there is no liability to the insured under the policy provisions. However, in this case plaintiff's subcontractor provided a faulty product that was passed on to and accepted by plaintiff before the defect was discovered. The insurer had knowledge of the subcontractor involvement even though it was not mentioned in the complaint. Under these circumstances, the policy provided coverage for the subcontractor-caused damages, and the insurer had a duty to defend and indemnify plaintiff. The District Court's holding that there was no duty to defend was reversed and the case was remanded for further proceedings. Revelation Indus., Inc. v. St. Paul Fire & Marine Ins. Co., 2009 MT 123, 350 M 184, 206 P3d 919 (2009). See also NW. Nat'l Cas. Co. v. Phalen, 182 M 448, 597 P2d 720 (1979), and Geraldine v. Mont. Municipal Ins. Authority, 2008 MT 411, 347 M 267, 198 P3d 796 (2008).

No Breach of Duty to Defend When Claim Excluded Under Policy's Breach of Contract Provision: Plaintiff town entered a contract with a drilling company. The mayor allegedly instructed the company to perform work beyond the scope of the contract and said the town would pay for the work. When the town refused to pay, the company sued for breach of contract. The town then contacted defendant insurer, requesting a defense and indemnification, but the insurer refused coverage. The District Court held that the insurer did not have a duty to defend or indemnify. On appeal, the Supreme Court affirmed. The policy contained exclusions for nonmonetary damages, punitive damages, breach of contract, and liability based on estimated probable costs or faulty bid specifications. The complaint against the town alleged breach of contract, negligent misrepresentation, and constructive fraud. Despite the town's assertion that legal theories and conclusory language in the complaint formed the basis for coverage, the basis for coverage is the acts giving rise to the complaint, and in this case the actions of the mayor were all grounded in contract and thus fell within the policy exclusions, so the insurer had no duty to defend. Additionally, the company's constructive fraud complaint failed to state fraudulent circumstances with particularity and thus was inadequately pleaded, so the insurer had no duty to defend the claim. Geraldine v. Mont. Municipal Ins. Authority, 2008 MT 411, 347 M 267, 198 P3d 796 (2008).

Claim Outside Policy Coverage — No Duty to Defend: The Twites, who built housing complexes, were sued for failure to construct a housing complex in conformity with state and federal requirements to provide equal use and access for persons with disabilities. The Twites had a commercial insurance policy that required the insurer to defend the Twites against lawsuits alleging bodily injury resulting from accidents. The insurer determined that the claim against the Twites did not involve an injury and refused to defend, so the Twites brought a state action to require the insurer to defend. The District Court examined the policy, found no duty to defend, and granted summary judgment for the insurer, so the Twites appealed, but the Supreme Court affirmed. Liberally construing the policy in favor of finding an obligation to defend, the court nevertheless found that the policy covered only bodily injury caused by an accident, and here no accident occurred. The claim unequivocally fell outside the policy's coverage, so there was nothing for a court to construe and no reason to impose a duty to defend. The Twites failed to raise a genuine issue of material fact, and summary judgment for the insurer was affirmed. Twite Family Partnership v. Unitrin Multi Line Ins., 2008 MT 310, 346 M 42, 192 P3d 1156 (2008).

No Duty of Insurer to Defend for Damages Not Covered in Policy — Summary Judgment Proper: Rumph's insurance policy covered vehicle accidents resulting from garage operations. The insurer denied coverage for damages resulting from an accident in which Rumph's son drove the insured vehicle home after a party. The District Court granted summary judgment to the insurer because the accident was not incidental to garage operations and thus was not covered by the policy. The Supreme Court affirmed, holding that the insurer was not estopped from denying coverage and had no duty to defend when no reference in the complaint was made to anything remotely necessary or incidental to the garage business and that coverage unequivocally did not apply. No material facts precluded summary judgment, and because the accident was not covered, the insurer was not liable for breach of contract or unfair claims and settlement practices. Farmers Union Mut. Ins. Co. v. Rumph, 2007 MT 249, 339 M 251, 170 P3d 934 (2007), followed in Geraldine v. Mont. Municipal Ins. Authority, 2008 MT 411, 347 M 267, 198 P3d 796 (2008).

Policy Limiting Coverage to Accidents Not Applicable to Damage From Intentional Act — No Duty of Insurer to Defend: Blair was sued by his subdivision's architectural control committee for violating a residential covenant by removing and selling gravel from Blair's subdivision property. Blair sought coverage from defendant insurer. The insurer declined coverage and declined to defend Blair in the suit because the policy covered only bodily and property injuries caused by an accident, so Blair sued the insurer. The District Court granted summary judgment to the insurer, and on appeal, the Supreme Court affirmed. Although an insurer has a duty to defend an insured when a complaint alleges facts representing a risk covered by the terms of a policy, in this case Blair deliberately moved gravel on his property, which unequivocally was not an accident, so coverage under Blair's policy did not apply and the insurer had no duty to defend. Blair v. Mid-Continent Cas. Co., 2007 MT 208, 339 M 8, 167 P3d 888 (2007), distinguishing NW. Nat'l Cas. Co. v. Phalen, 182 M 448, 597 P2d 720 (1979), and Lindsay Drilling v. USF&G, 208 M 91, 676 P2d 203 (1984), and followed in Farmers Union Mut. Ins. Co. v. Rumph, 2007 MT 249, 339 M 251, 170 P3d 934 (2007). See also Safeco Ins. Co. of America v. Liss, 2000 MT 380, 303 M 519, 16 P3d 399 (2000), Staples v. Farmers Union Mut. Ins. Co., 2004 MT 108, 321 M 99, 90 P3d 381 (2004), and Employers Mut. Cas. Co. v. Fisher Builders, Inc., 2016 MT 91, 383 Mont. 187, 371 P.3d 375.

Improper Resolution of Disputed Issues of Material Fact Once Insurer's Duty to Defend Established — Reversible Error: A driver was injured when his vehicle struck a horse and filed a claim against Staples, who was allegedly pasturing the horse just prior to the accident. Staples then filed a third-party complaint against the horse owners, claiming that as the horse's custodian, he was an additional insured under the insurance policy of one owner and was entitled to a defense. Defendant insurer unilaterally decided that its insured was not the horse's owner and sought a declaration that it had no duty to defend or provide coverage to Staples. On cross-motions for summary judgment, the District Court found that Staples might be an insured under the policy and that defendant had a duty to defend Staples, but then went on to conclude that because the policyholder did not own the horse at the time of the accident, Staples was not a third-party insured. Therefore, summary judgment was granted to the insurer. On appeal, the Supreme Court reversed. Having correctly determined that the insurer had a duty to defend, the District Court should have ended the analysis and concluded that because the insurer breached that duty, it was estopped from denying coverage and that Staples was entitled to coverage. It was error for the District Court to then proceed to resolve disputed issues of fact in ruling on the summary judgment motion in favor of the insurer. Staples v. Farmers Union Mut. Ins. Co., 2004 MT 108, 321 M 99, 90 P3d 381 (2004), following Independent Milk & Cream Co. v. Aetna Life Ins. Co., 68 M 152, 216 P 1109 (1923), Graber v. St. Farm Fire & Cas. Co., 244 M 265, 797 P2d 214 (1990), Grindheim v. Safeco Ins. Co., 908 F. Supp. 794 (D.C. Mont. 1995), Insured Titles, Inc.

v. McDonald, 275 M 111, 911 P2d 209 (1996), Farmers Union Mut. Ins. Co. v. Horton, 2003 MT 79, 315 M 43, 67 P3d 285 (2003), and Lee v. USAA Cas. Ins. Co., 2004 MT 54, 320 M 174, 86 P3d 562 (2004), and followed in Farmers Union Mut. Ins. Co. v. Rumph, 2007 MT 249, 339 M 251, 170 P3d 934 (2007), and Newman v. Scottsdale Ins. Co., 2013 MT 125, 370 Mont. 133, 301 P.3d 348.

Contractual Indemnity Clear — Costs and Attorney Fees for Defending Suit: A contract's indemnity provision stated that contractor indemnified client for costs and reasonable attorney fees arising in whole or in part from contractor's negligence and that client indemnified contractor for costs and reasonable attorney fees arising solely from client's negligence. In a suit against both of them, client's request that the contractor defend was refused. Client defended, and contractor was ordered to pay client's costs and reasonable attorney fees. For purposes of appeal, contractor admitted it was at least partially negligent. Contractor's claim that client was not indemnified for client's negligence was denied. If both were negligent or if contractor was solely negligent, client was entitled to recover its costs and reasonable attorney fees under the indemnity agreement. Amazi v. Atl. Richfield Co., 249 M 335, 816 P2d 431, 48 St. Rep. 737 (1991).

Right to Indemnity for Costs and Attorney Fees Incurred in Proving Right to Indemnity: A provision that contractor indemnified client, including indemnity for costs, attorney fees, judgments, settlements, and other similar or dissimilar related expenses, was merely one provision in a contract to perform geophysical exploration. Because client was not expressly indemnified for establishing the right to indemnification, client was not entitled to be indemnified for costs and attorney fees client incurred in proving client's right to indemnity under the contract. The court rejected client's claim that the indemnity provision was similar to a contract of insurance and that therefore client was entitled to costs and attorney fees for proving client's indemnity right. The court also rejected the claim that the "related expenses" clause should be liberally construed to require indemnity for costs and attorney fees incurred in proving the right to indemnity. Amazi v. Atl. Richfield Co., 249 M 335, 816 P2d 431, 48 St. Rep. 737 (1991).

Burden of Proof:

In an action on an indemnity policy, the burden is upon the insurer to rebut the presumption provided for by this section, that if after request the insurer neglects to defend the person indemnified, a recovery against the latter suffered by him in good faith is conclusive in his favor against the insurer. Independent Milk & Cream Co. v. Aetna Life Ins. Co., 68 M 152, 216 P 1109 (1923), followed in Lee v. USAA Cas. Ins. Co., 2004 MT 54, 320 M 174, 86 P3d 562 (2004). See also Grindheim v. Safeco Ins. Co. of America, 908 F. Supp. 794 (D.C. Mont. 1995).

The burden is on the indemnifying person in a suit on the contract of indemnity to rebut the presumption raised by this section. Butte v. Cook, 29 M 88, 74 P 67 (1903).

Cosurety's Signature as Condition: When the names of two sureties appear in the body of an indemnifying bond, which is however signed by but one, the condition of the bond is notice to the obligee, so as to permit the defense, by the surety signing, that his liability was conditioned on obtaining the signature of his cosurety. Butte v. Cook, 29 M 88, 74 P 67 (1903).

28-11-317. When judgment not conclusive against person indemnifying.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Determination in First Proceeding Binding Upon Second: Where the driver and manufacturer of an automobile which overturned, killing the passenger, were first found jointly liable for damages for the passenger's death, and the driver's insurer thereafter instituted a second action against the manufacturer in which it sought indemnity for amounts paid to satisfy the judgment against the driver and the costs incurred in defending the first suit, the jury finding in the first suit that the driver had been grossly negligent was binding in the second action under the doctrine of res judicata and precluded the insurer from receiving indemnity from the manufacturer. Auto. Club Ins. Co. v. Toyota Motor Sales, Inc., 166 M 221, 531 P2d 1337 (1975).

Cosurety's Signature as Condition: Where the names of two sureties appear in the body of an indemnifying bond, which is however signed by but one, the condition of the bond is notice to the obligee, so as to permit the defense, by the surety signing, that his liability was conditioned on obtaining the signature of his cosurety. Butte v. Cook, 29 M 88, 74 P 67 (1903).

Part 4
Suretyship

Part Case Notes

Setoffs Allowed Against Principal Also Allowed Against Surety: Where the surety of the principal, a subcontractor, was found by the court to be equitably liable for all the obligations of the principal, including a judgment against the principal in favor of another plaintiff in the same case, the Supreme Court held that the surety was subject to the same setoffs of its claim against a third-party defendant as the surety's principal was subject to. The Supreme Court based its holding upon a transfer by the principal of all its assets to the surety and the surety's ultimate responsibility to pay the judgment to the original plaintiff. Pioneer Concrete & Fuel, Inc. v. Apex Constr., Inc., 204 M 387, 664 P2d 938, 40 St. Rep. 956 (1983).

28-11-401. Surety defined.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Damages Awarded to Former Employee for Sexual Harassment and Retaliation — Appellant's Supersedeas Bond With Surety Not Adequate — No Creation of Security Relationship Separate From Relationship That Already Existed Between Appellant and Surety — No Good Cause to Stay Proceedings to Enforce Judgment — Affirmed on Appeal. NorVal Elec. Co-op, Inc. v. Lawson, 2022 MT 62, 408 Mont. 159, 507 P.3d 157.

Statutory Requirement for at Least Two Sureties for Filing Valid Undertaking Not Met When One of Two Sureties Is Person Acting as Own Surety: Following a Justice's Court award of attorney fees and costs against Miller in a lease action, Miller filed an appeal and an undertaking in District Court. Under 25-33-201, two or more sureties are required to validate an undertaking. As defined in this section, a surety is one who becomes responsible for performance by another or hypothecates property as security for another; so by definition, a person may not act as surety for oneself. The undertaking in this case listed only Miller and another person as sureties. Therefore, the undertaking did not meet the requirement for two or more sureties and was deficient. The District Court did not have jurisdiction to consider the appeal because the undertaking was invalid, and the appeal was properly dismissed. Miller's contention that the provisions of 25-33-205 worked as an alternative to filing the undertaking on appeal also failed because there was no money that could be considered as a deposit filed within 10 days after notice of appeal. Red Lodging v. Miller, 2001 MT 135, 305 M 477, 29 P3d 477 (2001). See also Adams v. Crismore, 211 M 245, 683 P2d 497 (1984).

Clear Language of Surety Agreement Binds Surety — Impairment of Collateral: Plaintiff contended that he was entitled to discharge from his surety agreement under Montana statutes on the remedies and rights of a surety. He claimed that the creditor bank's unconsented release of collateral, which exposed plaintiff to increased liability, discharged him from the surety agreement. The Supreme Court held that plaintiff is not entitled to be discharged as an original obligor because the clear language of the surety agreement makes him liable and allows the creditor bank to realize on any collateral it held without obtaining plaintiff's consent. Mont. Bank of Livingston v. Old Saloon, Inc., 235 M 244, 766 P2d 878, 45 St. Rep. 2354 (1988).

Guaranty for Repayment of Money Loaned: A guaranty for repayment of money loaned was not a suretyship within the meaning of this section. Stensvad v. Miners and Merchants Bank of Roundup, 183 M 160, 598 P2d 1083 (1979).

Pledging Property as Surety for Obligation of Another — Pledgor a Surety: The owner of property who pledges it as security for the obligation of another person becomes a surety, and as such is discharged from liability when the creditor, without the pledgor's consent, alters the terms of the original obligation or in anywise impairs or suspends any remedies he may have against the principal. Vinson v. Pelletier, 78 M 254, 255 P 1067 (1927).

When Negotiable Instruments Act Supersedes the Law of Suretyship: The Uniform Negotiable Instruments Act supersedes the law of suretyship (31-4-401 to 31-4-507) as theretofore applicable to negotiable instruments; therefore one who signed a note as maker bound himself absolutely to pay, though in fact but an accommodation maker, and could not escape liability to a holder in due course under a plea of having been a surety only. Merchants' Nat'l Bank v. Smith, 59 M 280, 196 P 523 (1921).

Distinction Between Surety and Guarantor: The codes preserve the general distinction between suretyship and guaranty, which is that a surety is bound with the principal as an original promisor on the same contract, while the guarantor makes his own separate contract. Cole Mfg. Co. v. Morton, 24 M 58, 60 P 587 (1900).

Surety in General: When part of an agreement creating an agency was a bond executed to plaintiff by the agent and the defendants, conditioned that if the agent failed to perform his duties and pay over to the plaintiff such sums as might be due him the defendants would pay such sum, the defendants were sureties within the meaning of this section. Cole Mfg. Co. v. Morton, 24 M 58, 60 P 587 (1900).

28-11-402. When apparent principal may show surety.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Vehicle Purchase Contract: In an action between the original parties to a contract, it is competent to show that the purchaser of an automobile was the principal and each of the other defendants a surety only. Stanhope v. Shambow, 54 M 360, 170 P 752 (1918).

28-11-403. Interpretation of contract of suretyship.

Case Notes

Clear Breach of Bond: Though sureties are in a sense favorites in the law, such rule does not prevent a recovery when the facts are sufficient to show that the provisions of a bond given by them have been breached. Roper v. Caterpillar Tractor Co., 98 M 76, 37 P2d 812 (1934).

Bond and Contract Together: In determining the liability of a surety, the courts must first determine the liability of the principal. In so doing, the court had to construe the contract entered by the principal and the bond together. The provision covering all damages from failure to perform did not include attorney fees, however. Fed. Sur. Co. v. Basin Constr. Co., 91 M 114, 5 P2d 775 (1931). See also Gary Hay & Grain Co. v. Carlson, 79 M 111, 255 P 722 (1927).

Contract Controls: The liability of a surety is controlled and governed by the contract and may not be extended to cover matters outside the contract. The surety was not liable for the sheriff's wrongful conversion of attached property, as that action was beyond the scope of the official bond. McGinley v. Md. Cas. Co., 85 M 1, 277 P 414 (1929).

Construction Against Surety: Surety bonds are regarded as contracts of insurance and are therefore construed most strongly against the party creating the document. The contract is construed against the surety and in favor of the indemnity that the obligee has reasonable grounds to expect. St. v. Am. Sur. Co. of N.Y., 78 M 504, 255 P 1063 (1927).

Official Bond: When the law defines the duties of a public officer, his sureties are responsible for the faithful performance of such duties only and not for acts not pertaining thereto. Butte v. Bennetts, 51 M 27, 149 P 92 (1915).

Failure of Principal to Sign: The surety on an official bond, joint and several in nature, is not released from liability because of the failure of the principal to sign the bond. Deer Lodge County v. USF&G Co., 42 M 315, 112 P 1060 (1910).

Stay of Execution Bond: Stay of execution being a consideration of great value, sureties who execute an undertaking therefor have a right to rely upon the letter of their bond and to stand upon the entirety of the expressed consideration therein, and their liability cannot be extended by implication. State ex rel. Reins v. District Court, 22 M 449, 57 P 89 (1899).

28-11-404. Suretyship unaffected by judgment against surety.

Case Notes

Clear Breach of Bond: Though sureties are in a sense favorites in the law, such rule does not prevent a recovery when the facts are sufficient to show that the provisions of a bond given by them have been breached. Roper v. Caterpillar Tractor Co., 98 M 76, 37 P2d 812 (1934).

28-11-411. Extent of surety's liability.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Guarantor Not Liable Until Intervening Act Occurs: Plaintiff stockholders' damage claims against a bank for fraud and negligent misrepresentation because of the bank's failure to monitor for misuse and misappropriation of corporate funds were speculative and premature because the bank had not instituted a collection or foreclosure action. A guarantor does not become liable until an intervening act occurs, such as a default of the original borrower. Kondelik v. First Fidelity Bank of Glendive, 259 M 446, 857 P2d 687, 50 St. Rep. 874 (1993).

Tort by Surety in Violation of Insurance Code — Liability Not Limited: This section does not limit the liability of a surety if the surety commits an independent tort in violation of provisions of the insurance code. K-W Indus. v. Nat'l Surety Corp., 231 M 461, 754 P2d 502, 45 St. Rep. 762 (1988).

Subcontractor's Surety Not Liable to Materialman — No Third-Party Provision in Bond: Where the defendant, surety on two bonds for a subcontractor, executed bonds providing for the indemnification of the general contractor against all losses sustained by the general contractor because of the subcontractor's failure to pay for labor and materials and was sued by a third-party materialman, the District Court did not err in holding that the defendant had no contractual obligation to indemnify that materialman as a creditor of the subcontractor. Under the rationale of Treasure St. Indus., Inc. v. Welch, 173 M 403, 567 P2d 947 (1977), the surety is not liable to third-party creditors of its principal unless the bond between surety and principal expressly so provides. Absent any such express agreement, a materialman like the plaintiff has no right of action to recover as a matter of contract law under the bonds. Pioneer Concrete & Fuel, Inc. v. Apex Constr., Inc., 204 M 387, 664 P2d 938, 40 St. Rep. 956 (1983).

Transfer of Principal's Assets to Surety — Equitable Duty of Surety to Pay Principal's Obligations: Where the defendant surety company entered into an agreement with its principal requiring the principal to reimburse the defendant for any costs incurred in the bonding of the principal, received assets from its principal that made it impossible for the principal to pay a judgment, and represented the interest of the principal in litigation, the Supreme Court upheld on equitable grounds a District Court judgment against the surety for the obligations of its principal. Even though there was no contractual liability for the surety to pay the precise kind of debts incurred by the principal, the evidence showed an intent that all the principal's obligations be paid by the defendant. Pioneer Concrete & Fuel, Inc. v. Apex Constr., Inc., 204 M 387, 664 P2d 938, 40 St. Rep. 956 (1983).

Bond Controls: A surety is entitled to stand upon the precise terms of its contract. Where the bond is limited to the duties of the principal, it cannot be extended. There cannot always be a recovery against the surety where there is recovery against the principal. The surety may assert nonliability under the terms of the bond. Swanberg v. Nat'l Sur. Co., 86 M 340, 283 P 761 (1930).

Official Bond: Where the law defines the duties of a public officer, his sureties are responsible for the faithful performance of such duties only, and not for acts not pertaining thereto; under this rule an action did not lie against the sureties on a County Assessor's bond to recover money improperly paid to him as compensation for the collection by him of certain city taxes, which is a duty imposed by law upon other officers. Butte v. Bennetts, 51 M 27, 149 P 92 (1915).

Stay of Execution Bond: Stay of execution being a consideration of great value, sureties who execute an undertaking therefor have a right to rely upon the letter of their bond, and to stand upon the entirety of the expressed consideration therein, and their liability cannot be extended by implication. This principle is formulated in this section and the next succeeding section. State ex rel. Reins v. District Court, 22 M 449, 57 P 89 (1899).

28-11-412. Exoneration of surety.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

No Impairment of Collateral Used to Secure Loan — No Exoneration of Surety: Plaintiff read and signed a promissory note to secure a small business loan for a friend who subsequently went bankrupt. The promissory note provided that plaintiff would secure the friend's loan with logging equipment that plaintiff had used to secure his loan. After defendant bank foreclosed on the logging equipment, plaintiff claimed that the bank improperly impaired the collateral and improperly subordinated plaintiff's loan to his friend's loan without plaintiff's knowledge, thereby relieving plaintiff, as surety, of the obligation to repay the loan. The bank contended that plaintiff was fully informed of the loan structure and the requirement that plaintiff's loan was junior to the friend's small business loan. The trial court weighed the conflicting evidence and agreed that the bank had explained to plaintiff that proceeds from the sale of the collateral would be applied to the small business loan first and that plaintiff's loan was structured to limit plaintiff's potential exposure while ensuring that plaintiff would not have to provide cash up front to help the friend secure the small business loan. On appeal, the Supreme Court declined to second-guess the trial court's findings regarding the conflicting testimony, and the trial court was affirmed. Denton v. First Interstate Bank of Commerce, 2006 MT 193, 333 M 169, 142 P3d 797 (2006).

Clear Language of Surety Agreement Binds Surety — Impairment of Collateral: Plaintiff contended that he was entitled to discharge from his surety agreement under Montana statutes on the remedies and rights of a surety. He claimed that the creditor bank's unconsented release of collateral, which exposed plaintiff to increased liability, discharged him from the surety agreement. The Supreme Court held that plaintiff is not entitled to be discharged as an original obligor because the clear language of the surety agreement makes him liable and allows the creditor bank to realize on any collateral it held without obtaining plaintiff's consent. Mont. Bank of Livingston v. Old Saloon, Inc., 235 M 244, 766 P2d 878, 45 St. Rep. 2354 (1988).

Exoneration by Death of Surety: Where deceased had previously cosigned a promissory note for the purpose of lending his name to another party, he became an accommodation maker. As such he is primarily responsible for the payment of the note, without necessity of resort to the principal, and it was error for the District Court to disallow the holder's claim against the deceased's estate. In re Estate of Harbaugh, 196 M 274, 639 P2d 495, 39 St. Rep. 84 (1982).

Impairment of Remedies or Rights: A surety is discharged when his remedies or rights are impaired by an act of the creditor. U.S. v. Helena Office Supply Co., 256 F. Supp. 53 (D.C. Mont. 1966).

Prejudice of Surety Required for Release: This section and 31-4-502 relieve a surety in cases of omission or neglect, but only after a request by the surety that the creditor proceed. U.S. v. Helena Office Supply Co., 256 F. Supp. 53 (D.C. Mont. 1966).

Rescission of Contract by Creditor: When vendees of real estate abandoned premises with the knowledge of vendors, who repossessed by permitting another party to occupy and served a notice of cancellation of the contract for sale upon vendees, vendors, by such rescission of contract, lost their right to bring action against vendees' guarantor for unpaid purchase price. Scott v. Kyhl, 141 M 523, 379 P2d 803 (1963).

Effect of Impossibility of Performance of Contract by Principal: In holding a contract void because the impossibility preventing performance was due to the nature of the thing the contracting company undertook to do, the contractor was entitled to a recovery on the quantum meruit; his bond did not permit recovery of damages; a collateral promise in the contract consisting of warranty was invalid and would not support action for breach of warranty, and contractor's lien was supported by the implied contract. Smith Eng'r Co. v. Rice, 102 F2d 492 (9th Cir. 1958).

Release of Sureties in General:

When a creditor bank in an action against the receiver of an insolvent debtor bank compromised its claim against the latter thereon, thus discharging its obligation and suspending its rights and remedies against the principal, without the consent of the sureties, they were exonerated. First Nat'l Bank v. Holding, 90 M 529, 4 P2d 709 (1931).

The surety on an undertaking to secure the release of property from attachment enters into the obligation with reference to the cause as it then stands; and if the plaintiff in the action in which the attachment was levied, without the consent of the surety, subsequently changes his pleading so as to state another and different cause of action, it is such a change as will work a release of the surety. Gilna v. Fidelity & Deposit Co., 83 M 231, 272 P 540 (1928).

Crystallization of Common Law: Section 28-11-414, providing that a surety has all the rights of a guarantor, and 28-11-211 and this section, declaring when a surety and a guarantor are exonerated, are but crystallizations of common-law principles, and therefore common-law rules must be followed in their interpretation unless otherwise provided by statute. U.S. Bldg. & Loan Ass'n v. Burns, 90 M 402, 4 P2d 703 (1931).

Prejudice by Release of Other Surety: In an action on the official bond of a Sheriff to recover damages for the wrongful conversion of attached property, defendant surety company was not prejudiced by release of other sureties and therefore their release did not result in its exoneration to the extent of the alleged prejudice. McGinley v. Maryland Cas. Co., 85 M 1, 277 P 414 (1929).

Release of Surety Special Defense — Must Be Pleaded: Release of a surety is a special defense which must be pleaded; hence when it was not pleaded, refusal to permit defendant sureties to ask a witness for plaintiff whether plaintiff had not accepted a receiver's certificate in partial satisfaction of the obligation sued on, in an effort to establish that defense, was proper. Mut. Oil Co. v. Hamilton, 73 M 385, 236 P 545 (1925).

Negotiable Instruments: The Uniform Negotiable Instruments Act supersedes the law of suretyship (31-4-401 to 31-4-507) as theretofore applicable to negotiable instruments; therefore, one who signed a note as maker bound himself absolutely to pay, though in fact but an accommodation maker, and could not escape liability to a holder in due course under a plea of having been a surety only. Merchants' Nat'l Bank v. Smith, 59 M 280, 196 P 523 (1921).

Premature Payments to Principal: A surety is not released by premature payments to his principal, whereby the surety could not be injured. Nat'l Sur. Co. v. Lincoln County, 238 F 705 (9th Cir. 1917), affirming Lincoln County v. Coast Bridge Co., 231 F 468 (1916).

When Assignment Exonerates Surety: A contract in its nature unassignable by one of the parties without the consent of the other and to which a bond was attached guaranteeing faithful performance by the latter was further incapable of assignment without the consent of the sureties. Standard Sewing Mach. Co. v. Smith, 51 M 245, 152 P 38 (1915).

Estoppel of Sureties by Implied Assent: When endorsers on a note knew of, and impliedly gave their assent to, sales of livestock mortgaged to secure it, they were estopped, on the theory that their liability was that of sureties only. Columbus St. Bank v. Erb, 50 M 442, 147 P 617 (1915).

Prejudice of Surety Required for Release: When a lease of real property provided that rent should be paid quarterly in advance, a bond being given to secure the payment of the rent, and the lessor voluntarily, and without consideration therefor, reduced the rent for one quarter, and at different times permitted the lessee to make payments at irregular intervals, and not as provided in the lease, the sureties on the bond were not released from liability under this section. Dodd v. Vucovich, 38 M 188, 99 P 296 (1909). See Nat'l Sur. Co. v. Lincoln County, 238 F 705 (9th Cir. 1917).

Law Review Articles

Suretyship: Defenses of Sureties and Guarantors Under R.C.M. 1935, §§ 8188 and 8201, Browning, 2 Mont. L. Rev. 155 (1941).

28-11-413. Effect of performance or offer of performance on surety's liability.

Case Notes

Contractual Waiver of Exoneration of Suretyship: Beginning in 1983, a corporation borrowed from and subsequently repaid money to a bank over a 3-year period, with defendant listed as surety and guarantor. In 1986, the corporation borrowed $293,000 more from the bank, but no surety or guaranty documents were executed contemporaneously with the loan. The corporation defaulted on the 1986 loan. Defendant contended that each surety was attached to a specific note and should be exonerated as a matter of law when each note was repaid and that because no surety agreement was executed on the 1986 loan, he was not personally responsible for the corporate default. However, earlier surety and guaranty agreements signed by defendant stated that no payments made upon borrower's indebtedness would discharge surety's obligation "for any and all remaining and succeeding indebtedness of Borrower to Bank". This constituted a valid express waiver of defendant's right to exoneration and a waiver of exoneration as a statutory defense available to him as a surety. It was proper for the District Court to rule that the surety and guaranty documents signed by defendant were in effect at the time of corporate default. Mont. Bank of Circle v. Ralph Meyers & Son, Inc., 236 M 236, 769 P2d 1208, 46 St. Rep. 324 (1989).

28-11-414. Application to surety of rights of guarantor.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

Case Notes

Crystallization of Common Law: This section, providing that a surety has all the rights of a guarantor, and 28-11-211 and 28-11-412, declaring when a surety and a guarantor are exonerated, are but crystallizations of common-law principles, and therefore common-law rules must be followed in their interpretation unless otherwise provided by statute. U.S. Bldg. & Loan Ass'n v. Burns, 90 M 402, 4 P2d 703 (1931).

28-11-415. Power of surety to compel principal to perform.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

28-11-416. When surety may require creditor to pursue remedy.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Prejudice of Surety Required for Release: Subsection (3) of 28-11-412 and this section relieve a surety in cases of omission or neglect, but only after a request by the surety that the creditor proceed. U.S. v. Helena Office Supply Co., 256 F. Supp. 53 (D.C. Mont. 1966).

Withholding Distribution of Estate: Under this section an administratrix with the will annexed must withhold from the distributive share of a former executor (who was also a beneficiary under the will) any money for which such former executor became indebted to the estate during his administration thereof, when required by the surety of such former executor to do so, otherwise the surety will be exonerated to the extent that the distributive share will cover the indebtedness, since the surety as well as the estate of the former executor is liable for the indebtedness. Maryland Cas. Co. v. Walsh, 116 M 559, 155 P2d 759 (1945).

Surety's Rights as Against Assignee: Under this section and 28-11-418, the surety on a bond of a road contractor given the State Highway Commission (now Transportation Commission) pursuant to section 32-1608, R.C.M. 1947 (since repealed), acquired an equity in the earnings of the contractor remaining in the hands of the Commission, superior to that of a bank to which the contractor had made an assignment of money due him under the contract as security for loans extended, and was entitled to have the funds retained by the Commission applied in satisfaction of labor and material claims, payment of which was secured by the bond, before any portion of it was paid to the assignee. Lanstrum v. Zumwalt, 73 M 502, 237 P 205 (1925).

28-11-417. Surety's right to reimbursement and contribution.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Agreement of Principal to Reimburse Surety — When Material: Since the principal is bound under this section to reimburse the surety for what he has disbursed, an agreement of principal to do so when applying for the bond becomes material only if it entitles the surety to indemnity without any part of the principal obligation having been satisfied. Maryland Cas. Co. v. Walsh, 116 M 559, 155 P2d 759 (1945).

Equitable Assignments — Procedure to Determine Heirship: Neither statutory nor contractual liability constitutes equitable assignment of principal's property; nor does plaintiff's claim have priority over all other claims. Maryland Cas. Co. v. Walsh, 116 M 559, 155 P2d 759 (1945).

Implied Contract of Cosureties to Contribute:

When one of several sureties is compelled to pay the principal debtor's obligation, the law implies a contract on the part of his cosureties to contribute their share, and such implied contract is one for the direct payment of money, warranting the issuance of a Writ of Attachment. Kipp v. Paul, 110 M 513, 103 P2d 675 (1940).

An action by a surety for contribution from his cosurety is one on an implied contract for money paid by the former for the use and benefit of the latter, which the latter unconditionally and absolutely is required to pay. Wall v. Brookman, 72 M 228, 232 P 774 (1925).

Judgment Against Surety Not Required: While it is the law that unless a surety is legally bound to make payment on behalf of his principal he is not entitled to reimbursement, and if he makes payment he is a volunteer-payer, it is not the law that he is legally bound only after judicial determination; if he can prove that he was legally bound to pay, he can recover in an action for reimbursement, under attachment. Kipp v. Paul, 110 M 513, 103 P2d 675 (1940).

Accommodation Paper: The relations between parties to accommodation paper are those of principal and surety and therefore the right of the accommodation party to recourse against the party accommodated is that of a surety against the principal debtor. Bielenberg v. Higgins, 85 M 69, 277 P 636 (1929).

Depository Bond Surety: When deposits of state funds are secured by a bond and the surety is compelled to pay the amount thereof upon failure of the bank, the right of the state passes by subrogation to the surety. Aetna Accident & Liab. Co. v. Miller, 54 M 377, 170 P 760 (1918).

Payment by Surety Not to Relieve Cosureties: A judgment against a principal and sureties was paid by one of the sureties who took an assignment of it to compel contribution from his cosureties. The judgment was at the request of the paying surety, satisfied of record to relieve the real estate of the paying surety from the lien. It was intended to have the record satisfied only as to the paying surety. Such satisfaction did not release the liability for contribution of the cosureties who paid no consideration for it. Merchants' Nat'l Bank v. Great Falls Opera House Co., 23 M 33, 57 P 445 (1899).

28-11-418. Surety entitled to benefit of security held by creditor or cosurety.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

Case Notes

Clear Language of Surety Agreement Binds Surety — Impairment of Collateral: Plaintiff contended that he was entitled to discharge from his surety agreement under Montana statutes on the remedies and rights of a surety. He claimed that the creditor bank's unconsented release of collateral, which exposed plaintiff to increased liability, discharged him from the surety agreement. The Supreme Court held that plaintiff is not entitled to be discharged as an original obligor because the clear language of the surety agreement makes him liable and allows the creditor bank to realize on any collateral it held without obtaining plaintiff's consent. Mont. Bank of Livingston v. Old Saloon, Inc., 235 M 244, 766 P2d 878, 45 St. Rep. 2354 (1988).

Assignment as Chattel Mortgage: When a road construction contractor in his application for a surety company bond to secure the performance of his contract assigns his tools, equipment, etc., to the surety, the assignment to become of full force and effect upon his failure or inability to complete the work, the application constitutes a chattel mortgage upon the property as between him and the surety. Brown v. Fed. Sur. Co., 91 M 389, 8 P2d 647 (1932).

Surety's Rights as Against Assignee: Under 28-11-416 and this section, the surety on a bond of a road contractor given the State Highway Commission (now Transportation Commission) pursuant to section 32-1608, R.C.M. 1947 (since repealed), acquired an equity in the earnings of the contractor remaining in the hands of the Commission, superior to that of a bank to which the contractor had made an assignment of money due him under the contract as security for loans extended, and was entitled to have the funds retained by the Commission applied in satisfaction of labor and material claims, payment of which was secured by the bond, before any portion of it was paid to the assignee. Lanstrum v. Zumwalt, 73 M 502, 237 P 205 (1925).

28-11-419. Creditor entitled to benefit of security held by surety.

Case Notes

Security Provided by Stranger: In an action to recover on an appeal bond, when it appeared that a stranger to the original action had deposited in bank a sum of money to indemnify the sureties on the bond, the principle of subrogation embodied in this section may not be invoked by the creditor. O'Neill v. St. Sav. Bank, 34 M 521, 87 P 970 (1906).

TITLE 29
RESERVED

TITLE 30
TRADE AND COMMERCE

CHAPTER 1
UNIFORM COMMERCIAL CODE GENERAL PROVISIONS

Chapter Official Comments

[*Corresponding U.C.C. Section:* Article 1, U.C.C.]

PREFATORY NOTE

I. Introduction

From its inception, the Article 1 Drafting Committee performed two related, but distinct, tasks - revision of the current text of Uniform Commercial Code Article 1 [Title 30, chapter 1] and harmonization of ongoing UCC projects. This draft represents the product of one of those tasks - revision of the provisions of Article 1 [Title 30, chapter 1]. The other task entailed the Drafting Committee serving as a harmonization committee for the purpose of seeking to insure that the Uniform Commercial Code [Title 30, chapters 1 through 9A] speaks with a single voice to the extent appropriate.

After lengthy analysis and discussion, the Drafting Committee decided to recommend a relatively small number of substantive changes to the law as it is currently set forth in Article 1 [Title 30, chapter 1]. Those changes, concerning scope of the Article, applicability of supplemental principles of law, the concept of good faith, choice of law, the relevance of course of performance between the parties, and the existence of an independent statute of frauds, are described in some detail in Part II below. The changes with respect to choice of law are probably the most important changes in this draft and were the subject of more extensive Drafting Committee analysis and deliberation than any other topic.

In addition to these substantive changes, the Drafting Committee decided to make some structural changes to Article 1 [Title 30, chapter 1]. These structural changes, intended to make this Article more closely fit with the drafting conventions of the more recently addressed Articles and to lessen some difficulties in interpretation, are described in Part III below. Other than these structural changes, the Drafting Committee generally decided to resist the temptation to make non-substantive changes to provisions that have not been a source of serious problems in the nearly four decades since the widespread enactment of the UCC. A few such changes should be noted, however. First, as in all of the other UCC Articles promulgated in the last decade, provisions have been reformulated in a gender-neutral fashion. Second, in a very small number of cases, minor changes in wording have been made when the current wording has proven confusing. Those changes are noted in the Preliminary Comments following each section but are not otherwise described in this Prefatory Note.

II. Substantive Issues

The following are significant substantive issues raised by changes from current Article 1 [Title 30, chapter 1], in the order of their appearance in the draft:

A. Scope

Article 1 [Title 30, chapter 1] contains a relatively small number of substantive rules, but those rules are of fundamental importance. Occasionally courts and commentators have expressed uncertainty as to which transactions are governed by the substantive rules. Section 1-102 [30-1-101(4)] expresses a point that is implicit in current Article 1 [Title 30, chapter 1] - namely, that the substantive rules in Article 1 [Title 30, chapter 1] apply only to transactions within the scope of the other Articles [Title 30, chapters 2 through 5, 7, 8, and 9A].

B. Applicability of Supplemental Principles of Law

This draft merges subsections (1) and (2) of current Section 1-102 [30-1-102(1) and (2), 2003 MCA] (concerning the underlying purposes and policies of the UCC) and current Section 1-103 [30-1-103, 2003 MCA] (concerning the applicability of supplemental principles of law) into a revised Section 1-103 [30-1-102(1) and 30-1-103, 2005 MCA]. The provisions have been combined in this section [30-1-102(1) and 30-1-103, 2005 MCA] to reflect the interrelationship between the Code's purposes and policies and the extent to which other law is available to supplement it.

Except for changing the form of reference to the Uniform Commercial Code [Title 30, chapters 1 through 9A], subsection (b) of this section [30-1-103, 2005 MCA] is identical to current Section 1-103 [30-1-103, 2003 MCA]. The Preliminary Comments to this section [30-1-102(1) and 30-1-103, 2005 MCA], though, give more helpful guidance as to the distinction between situations in which Code provisions preempt the application of other law and those in which such supplementation is permissible.

C. Good Faith

Section 1-201(19) [sic] [30-1-201(2)(u), 2005 MCA] replaces the current definition of "good faith" ("honesty in fact in the conduct or transaction concerned") with the definition adopted by all but one of the recently revised UCC Articles as well as drafts of Revised Articles 2 and 2A [Title 30, chapters 2 and 2A]- "honesty in fact *and the observance of reasonable commercial standards of fair dealing.*" The section explicitly provides, however, that its definition of "good faith" does not displace the narrower definition in UCC Article 5 [Title 30, chapter 5]. In addition to centralizing the developments already taking place in other Articles, the new definition resolves any ambiguity as to the proper definition to apply to the general duty of good faith imposed by Article 1 [Title 30, chapter 1].

D. Choice of Law

Section 1-301 [30-1-301, 2005 MCA] represents a significant rethinking of choice of law issues addressed in current UCC Section 1-105 [30-1-105, 2003 MCA, now repealed]. The new section [30-1-301, 2005 MCA] reexamines both the power of parties to select the jurisdiction whose law will govern their transaction and the determination of the governing law in the absence of such selection by the parties. With respect to the power to select governing law, the draft affords greater party autonomy, but with important safeguards protecting consumer interests and fundamental policies. While the Drafting Committee considered also addressing the related topic of forum selection clauses, it ultimately decided that it was not workable for the Uniform Commercial Code [Title 30, chapters 1 through 9A] to govern such clauses.

1. Contractual Designation of Governing Law

Revised UCC Section 1-301 [30-1-301, 2005 MCA] addresses contractual designation of governing law somewhat differently than does current Section 1-105 [30-1-105, 2003 MCA, now repealed]. Current law allows the parties to any transaction to designate a jurisdiction whose law governs if the transaction bears a "reasonable relation" to that jurisdiction. Revised Article 1 [Title 30, chapter 1, 2005 MCA] deviates from this unified approach by providing different rules for consumer transactions than for "business to business" transactions.

In the context of consumer transactions, revised Article 1 [Title 30, chapter 1, 2005 MCA], unlike current law, protects consumers against the possibility of losing the protection of consumer protection laws of their home jurisdiction.

In the context of business-to-business transactions, revised Article 1 [Title 30, chapter 1, 2005 MCA] generally provides the parties with greater autonomy to designate a jurisdiction whose law will govern than does current Article 1 [Title 30, chapter 1, 2003 MCA], but also provides some safeguards against abuse that do not appear in current Article 1 [Title 30, chapter 1, 2003 MCA]. Following emerging international norms, greater autonomy is provided in subsections (b) and (c) [30-1-301(1) and (2)] by deleting the requirement that the transaction bear a "reasonable relation" to the jurisdiction designated in this non-consumer context. It should be noted in this regard that in the case of wholly domestic transactions the jurisdiction designated must be a State. An important safeguard not present in current law is provided in subsection (e) [not adopted]. Subsection (e) [not adopted] indicates that the designation of a jurisdiction's law is not effective (even if the transaction bears a reasonable relation to that jurisdiction) to the extent that application of that law would be contrary to a fundamental policy of the jurisdiction whose law would govern in the absence of contractual designation. Application of the law designated may be contrary to a fundamental policy of the State or country whose law would otherwise govern either because of the nature of the law designated or because of the "mandatory" nature of the law that would otherwise apply.

2. Choice of Law in the Absence of Contractual Designation of Governing Law

In the absence of an effective contractual designation of governing law, current UCC Section 1-105(1) [30-1-105, 2003 MCA, now repealed] directs the forum to apply its own law if the transaction bears "an appropriate relation to this state." This provision, however, is frequently ignored by courts. Revised UCC Section 1-301(b) [30-1-301(1)] provides simply that, in the absence of contractual designation, the court should apply the forum's choice of law principles.

E. Course of Performance

Section 1-304 [30-1-203, MCA] adds the concept of "course of performance," currently utilized only in Articles 2 and 2A [Title 30, chapters 2 and 2A], to course of dealing and usage of trade as the contextual clues that a court may use to interpret a contract.

F. Statute of Frauds

The Statute of Frauds "for kinds of personal property not otherwise covered" that appears in current Section 1-206 [30-1-206, 2003 MCA, now repealed] has been deleted. The Drafting Committee noted that the other Articles of the Uniform Commercial Code make individual determinations as to writing requirements for transactions within their scope, so that the only effect of Section 1-206 [30-1-206, 2003 MCA, now repealed] was to impose a writing requirement on transactions not otherwise governed by the UCC. The Drafting Committee decided that it is inappropriate for Article 1 [Title 30, chapter 1] to impose that requirement.

III. Structural Issues

A. General Organization

Current Article 1 [Title 30, chapter 1, 2003 MCA] is divided into two parts. Part 1 [Title 30, chapter 1, part 1, 2003 MCA] is entitled "Short Title, Construction, Application and Subject Matter of Act." Part 2 [Title 30, chapter 1, part 2, 2003 MCA] is entitled "General Definitions and Principles of Interpretation." The rationale for placement of particular sections in one part or the other is occasionally obscure. This draft reorganizes Article 1 [Title 30, chapter 1, 2005 MCA] into three parts. Part 1 [Title 30, chapter 1, part 1, 2005 MCA] - "General Provisions" - contains general rules about the UCC as a whole. Part 2 [Title 30, chapter 1, part 2, 2005 MCA] - "General Definitions and Principles of Interpretation" - contains the Code's major definitional section as well as additional rules of interpretation. Part 3 [Title 30, chapter 1, part 3, 2005 MCA] - "Territorial Applicability and General Rules" - contains substantive rules that apply to all transactions that are within the scope of the Code.

B. Relocation of Substantive Rules Embedded in Definitions

The Drafting Committee identified four cases in which definitions in Section 1-201 [30-1-201, 2003 MCA] were made unnecessarily complicated by substantive rules embedded within them. Extracting those substantive rules and placing them in separate sections enables those rules to be presented more effectively and is more consistent with current drafting principles in many States.

1. Notice and knowledge

The rules concerning notice and knowledge have been moved from their current location in three subsections of Section 1-201 [30-1-201, 2003 MCA] to a separate substantive section. The Drafting Committee believes that, with this reorganization, the concepts are more clearly articulated and more easily found.

2. Distinguishing leases from security interests

In current Article 1 [Title 30, chapter 1, 2003 MCA], the definition of "security interest" consists of a short paragraph elucidating a basic principle that resolves almost every issue, followed by over 50 lines of clarification and qualification that serve only one function - distinguishing "true leases" from transactions that are leases in form but security interests in substance. This extended rule even contains a nested definition of the term "present value," which it uses as part of drawing the distinction between true leases and security interests. The portion of the definition of "security interest" that distinguishes true leases from security interests has been moved to a separate substantive section. As a result, the remaining portion of the definition of "security interest" is shorter and clearer. The definition of "present value" is moved to its own definitional subsection [not adopted].

3. Value

Whether a person acquires rights "for value" is at present the subject of a definitional provision in current Section 1-201(44) [30-1-201(44), 2003 MCA]. Yet, as the NCCUSL Committee on Style correctly noted to the Drafting Committee, the provision is more appropriately articulated as a free-standing rule. It has been moved to Section 1-204 [30-1-212, 2005 MCA].

Chapter Compiler's Comments

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Section Not Codified: Section 87A-10-101, R.C.M. 1947, an effective date, was not codified in the MCA. This clause has not been repealed and is still valid law. Citation may be made to sec. 10-101, Ch. 264, L. 1963.

Montana Compiler Changes: Compiler has changed the Official Comments by changing "Article" to "Chapter" wherever it appears and by prefacing section numbers with Title 30 so as to reflect Montana's codification of the U.C.C.

Part 1
Short Title, Construction, Application, and Subject Matter of the Code

30-1-101. Short titles — scope of chapter.

Official Comment

[*Corresponding U.C.C. Section:* Section 1-101, 1-102, U.C.C.]

Source: Former Section 1-101.

Source: New.

Changes From Former Law: Subsection (b) [subsection (3)] is new. It is added in order to make the structure of Article 1 [Title 30, chapter 1] parallel with that of the other Articles of the Uniform Commercial Code [Title 30, chapters 2 through 5, 7, 8, and 9A].

1. Each other Article of the Uniform Commercial Code (except Articles 10 and 11) may also be cited by its own short title. See Sections 2-101 [30-2-101], 2A-101 [30-2A-101], 3-101 [30-3-101], 4-101 [30-4-101], 4A-101 [30-4A-101], 5-101 [30-5-101], 6-101 [30-6-101, now repealed], 7-101 [30-7-101], 8-101 [30-8-101], and 9-101 [30-9A-101].

1. [2.] [Subsection (4) is new.] This section [1-102, UCC] [subsection (4)] is intended to resolve confusion that has occasionally arisen as to the applicability of the substantive rules in this article [Title 30, chapter 1]. As this section [subsection (4)] makes clear, the rules in article 1 [Title 30, chapter 1] apply to transactions to the extent that those transactions are governed by one of the other articles of the Uniform Commercial Code. This article [Title 30, chapter 1] does not apply to transactions to the extent that they are governed by other law. See Preliminary Comment 1 to Section 1-301 [30-1-301].

Compiler's Comments

2005 Amendment: Chapter 575 in catchline inserted "scope of chapter"; inserted (3) giving cite to chapter; inserted (4) relating to application of chapter; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-1-102. Purposes — rules of construction.

Official Comment

[*Corresponding U.C.C. Section:* Section 1-103(a) and 1-106, U.C.C.]

Source: Former Section 1-102 (1)-(2) [30-1-102(1), (2), and (5), 2003 MCA]; Former Section 1-103 [30-1-103, 2003 MCA].

Source: Former Section 1-102(5) [30-1-102(5), 2003 MCA]. See also 1 U.S.C. § 1.

Changes From Former Law: This section is derived from subsections (1) and (2) of former Section 1-102 [30-1-102(1), (2), and (5), 2003 MCA] and from former Section 1-103 [30-1-103]. Subsection (a) of this section [30-1-102(1), 2005 MCA] combines subsections (1) and (2) of former Section 1-102 [30-1-102(1) and (2), 2003 MCA]. Except for changing the form of reference to the Uniform Commercial Code [Title 30, chapters 1 through 9A] and minor stylistic changes, its language is the same as subsections (1) and (2) of former Section 1-102 [30-1-102(1) and (2), 2003 MCA]. Except for changing the form of reference to the Uniform Commercial Code [Title 30, chapters 1 through 9A], subsection (b) of this section [30-1-103, 2005 MCA] is identical to former Section 1-103 [30-1-103, 2003 MCA]. The provisions have been combined in this section [30-1-102(1) and 30-1-103, 2005 MCA] to reflect the interrelationship between them.

1. The Uniform Commercial Code [Title 30, chapters 1 through 9A] is drawn to provide flexibility so that, since it is intended to be a semi-permanent piece of legislation, it will provide its own machinery for expansion of commercial practices. It is intended to make it possible for the law embodied in the Uniform Commercial Code [Title 30, chapters 1 through 9A] to be developed

by the courts in the light of unforeseen and new circumstances and practices. However, the proper construction of the Uniform Commercial Code [Title 30, chapters 1 through 9A] requires that its interpretation and application be limited to its reason.

Even prior to the enactment of the Uniform Commercial Code [Title 30, chapters 1 through 9A], courts were careful to keep broad acts from being hampered in their effects by later acts of limited scope. [*Pacific Wool Growers v. Draper & Co.*, 158 Or. 1, 73 P.2d 1391 (1937), and] compare Section 1-104 [30-1-104]. The courts recognized the policies embodied in an act as applicable in reason to subject-matter that was not expressly included in the language of the act, [*Commercial Nat. Bank of New Orleans v. Canal-Louisiana Bank & Trust Co.*, 239 U.S. 520, 36 S.Ct. 194, 60 L.Ed. 417 (1916) (bona fide purchase policy of Uniform Warehouse Receipts Act extended to case not covered but of equivalent nature)] and did the same where reason and policy so required, even where the subject-matter had been intentionally excluded from the act in general. [*Agar v. Orda*, 264 N.Y. 248, 190 N.E. 479 (1934) (Uniform Sales Act change in seller's remedies applied to contract for sale of choses in action even though the general coverage of that Act was intentionally limited to goods "other than things in action.")] They implemented a statutory policy with liberal and useful remedies not provided in the statutory text. They disregarded a statutory limitation of remedy where the reason of the limitation did not apply. [*Fiterman v. J. N. Johnson & Co.*, 156 Minn. 201, 194 N.W. 399 (1923) (requirement of return of the goods as a condition to rescission for breach of warranty; also, partial rescission allowed).] Nothing in the Uniform Commercial Code [Title 30, chapters 1 through 9A] stands in the way of the continuance of such action by the courts.

The Uniform Commercial Code [Title 30, chapters 1 through 9A] should be construed in accordance with its underlying purposes and policies. The text of each section should be read in the light of the purpose and policy of the rule or principle in question, as also of the Uniform Commercial Code [Title 30, chapters 1 through 9A] as a whole, and the application of the language should be construed narrowly or broadly, as the case may be, in conformity with the purposes and policies involved.

Other than minor stylistic changes, this section [subsection (2)] is identical to former UCC Section 1-102(5) [30-1-102(5), 2003 MCA].

1. [2.] This section [subsection (2)] makes it clear that the use of singular or plural in the text of the Uniform Commercial Code [Title 30, chapters 1 through 9A] is generally only a matter of drafting style - singular words may be applied in the plural, and plural words may be applied in the singular. Only when it is clear from the statutory context that the use of the singular or plural does not include the other is this rule inapplicable. *See, e.g.*, Section 9-322 [30-9A-322].

Compiler's Comments

2005 Amendment: Chapter 575 in catchline at end deleted "variation by agreement"; deleted former (3) and (4) that read: "(3) The effect of provisions of this code may be varied by agreement, except as otherwise provided in this code and except that the obligations of good faith, diligence, reasonableness and care prescribed by this code may not be disclaimed by agreement but the parties may by agreement determine the standards by which the performance of such obligations are to be measured if such standards are not manifestly unreasonable.

(4) The presence in certain provisions of this code of the words "unless otherwise agreed" or words of similar import does not imply that the effect of other provisions may not be varied by agreement under subsection (3)"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

Case Notes

Applicability of Discovery Doctrine to Uniform Commercial Code Conversion Cases: Over a 2½-year period, one of plaintiff's employees forged signatures on more than 100 company checks and money orders, made them payable to herself, and deposited the proceeds in her personal account at defendant credit union. Plaintiff ultimately filed an action against the credit union, seeking damages in the amount of the checks and money orders and alleging unlawful conversion of negotiable instruments under 30-3-419 and breach of transfer warranties under 30-4-207. The credit union moved for summary judgment on grounds that the conversion action was barred by the statutes of limitations in 30-3-417(4) and 30-4-207(5). However, the statutes of limitations in 30-3-417(4) and 30-4-207(5) apply only to breach of warranty actions, not to conversion actions. The credit union then asserted that the discovery doctrine should apply. The doctrine is an equitable exception to the general rule that the statute of limitations begins to run as soon as the cause of action accrues, allowing instead that the applicable statute of limitations begins to run once plaintiff knew or should have known that a cause of action existed. In a case of first impression, the Supreme Court declined to apply the discovery doctrine to the Uniform Commercial Code conversion claim. Conversion actions are subject to the statute of limitations in 30-3-122(7), which requires commencement of a conversion action within 3 years of the action's accrual. The public would be poorly served by a rule that shifts the responsibility for careful bookkeeping and employee supervision away from those in the best position to monitor accounts and employees. Although predictably harsh in some cases, the 3-year statute of limitations will be strictly applied as best serving the goals of the Uniform Commercial Code. The facts regarding the date of the conversion and the filing of plaintiff's complaint were not in dispute, so the credit union was entitled to judgment as a matter of law on the conversion claim. Yarbro, Ltd. v. Missoula Fed. Credit Union, 2002 MT 152, 310 M 346, 50 P3d 158 (2002).

30-1-103. Supplementary general principles of law applicable.

Official Comment

[*Corresponding U.C.C. Section:* Section 1-103(b), U.C.C.]

Source: Former Section 1-102 (1)-(2) [30-1-102(1), (2), and (5), 2003 MCA]; Former Section 1-103 [30-1-103, 2003 MCA].

Changes From Former Law:

2.[1.] **Applicability of supplemental principles of law.** Subsection (b) [of section 1-103, UCC] [30-1-103] states the basic relationship of the Uniform Commercial Code [Title 30, chapters 1 through 9A] to supplemental bodies of law. The Uniform Commercial Code [Title 30, chapters 1 through 9A] was drafted against the backdrop of existing bodies of law, including the common law and equity, and relies on those bodies of law to supplement it provisions in many important ways. At the same time, the Uniform Commercial Code [Title 30, chapters 1 through 9A] is the primary source of commercial law rules in areas that it governs, and its rules represent choices made by its drafters and the enacting legislatures about the appropriate policies to be furthered in the transactions it covers. Therefore, while principles of common law and equity may *supplement* provisions of the Uniform Commercial Code [Title 30, chapters 1 through 9A], they may not be used to *supplant* its provisions, including the purposes and policies those provisions reflect, unless a specific provision of the Code [Title 30, chapters 1 through 9A] provides otherwise. In the absence of such a provision, the Uniform Commercial Code [Title 30, chapters 1 through 9A] preempts principles of common law and equity that are inconsistent with either its provisions, or its purposes and policies.

The language of subsection (b) [of section 1-103, UCC] [30-1-103] is intended to reflect both the concept of supplementation and the concept of preemption. Some courts, however, had difficulty in applying the identical language of former Section 1-103 [30-1-103, 2003 MCA] to determine when other law appropriately may be applied to supplement the Code [Title 30, chapters 1 through 9A], and when that law has been displaced by the Code [Title 30, chapters 1 through 9A]. Some decisions applied other law in situations in which that application, while not inconsistent with the text of any particular provision of the Code [Title 30, chapters 1 through 9A], clearly was inconsistent with the underlying purposes and policies reflected in the relevant Code provisions [Title 30, chapters 1 through 9A]. *See, e.g., Sheerbonnet, Ltd. v. American Express Bank, Ltd.*, 951 F. Supp. 403 (S.D.N.Y. 1995). In part, this difficulty arose from Comment 1 to former Section 1-103 [30-1-103, 2003 MCA], which stated that "this section indicates the continued applicability to commercial contracts of all supplemental bodies of law except insofar as they are explicitly displaced by this Act." The "explicitly displaced" language of that Comment does not accurately reflect the proper scope of Code preemption, which extends to displacement of other law that is inconsistent with its purposes and policies as well as its text.

3.[2.] **Application of subsection (b) to statutes.** The primary focus of Section 1-103 [30-1-102(1) and 30-1-103, 2005 MCA] is on the relationship between the Uniform Commercial Code [Title 30, chapters 1 through 9A] and principles of common law and equity as developed by the courts. State law, however, increasingly is statutory. Not only are there a growing number of state statutes addressing specific issues that come within the scope of the Uniform Commercial

Code [Title 30, chapters 1 through 9A], but in some States many general principles of common law and equity have been codified. When the other law relating to a matter within the scope of the Uniform Commercial Code [Title 30, chapters 1 through 9A] is a statute, the principles of subsection (b) [30-1-103, 2005 MCA] remain relevant to the court's analysis of the relationship between that statute and the Uniform Commercial Code [Title 30, chapters 1 through 9A], but will be supplemented by other principles of statutory interpretation that specifically address the interrelationship between statutes. In some situations, the principles of subsection (b) [30-1-103, 2005 MCA] still will be determinative. For example, the mere fact that an equitable principle is stated in statutory form rather than in judicial decisions should not change the court's analysis of whether the principle can be used to supplement the Uniform Commercial Code [Title 30, chapters 1 through 9A] - under subsection (b) [30-1-103, 2005 MCA], equitable principles may supplement provisions of the Uniform Commercial Code [Title 30, chapters 1 through 9A] only if they are consistent with the purposes and policies of the Uniform Commercial Code [Title 30, chapters 1 through 9A] as well as its text. In other situations, however, other interpretive principles addressing the interrelationship between statutes may lead the court to conclude that the other statute is controlling, even though it conflicts with the Uniform Commercial Code [Title 30, chapters 1 through 9A]. This, for example, would be the result in a situation where the other statute was specifically intended to provide additional protection to a class of individuals engaging in transactions covered by the Uniform Commercial Code [Title 30, chapters 1 through 9A].

4.[3.] **Listing not exclusive.** The list of sources of supplemental law in subsection (b) [30-1-103, 2005 MCA] is intended to be merely illustrative of the other law that may supplement the Uniform Commercial Code [Title 30, chapters 1 through 9A], and is not exclusive. No listing could be exhaustive. Further, the fact that a particular section of the Uniform Commercial Code [Title 30, chapters 1 through 9A] makes express reference to other law is not intended to suggest the negation of the general application of the principles of subsection (b) [30-1-103, 2005 MCA]. Note also that the word "bankruptcy" in subsection (b) [30-1-103, 2005 MCA], continuing the use of that word from former Section 1-103 [30-1-103, 2003 MCA], should be understood not as a specific reference to federal bankruptcy law but, rather as a reference to general principles of insolvency, whether under federal or state law.

Case Notes

Plaintiff Debtor Not Equitably Estopped — No Evidence Plaintiff Knew Rights Under U.C.C. — No Language in Debtor-Supplied Release Document Regarding U.C.C. Rights: Because all six elements of equitable estoppel could not be satisfied, the District Court erred in granting the defendant creditor summary judgment based on its determination that the plaintiff debtor was equitably estopped from pursuing her claims. There was no language in the release document that was prepared by the defendant to suggest that the plaintiff knew of her rights under the Uniform Commercial Code (U.C.C.) or knew that the release was an attempt to waive all of her rights under the U.C.C. Kapor v. RJC Inv., Inc., 2019 MT 41, 394 Mont. 311, 434 P.3d 869.

Partial Performance Principle Displaced by Montana Uniform Commercial Code: The District Court erred in denying the defendant's motion for judgment as a matter of law to the extent that it relied on the part performance exception. Unlike estoppel, the principle of partial performance is displaced by the particular provisions of the Montana Uniform Commercial Code. The part performance exception to the Montana UCC statute of frauds is much more limited than the part performance doctrine outside the Montana UCC context. As such, the plaintiff could not rely on a partial performance exception to exempt an alleged oral contract from the Montana UCC statute of frauds. S & P Brake Supply, Inc. v. STEMCO LP, 2016 MT 324, 385 Mont. 488, 385 P.3d 567.

Promissory Estoppel Does Not Require Showing of Intent to Mislead: The elements of promissory estoppel are distinct from the elements of estoppel by silence. Promissory estoppel does not require a showing of an intent to mislead. S & P Brake Supply, Inc. v. STEMCO LP, 2016 MT 324, 385 Mont. 488, 385 P.3d 567. See also NW. Potato Sales, Inc. v. Beck, 208 Mont. 310, 678 P.2d 1138 (1984), and Turner v. Wells Fargo Bank, N.A., 2012 MT 213, 366 Mont. 285, 291 P.3d 1082.

Promissory Estoppel Not Displaced by Montana Uniform Commercial Code: The District Court did not err in denying the defendant's summary judgment motion and allowing the question of whether the plaintiff could satisfy the promissory estoppel exception to proceed to trial. Like other forms of estoppel, promissory estoppel is not displaced by the particular provisions of the Montana Uniform Commercial Code. Promissory estoppel may apply to remove a transaction from the Montana UCC statute of frauds. S & P Brake Supply, Inc. v. STEMCO LP, 2016 MT 324, 385 Mont. 488, 385 P.3d 567. See also NW. Potato Sales, Inc. v. Beck, 208 Mont. 310, 678 P.2d 1138 (1984).

Bank's Charge-Back Right Terminated Only on Final Settlement of Check — Estoppel Verdict Inapplicable to Bank's Right to Charge Back Provisional Settlement Funds From Defendant's Account — Fees and Costs: Shupak sold a car to a buyer in Germany for $7,400. The German sent Shupak a check for $11,500 and asked Shupak to send the $4,100 difference to a "shipper" in Belgium. Because of the unusual nature of the check and the misspelling of Shupak's name on the check, Shupak inquired with plaintiff credit union before cashing the check, and plaintiff authorized cashing the check. Shupak placed $4,000 in his account, made a loan payment on a vehicle, and mailed $4,100 to Belgium. The check was subsequently returned as counterfeit and plaintiff charged back Shupak's account for $11,500, leaving the account overdrawn and the vehicle loan past due. After unsuccessful attempts to repossess Shupak's vehicles, plaintiff eventually sued Shupak to recover the outstanding balance, which at that point was $8,185.97. Shupak raised several defenses, including estoppel, and countersued for negligence, malicious prosecution, breach of the duty of good faith under the Uniform Commercial Code, breach of fair debt collection practices, and fraud. The District Court concluded that plaintiff had a statutory right to charge back the money given Shupak for the fraudulent check and granted plaintiff partial summary judgment on that issue, but reserved judgment against Shupak until the jury could determine whether Shupak was entitled to offset the amount because of plaintiff's alleged negligent misrepresentations regarding the validity of the check. The jury ultimately found that plaintiff was 77.5% negligent and Shupak was 22.5% negligent, that the negligence had caused $5,000 in damages, and that plaintiff was estopped from enforcing the provisions of its membership and loan liner agreements, but Shupak's fraud and punitive damage claims were rejected. Shupak was awarded $3,874 for plaintiff's negligence, which was subtracted from the $8,185.97 owed to plaintiff by reason of the charge-back right, resulting in a net judgment to plaintiff of $4,310.97. Both parties then sought attorney fees and costs. Shupak was determined to be the prevailing party because he had prevailed on the negligence claim, despite plaintiff prevailing on the charge-back issue and receiving a net judgment, and Shupak was awarded fees and costs of $49,918.65, for a net judgment of $44,606.88 in Shupak's favor. Plaintiff appealed. The Supreme Court, citing Valley Bank of Ronan v. Hughes, 2006 MT 285, 334 M 335, 147 P3d 185 (2006), concluded that plaintiff's charge-back right terminated only upon final settlement of the check, and the right was not affected by Shupak's use of the provisional settlement funds or by plaintiff's failure to exercise ordinary care in handling the check for settlement purposes. Until a check becomes final, a bank may charge back provisional settlement funds to the customer, and the risk of loss remains with the customer, so the charge-back right may not be equitably estopped. Additionally, the District Court erred in awarding Shupak's attorney fees and costs. Plaintiff was entitled to that portion of its attorney fees and costs related to enforcement of its statutory charge-back right as a matter of law. Because plaintiff prevailed on the charge-back claim and received a net judgment, plaintiff was considered the prevailing party and the award of attorney fees and costs to Shupak was reversed. Avanta Fed. Credit Union v. Shupak, 2009 MT 458, 354 M 372, 223 P3d 863 (2009), followed in Total Indus. Plant Serv., Inc. v. Turner Indus. Group, LLC, 2013 MT 5, 368 Mont. 189, 294 P.3d 363.

Bank to Exercise Ordinary Care in Settling Checks — Common Law That Bank Exercise Ordinary Care in Processing Checks Preempted by Uniform Commercial Code: Hughes brought common-law claims against a bank for failing to exercise ordinary care in processing checks and for communications that the bank made regarding check processing. A bank that receives a check from a depositor must use ordinary care, as defined in the Uniform Commercial Code (U.C.C.), in settling those checks. However, when a check is processed by automated means, reasonable commercial standards do not require the bank to examine the check, subject to certain exceptions. To the extent that common-law claims relate to processing checks, the specific provisions of the U.C.C. prevail, so Hughes' claims regarding the propriety of the bank's check processing were preempted. However, because the U.C.C. does not address misrepresentation in communications, Hughes' common-law and equitable claims for negligence were not preempted by the U.C.C., and the District Court committed reversible error by failing to consider whether common-law and equitable principles supplement the U.C.C.-defined duty of ordinary care with respect to the bank's representations about the check settlement process. Valley Bank of Ronan v. Hughes, 2006 MT 285, 334 M 335, 147 P3d 185 (2006).

Failure to Demonstrate That Equitable Interest in Cattle Sold Displaced Perfected Security Interest in Cattle as After-Acquired Property: Bellanger obtained loans from the Daniels-Sheridan Federal Credit Union to finance a ranching operation, securing the loans with several promissory notes securing an interest in the cattle on the ranch. Bellanger subsequently defaulted on the loans, and the credit union initiated an action to enforce the promissory notes pursuant to the

Uniform Commercial Code (U.C.C.). The case broadened to encompass disputes over proceeds from the sale of the cattle to include Smith, the owner of the auction company where Bellanger customarily sold cattle, whom the credit union alleged had an inferior security interest in some of the cattle that Smith had sold to Bellanger. The credit union pointed out that Smith had only an unperfected security interest because he failed to perfect a security interest pursuant to the U.C.C. Smith contended that Bellanger had obtained only a leasehold interest in the cattle and that the credit union thus had no security interest in those cattle. The cattle were subsequently seized and sold for $79,012.27, and the District Court split the proceeds, with $45,467.94 paid to the credit union and a judgment for the remainder owed on the promissory notes, and $33,544.33 paid to Smith. The credit union appealed, and the Supreme Court reversed. The District Court erred in equitably subordinating the credit union's prior perfected security interest to Smith's unperfected security interest. The Supreme Court held that Smith's transaction with Bellanger was a sale, not a lease or bailment, and as such, the hierarchy of priorities for security interests set forth in Article 9 of the U.C.C. (now Title 30, ch. 9A) applied in the credit union's favor. Smith failed to demonstrate that any equitable interest that he had in the cattle displaced the credit union's perfected security interest in the cattle as an after-acquired property of Bellanger, so an equitable carve-out from the U.C.C. principles of hierarchy priority was not justified. Daniels-Sheridan Fed. Credit Union v. Bellanger, 2001 MT 235, 307 M 22, 36 P3d 397 (2001), following Rudio v. Yellowstone Merchandising Corp., 200 M 537, 652 P2d 1163 (1982), and distinguishing NW. Potato Sales, Inc. v. Beck, 208 M 310, 678 P2d 1138 (1984), and Ninth District Prod. Credit Ass'n v. Ed Duggan, Inc., 821 P2d 788 (Colo. 1991).

Merchant Pawnbroker Held to Good Faith Requirement: Defendant pawnshop operator who sold stolen property to plaintiff refused to give plaintiff a refund after the property was recovered by police. Defendant argued that he disclaimed any warranty of title to goods sold in his business by posting a sign alerting buyers that merchandise is sold "as is" and by writing the same notation on his sales slips. Defendant clearly breached the warranty of clear title under 30-2-312 when he sold stolen goods because neither a thief nor his successor pass clear title to stolen goods. It was irrelevant that defendant claimed he did not know the goods were stolen. With respect to breach of warranty, defendant as a merchant is held to a higher standard of dealing than ordinary consumers. In addition, he is held to the obligatory good faith required in the performance of every contract under the U.C.C., which is defined under 30-1-201 as "honesty in fact". Brokke v. Williams, 235 M 305, 766 P2d 1311, 46 St. Rep. 6 (1989).

Montana Forum for Settlement of Noncontractual Issues: Defendant argued that New York law should apply to a breach of contract action because a document giving plaintiffs authority to install phone systems expressly adopted New York law. However, the Supreme Court held Montana law applicable upon finding that the installation agreement did not relate to plaintiff's claims for relief based on purchase of goods, hands-on training, return policy, and exclusive dealership. Further, the injury occurred in Montana, plaintiff resided and did business in Montana, defendant solicited sales in Montana, and defendant visited Montana to check on plaintiffs and to solicit another distributor. Webcor Electronics, Inc. v. Home Electronics, Inc., 231 M 377, 754 P2d 491, 45 St. Rep. 695 (1988).

Cancellation of Promissory Notes — Erases Security Interest: In fashioning judgment in a case involving fraud and misrepresentation, the District Court awarded the bank all of plaintiff's property and canceled all of the promissory notes from plaintiffs to the bank. The bank contended this violated its rights as a secured creditor. It contended it was entitled to a variety of options in enforcing its security interest and could not be forced to satisfy its claim by taking possession of the property. On appeal, the Supreme Court upheld the award. By finding the bank guilty of fraud and misrepresentation, the trial court could properly cancel the promissory notes. Canceling the notes erased the bank's specific security interests. Having canceled the notes, the trial court, sitting in equity, had a great deal of leeway in fashioning a remedy. The remedy allowed the bank to mitigate its losses and was proper. Crystal Springs Trout Co. v. First State Bank of Froid, 225 M 122, 732 P2d 819, 44 St. Rep. 90 (1987).

Sale of Front-End Loader — Applicable Parol Evidence Rule: Front-end loader that buyer purchased from seller was within the definition of "goods" set out in 30-2-105. Therefore, the sale was governed by the Montana Uniform Commercial Code, and any Code provisions addressing a parol evidence question controlled the answer to the question, with the contract law parol evidence rule of 28-2-904 being used only to supplement the Code. Norwest Bank Billings v. Murnion, 210 M 417, 684 P2d 1067, 41 St. Rep. 1132 (1984).

Estoppel to Prevent Application of Statute of Frauds: In a contract action brought by the plaintiff buyer of seed potatoes against the seller, in which the evidence showed that the defendant had never signed a written contract for the potatoes, but by his active and passive conduct induced the plaintiff to change his position by agreeing to sell the potatoes that were the subject of the contract to other buyers, the Supreme Court held that the plaintiff had proved the elements of estoppel by silence or equitable estoppel and that the defendant would therefore be estopped in applying the Statute of Frauds to the oral contract. NW. Potato Sales, Inc. v. Beck, 208 M 310, 678 P2d 1138, 41 St. Rep. 362 (1984), followed, with regard to elements of estoppel, in CB&F Dev. Corp. v. Culbertson St. Bank, 256 M 1, 844 P2d 5, 49 St. Rep. 1122 (1992).

Joint Payee Conversion Suit Against Bank — Collateral Estoppel: Without his wife's knowledge or consent, husband deposited two checks made out to him and his wife in payment for property they jointly owned and then withdrew the money. He converted it and divorced her. Wife sued the depositary and payee banks for conversion of the checks, since they were paid despite the absence of any endorsement by husband or wife. Since the issues in the divorce and conversion proceedings were not the same and the conversion proceeding issues were not determined in the divorce proceeding, collateral estoppel did not bar wife's suit. Stapleton v. First Sec. Bank, 207 M 248, 675 P2d 83, 40 St. Rep. 2015 (1983).

Breach of Contractual Warranties — Proper Parties — Statute of Frauds: Plaintiffs in an action for breach of express and implied warranties were farmers. Defendants manufactured farm implements. One of the plaintiffs had an arm severed in an accident involving the defendants' machinery. On appeal, the defendants argued that the injured plaintiff was not a party to the purchase contract. The plaintiff alleged the salesman knew that he and the party who actually signed the purchase order were to be co-owners of the hay baler in question. The signature was for the one co-owner for himself and as agent for the plaintiff as well. Because principal and agent law supplements the Montana U.C.C. which covers the purchase of the baler, the court considered applying 28-10-203, which prevents oral authorization to contract when the contract itself must be written, as here. It noted exceptions to the Statute of Frauds, however. The question of whether payment of the purchase price took this contract out of the Statute of Frauds was a genuine issue of material fact preventing a summary judgment for the defendants under the Federal Rules of Civil Procedure. Holding the question one of law, the court said it had to hold an evidentiary hearing on the issues. Schlenz v. John Deere Co., 511 F. Supp. 224, 38 St. Rep. 579 (D.C. Mont. 1981).

30-1-104. Construction against implicit repeal.

Official Comment

[*Corresponding U.C.C. Section:* Section 1-104, U.C.C.]

Source: Former Section 1-104 [30-1-104, 2003 MCA].

Changes From Former Law: Except for changing the form of reference to the Uniform Commercial Code [Title 30, chapters 1 through 9A], this section is identical to former UCC Section 1-104 [30-1-104, 2003 MCA].

1. This section embodies the policy that an act that bears evidence of carefully considered permanent regulative intention should not lightly be regarded as impliedly repealed by subsequent legislation. The Uniform Commercial Code [Title 30, chapters 1 through 9A], carefully integrated and intended as a uniform codification of permanent character covering an entire "field" of law, is to be regarded as particularly resistant to implied repeal.

30-1-106. Remedies to be liberally administered.

Official Comment

[*Corresponding U.C.C. Section:* Section 1-305, U.C.C.]

Source: Former Section 1-106 [30-1-106, 2003 MCA].

Changes From Former Law: Other than changes in the form of reference to the Uniform Commercial Code [Title 30, chapters 1 through 9A], this section is identical to former UCC Section 1-106 [30-1-106, 2003 MCA].

1. Subsection (a) [subsection (1)] is intended to effect three propositions. The first is to negate the possibility of unduly narrow or technical interpretation of remedial provisions by providing that the remedies in the Uniform Commercial Code [Title 30, chapters 1 through 9A] are to be liberally administered to the end stated in this section. The second is to make it clear that compensatory damages are limited to compensation. They do not include consequential or special damages, or penal damages; and the Uniform Commercial Code [Title 30, chapters 1 through 9A] elsewhere makes it clear that damages must be minimized. Cf. Sections 1-203 [30-1-211], 2-706(1) [30-2-706(1)], and 2-712(2) [30-2-712(2)]. The third purpose of subsection (a) [subsection (1)] is to reject any doctrine that damages must be calculable with mathematical accuracy. Compensatory

damages are often at best approximate: they have to be proved with whatever definiteness and accuracy the facts permit, but no more. Cf. Section 2-204(3) [30-2-204(3)].

2. Under subsection (b) [subsection (2)], any right or obligation described in the Uniform Commercial Code [Title 30, chapters 1 through 9A] is enforceable by action, even though no remedy may be expressly provided, unless a particular provision specifies a different and limited effect. Whether specific performance or other equitable relief is available is determined not by this section but by specific provisions and by supplementary principles. Cf. Sections 1-103 [30-1-102(1) and 30-1-103], 2-716 [30-2-716].

3. "Consequential" or "special" damages and "penal" damages are not defined in the Uniform Commercial Code [Title 30, chapters 1 through 9A]; rather, these terms are used in the sense in which they are used outside the Uniform Commercial Code [Title 30, chapters 1 through 9A].

Case Notes

No Award of Attorney Fees Absent Statutory or Contract Provisions: Under 30-1-106, remedies under the U.C.C. shall be liberally administered to the end that the aggrieved party may be put in as good a position as if the other party had fully performed, but neither consequential, special, nor penal damages may be had except as specifically provided in the U.C.C. or by other rule of law. Although 30-2-714 allows recovery of incidental and consequential damages when accepted goods are in issue, the definitions of incidental and consequential damages contained in 30-2-715 do not include the award of attorney fees. In this case, the District Court awarded damages for delivery of nonconforming goods, plus attorney fees. The Supreme Court affirmed the award of damages but reversed the award of attorney fees as costs or damages absent any statutory or contract provisions, citing Martin v. Crown Life Ins. Co., 202 M 461, 658 P2d 1099 (1983). Meland v. Intermtn. Sys., Inc., 219 M 242, 712 P2d 1295, 42 St. Rep. 1987 (1985).

Contract for Scrap Metal — Resale After Breach — Measure of Damages: Where plaintiff and defendant entered into a contract whereby defendant was to purchase crushed auto bodies from plaintiff and where defendant refused to accept approximately one-half of the bodies at the agreed price, the plaintiff was entitled to damages representing the difference in price between what he actually received for the auto bodies upon resale, after the defendant refused to accept them, and what he would have received had the defendant not breached the contract. The plaintiff was not required to resell the bodies to the defendant. Weissman & Sons, Inc. v. Pepper, 480 F. Supp. 1364 (D.C. Mont. 1979).

30-1-107. Waiver or renunciation of claim or right after breach.

Official Comment

[*Corresponding U.C.C. Section:* Section 1-306, U.C.C.]

Source: Former Section 1-107 [30-1-107, 2003 MCA].

Changes From Former Law: This section changes former law in two respects. First, former Section 1-107 [30-1-107, 2003 MCA], requiring the "delivery" of a "written waiver or renunciation" merges the separate concepts of the aggrieved party's agreement to forego rights and the manifestation of that agreement. This section separates those concepts, and explicitly requires *agreement* of the aggrieved party. Second, the revised section reflects developments in electronic commerce by providing for memorialization in an authenticated record.

1. This section makes consideration unnecessary to the effective renunciation or waiver of rights or claims arising out of an alleged breach of a commercial contract where the agreement effecting such renunciation is memorialized in a record authenticated by the aggrieved party. Its provisions, however, must be read in conjunction with the section imposing an obligation of good faith. (Section 1-304) [30-1-203].

Compiler's Comments

2005 Amendment: Chapter 575 at end substituted "by agreement of the aggrieved party in an authenticated record" for "by a written waiver or renunciation signed and delivered by the aggrieved party"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-1-108. Severability.

Official Comment

[*Corresponding U.C.C. Section:* Section 1-105, U.C.C.]

Source: Former Section 1-108 [30-1-108, 2003 MCA].

Changes From Former Law: Except for changing the form of reference to the Uniform Commercial Code [Title 30, chapters 1 through 9A], this section is identical to former UCC Section 1-108 [30-1-108, 2003 MCA].

1. This is the model severability section recommended by the National Conference of Commissioners on Uniform State Laws for inclusion in all acts of extensive scope.

30-1-109. Section captions.

Official Comment

[*Corresponding U.C.C. Section:* Section 1-107, U.C.C.]

Source: Former Section 1-109 [30-1-109, 2003 MCA].

Changes From Former Law: None.

1. Section captions are a part of the text of the Uniform Commercial Code [Title 30, chapters 1 through 9A], and not mere surplusage. This is not the case, however, with respect to subsection headings appearing in Article 9 [Title 30, chapter 9A]. See Preliminary Comment 3 to Section 9-101 [30-9A-101] ("subsection headings are not a part of the official text itself and have not been approved by the sponsors.").

Part 2

General Definitions and Principles of Interpretation

30-1-201. General definitions.

Official Comment

[*Corresponding U.C.C. Section:* Section 1-201, U.C.C.]

[*Code Commissioner Note:* For this section, in 2005, Montana adopted Alternative B of the 2003 revisions to Article 7.]

Source: Former Section 1-201 [30-1-201, 2003 MCA].

Changes From Former Law: In order to make it clear that all definitions in the Uniform Commercial Code [Title 30, chapters 1 through 9A] - not just those in Article 1 [Title 30, chapter 1] - do not apply if the context otherwise requires, a new subsection (a) [subsection (1)] to that effect has been added. The reference to the "context" is intended to refer to the context in which the defined term is used in the UCC [Title 30, chapters 1 through 9A]. In other words, the definition applies whenever the defined term is used unless the context in which the defined term is used in the statute indicates that the term was not used in its defined sense. Consider, for example, UCC § 3-103(a)(9) [30-3-102(1)(i)] (defining "promise," in relevant part, as "a written undertaking to pay money signed by the person undertaking to pay") and 3-303(a)(1) [30-3-303(1)(a)] (indicating that an instrument is issued or transferred for value if "the instrument is issued or transferred for a promise of performance, to the extent that the promise has been performed." It is clear from the statutory context of the use of the word "promise" in Section 3-303(a)(1) [30-3-303(1)(a)] that the term was not used in the sense of its definition in Section 3-103(a)(9) [30-3-102(1)(i)]. Thus, the Section 3-103(a)(9) [30-3-102(1)(i)] definition should not be used to give meaning to the word "promise" in Section 3-303(a) [30-3-303(1)]. The remainder of former Section 1-201 [30-1-201], as revised, now appears as subsection (b) [subsection (2)].

Other than minor stylistic changes, the definitions in this draft are as in former Article 1 [Title 30, chapter 1, 2003 MCA] (as amended, most recently, in conjunction with revisions to Article 9 [Title 30, chapter 9A]) except as noted below. It should be noted that numbering of existing definitions has been left constant even though some new definitions have been added to this section and some others have been moved to other sections.

1. [subsection (2)(a)] "Action." Unchanged from former Section 1-201 [30-1-201, 2003 MCA], which was derived from similar definitions in Section 191, Uniform Negotiable Instruments Law; Section 76, Uniform Sales Act; Section 58, Uniform Warehouse Receipts Act; Section 53, Uniform Bills of Lading Act.

2. [subsection (2)(b)] "Aggrieved party." Unchanged from former Section 1-201 [30-1-201, 2003 MCA].

3. [subsection (2)(c)] "Agreement." Derived from former Section 1-201 [30-1-201, 2003 MCA]. As used in the Uniform Commercial Code [Title 30, chapters 1 through 9A] the word is intended to include full recognition of usage of trade, course of dealing, course of performance and the surrounding circumstances as effective parts thereof, and of any agreement permitted under the

provisions of the Uniform Commercial Code [Title 30, chapters 1 through 9A] to displace a stated rule of law. Whether an agreement has legal consequences is determined by applicable provisions of the Uniform Commercial Code [Title 30, chapters 1 through 9A] and, to the extent provided in Section 1-103 [30-1-102(1) and 30-1-103], by the law of contracts.

3a. [subsection (2)(d)] "Authenticate." This is the standard definition of the term used in acts prepared by the National Conference of Commissioners on Uniform State Laws.

4. [subsection (2)(e)] "Bank." Derived from Section 4A-104 [sic] [30-4A-105].

5. [subsection (2)(f)] "Bearer". Unchanged, except in one respect, from former section 1-201 [30-1-201, 2003 MCA], which was derived from Section 191, Uniform Negotiable Instruments Law. The term bearer applies to negotiable documents of title and has been broadened to include a person in control of an electronic negotiable document of title. Control in the context of an electronic document of title is defined in Article 7 (Section 7-106) [Title 30, chapter 7 (30-7-107)].

6. [subsection (2)(g)] "Bill of Lading". Derived from former Section 1-201 [30-1-201, 2003 MCA]. The reference to, and definition of, an "airbill" has been deleted as no longer necessary. A bill of lading is one type of document of title as defined in subsection (16) [subsection (2)(q)]. This definition should be read in conjunction with the definition of carrier in Article 7 (Section 7-102) [Title 30, chapter 7 (30-7-102)].

7. [subsection (2)(h)] "Branch." Unchanged from former Section 1-201 [30-1-201, 2003 MCA].

8. [subsection (2)(i)] "Burden of establishing a fact." Unchanged from former Section 1-201 [30-1-201, 2003 MCA].

9. [subsection (2)(j)] "Buyer in ordinary course of business." Unchanged from former Section 1-201 [30-1-201, 2003 MCA] (as amended in conjunction with the 1999 revisions to Article 9 [Title 30, chapter 9A]). The major significance of the phrase lies in Section 2-403 [30-2-403] and in the Article on Secured Transactions (Article 9) [Title 30, chapter 9A].

The first sentence of paragraph (9) [subsection (2)(j)] makes clear that a buyer from a pawnbroker cannot be a buyer in ordinary course of business. The second sentence tracks Section 6-102(1)(m) [now repealed]. It explains what it means to buy "in the ordinary course." The penultimate sentence prevents a buyer that does not have the right to possession as against the seller from being a buyer in ordinary course of business. Concerning when a buyer obtains possessory rights, see Sections 2-502 [30-2-502] and 2-716 [30-2-716]. However, the penultimate sentence is not intended to affect a buyer's status as a buyer in ordinary course of business in cases (such as a "drop shipment") involving delivery by the seller to a person buying from the buyer or a donee from the buyer. The requirement relates to whether *as against the seller* the buyer or one taking through the buyer has possessory rights.

10. [subsection (2)(k)] "Conspicuous." Derived from Section 2-103(a)(10) [30-1-201(10), 2003 MCA]. It states the general standard that to be conspicuous a term ought to be noticed by a reasonable person. Whether a term is conspicuous is an issue for the court. Subparagraphs (A) and (B) [subsections (2)(k)(i) and (2)(k)(ii)] set out several methods for making a term conspicuous. Requiring that a term be conspicuous blends a notice function (the term ought to be noticed) and a planning function (giving guidance to the party relying on the term regarding how that result can be achieved). Although these paragraphs indicate some of the methods for making a term attention-calling, the test is whether attention can reasonably be expected to be called to it. The statutory language should not be construed to permit a result that is inconsistent with that test.

11. [subsection (2)(l)] "Consumer." Derived from Section 9-102(a)(25) [30-9A-102(1)(z)].

12. [subsection (2)(m)] "Contract." Unchanged from former Section 1-201 [30-1-201, 2003 MCA].

13. [subsection (2)(n)] "Creditor." Unchanged from former Section 1-201 [30-1-201, 2003 MCA].

14. [subsection (2)(o)] "Defendant." Unchanged from former Section 1-201 [30-1-201, 2003 MCA], which was derived from Section 76, Uniform Sales Act.

15. [subsection (2)(p)] "Delivery". Derived from former Section 1-201 [30-1-201, 2003 MCA]. The reference to certificated securities has been deleted in light of the more specific treatment of the matter in Section 8-301 [now repealed]. The definition has been revised to accommodate electronic documents of title. Control in the context of an electronic document of title is defined in Article 7 (Section 7-106) [Title 30, chapter 7 (30-7-107)].

16. [subsection (2)(q)] "Document of title". Derived from former Section 1-201 [30-1-201, 2003 MCA], which was derived from Section 76, Uniform Sales Act. This definition makes explicit that the obligation or designation of a third party as "bailee" is essential to a document of title and clearly rejects any such result as obtained in Hixson v. Ward, 254 Ill.App. 505 (1929), which treated a conditional sales contract as a document of title. Also the definition is left open

so that new types of documents may be included, including documents which gain commercial recognition in the international arena. See UNCITRAL Draft Instrument on Transport Law. It is unforeseeable what documents may one day serve the essential purpose now filled by warehouse receipts and bills of lading. The definition is stated in terms of the function of the documents with the intention that any document which gains commercial recognition as accomplishing the desired result shall be included within its scope. Fungible goods are adequately identified within the language of the definition by identification of the mass of which they are a part.

Dock warrants were within the Sales Act definition of document of title apparently for the purpose of recognizing a valid tender by means of such paper. In current commercial practice a dock warrant or receipt is a kind of interim certificate issued by shipping companies upon delivery of the goods at the dock, entitling a designated person to be issued a bill of lading. The receipt itself is invariably nonnegotiable in form although it may indicate that a negotiable bill is to be forthcoming. Such a document is not within the general compass of the definition, although trade usage may in some cases entitle such paper to be treated as a document of title. If the dock receipt actually represents a storage obligation undertaken by the shipping company, then it is a warehouse receipt within this Section regardless of the name given to the instrument.

The goods must be "described", but the description may be by marks or labels and may be qualified in such a way as to disclaim personal knowledge of the issuer regarding contents or condition. However, baggage and parcel checks and similar "tokens" of storage which identify stored goods only as those received in exchange for the token are not covered by this Article. The definition is broad enough to include an airway bill.

A document of title may be either tangible or electronic. Tangible documents of title should be construed to mean traditional paper documents. Electronic documents of title are documents that are stored in an electronic medium instead of in tangible form. The concept of an electronic medium should be construed liberally to include electronic, digital, magnetic, optical, electromagnetic, or any other current or similar emerging technologies. As to reissuing a document of title in an alternative medium, see Article 7, Section 7-105 [Title 30, chapter 7 (30-7-106)]. Control for electronic documents of title is defined in Article 7 (Section 7-106) [Title 30, chapter 7 (30-7-107)].

17. [subsection (2)(r)] "Fault." Derived from former Section 1-201 [30-1-201, 2003 MCA]. "Default" has been added to the list events constituting fault.

18. [subsection (2)(s)] "Fungible [goods]." Derived from former Section 1-201 [30-1-201, 2003 MCA]. The definition has been reorganized and references to securities have been deleted because Article 8 [Title 30, chapter 8] no longer uses the term "fungible" to describe securities.

19. [subsection (2)(t)] "Genuine." Unchanged from former Section 1-201 [30-1-201, 2003 MCA].

20. [subsection (2)(u)] "Good faith." Former Section 1-201(19) [30-1-201(19), 2003 MCA] defined "good faith" simply as honesty in fact; the definition contained no element of commercial reasonableness. Initially, that definition applied throughout the Code with only one exception. Former Section 2-103(1)(b) [30-2-103(1)(b)] provided that *"in this Article. . .* good faith in the case of a merchant means honesty in fact and the observance of reasonable commercial standards of fair dealing in the trade." This alternative definition was limited in applicability in three ways. First, it applied only to transactions within the scope of Article 2 [Title 30, chapter 2]. Second, it applied only to merchants. Third, strictly construed it applied only to uses of the phrase "good faith" *in Article 2 [Title 30, chapter 2]*; thus, so construed it would not define "good faith" for its most important use - the obligation of good faith imposed by former UCC Section 1-203 [sic] [30-2-103].

Over time, however, amendments to the UCC brought the Article 2 [Title 30, chapter 2] merchant concept of good faith (subjective honesty and objective reasonableness) into other Articles. First, Article 2A [Title 30, chapter 2A] explicitly incorporated the Article 2 [Title 30, chapter 2] standard. See current UCC Section 2A-103(7) [30-2A-103]. Then, other Articles broadened the applicability of that standard by adopting it for all parties rather than just for merchants. *See, e.g.*, UCC Sections 3-103(a)(4) [30-3-102(1)(d)], 4A-105(a)(6) [30-4A-105(1)(f)], 8-102(a)(10) [30-8-112(1)(j)], and 9-102(a)(43) [30-9A-102(1)(qq)]. See also Draft of Revised Article 2 [Title 30, chapter 2]. All of these definitions are comprised of two elements - honesty in fact *and* the observance of reasonable commercial standards of fair dealing. Only revised Article 5 [Title 30, chapter 5] defines "good faith" solely in terms of subjective honesty, and only Article 6 [Title 30, chapter 6, now repealed] and Article 7 [Title 30, chapter 7] are without definitions of good faith. (It should be noted that, while revised Article 6 [Title 30, chapter 6, now repealed] did not define good faith, Comment 2 to revised UCC Section 6-102 states that "this Article adopts the definition of 'good faith' in Article 1 in all cases, even when the buyer is a merchant.") Given this near unanimity, it is appropriate to move the broader definition of "good faith" to Article 1 [Title 30, chapter 1]. Of course, this definition is subject to the applicability of the narrower definition in revised Article 5 [Title 30, chapter 5].

21. [subsection (2)(v)] "Holder". Derived from former Section 1-201 [30-1-201, 2003 MCA]. The definition has been reorganized for clarity and amended to provide for electronic negotiable documents of title.

22. [subsection (2)(w)] "Insolvency proceedings." Unchanged from former Section 1-201 [30-1-201, 2003 MCA].

23. [subsection (2)(x)] "Insolvent." Derived from former Section 1-201 [30-1-201, 2003 MCA]. The three tests of insolvency - "generally ceased to pay debts in the ordinary course of business other than as a result of a bona fide dispute as to them," "unable to pay debts as they become due," and "insolvent within the meaning of the federal bankruptcy law" - are expressly set up as alternative tests and must be approached from a commercial standpoint.

24. [subsection (2)(y)] "Money." Unchanged from former Section 1-201 [30-1-201, 2003 MCA]. The test is that of sanction of government, whether by authorization before issue or adoption afterward, which recognizes the circulating medium as a part of the official currency of that government. The narrow view that money is limited to legal tender is rejected.

25. [subsection (2)(z)] "Organization." The former definition of this word has been replaced with the standard definition used in acts prepared by the National Conference of Commissioners on Uniform State Laws.

26. [subsection (2)(aa)] "Party." Substantively identical to former Section 1-201 [30-1-201, 2003 MCA]. Mention of a party includes, of course, a person acting through an agent. However, where an agent comes into opposition or contrast to the principal, particular account is taken of that situation.

27. [subsection (2)(bb)] "Person." The former definition of this word has been replaced with the standard definition used in acts prepared by the National Conference of Commissioners on Uniform State Laws.

28. [not adopted] "Present value." This definition was formerly contained within the definition of "security interest" in former Section 1-201(37) [30-1-201(37), 2003 MCA].

[28a.] [subsection (2)(cc)] "Presumption." Unchanged from former Section 1-201 [30-1-201, 2003 MCA].

29. [subsection (2)(dd)] "Purchase." Derived from former UCC Section 1-201 [30-1-201, 2003 MCA]. The form of definition has been changed from "includes" to "means."

30. [subsection (2)(ee)] "Purchaser." Unchanged from former Section 1-201 [30-1-201, 2003 MCA].

31. [subsection (2)(ff)] "Record." Derived from Section 9-102(a)(69) [30-9A-102(1)(l)].

32. [subsection (2)(gg)] "Remedy." Unchanged from former Section 1-201 [30-1-201, 2003 MCA]. The purpose is to make it clear that both remedy and right (as defined) include those remedial rights of "self help" which are among the most important bodies of rights under the Uniform Commercial Code [Title 30, chapters 1 through 9A], remedial rights being those to which an aggrieved party can resort on its own motion.

33. (2)(hh) "Representative." Derived from former Section 1-201 [30-1-201, 2003 MCA]. Reorganized, and form changed from "includes" to "means."

34. [subsection (2)(ii)] "Right." Unchanged from former Section 1-201 [30-1-201, 2003 MCA].

35. [subsection (2)(jj)] "Security Interest." The definition is the first paragraph of the definition of "security interest" in former Section 1-201 [30-1-201, 2003 MCA]. The remaining portion has been moved to Section 1-203 [30-1-211]. Notice that in view of Article 9 [Title 30, chapter 9A] the term includes the interest of certain outright buyers of certain kinds of property.

36. [subsection (2)(kk)] "Send." New. Compare "notifies".

37. [subsection (2)(ll)] "Signed." Derived from former Section 1-201 [30-1-201, 2003 MCA]. Former Section 1-201 [30-1-201, 2003 MCA] referred to "intention to authenticate"; because authenticate is now a defined term, the language has been changed to "intention to adopt or accept." The latter formulation is derived from the definition of "authenticate," The definition of "signed" is to make clear that, as the term is used in the Uniform Commercial Code [Title 30, chapters 1 through 9A], a complete signature is not necessary. The symbol may be printed, stamped or written; it may be by initials or by thumbprint. It may be on any part of the document and in appropriate cases may be found in a billhead or letterhead. No catalog of possible situations can be complete and the court must use common sense and commercial experience in passing upon these matters. The question always is whether the symbol was executed or adopted by the party with present intention to adopt or accept the writing.

38. [not adopted] “State.” This is the standard definition of the term used in acts prepared by the National Conference of Commissioners on Uniform State Laws.

39. [subsection (2)(mm)] “Surety.” This definition makes it clear that “surety” includes all secondary obligors, not just those whose obligation refers to them person obligated as a surety. As to the nature of secondary obligations generally, see Restatement of Suretyship and Guaranty § 1.

40. [subsection (2)(nn)] “Term.” Unchanged from former Section 1-201 [30-1-201, 2003 MCA].

41. [subsection (2)(oo)] “Unauthorized signature.” Unchanged from former Section 1-201 [30-1-201, 2003 MCA].

42. [subsection (2)(pp)] “Warehouse receipt”. Derived from former Section 1-201 [30-1-201, 2003 MCA], which was derived from Section 76(1), Uniform Sales Act; Section 1, Uniform Warehouse Receipts Act. Receipts issued by a field warehouse are included, provided the warehouseman and the depositor of the goods are different persons. The definition makes clear that the receipt must qualify as a document of title under subsection (16) [subsection (2)(q)].

43. [subsection (2)(qq)] “Written” or “writing.” Unchanged from former Section 1-201 [30-1-201, 2003 MCA].

Compiler’s Comments

2005 Amendment: Chapter 575 inserted (1) establishing scope of definitions; in (2) in introductory clause at end deleted “and unless the context otherwise requires, in this code”; in definition of aggrieved party substituted “pursue” for “resort to”; in definition of agreement substituted “inferred” for “by implication”, inserted “course of performance”, and at end substituted “as provided in 30-1-205” for “or course of performance as provided in this code (30-1-205 and 30-2-208). Whether an agreement has legal consequences is determined by the provisions of this code, if applicable; otherwise by the law of contracts (30-1-103)”; inserted definition of authenticate; in definition of bank inserted “and includes a savings bank, savings and loan association, credit union, and trust company”; in definition of bearer inserted “a person in control of a negotiable electronic document of title or a” and near middle substituted “of a negotiable instrument, negotiable tangible document” for “of an instrument, document”; in definition of bill of lading near beginning of (i) inserted “of title”, near end inserted “directly or indirectly”, and at end deleted “and includes an airbill. “Airbill” means a document serving for air transportation as a bill of lading does for marine or rail transportation, and includes an air consignment note or air waybill” and inserted (ii) relating to warehouse receipt; in definition of conspicuous near beginning of first sentence substituted “with reference to a term, means so written, displayed, or presented” for “A term or clause is conspicuous when it is so written”, deleted former second, third, and fourth sentences that read: “A printed heading in capitals (as: Non-Negotiable Bill of Lading) is conspicuous. Language in the body of a form is “conspicuous” if it is in larger or other contrasting type or color. But in a telegram any stated term is “conspicuous””, in second sentence after “term” deleted “or clause”, and inserted third sentence and (i) and (ii) regarding examples of conspicuous terms; inserted definition of consumer; in definition of contract near end inserted “as supplemented by”; in definition of defendant substituted “counterclaim or third-party claim” for “cross-action or counterclaim”; in definition of delivery inserted “an electronic document of title means voluntary transfer of control and with respect to”, inserted “tangible”, and after “paper” deleted “or certificated securities”; in definition of document of title in (i) at beginning substituted “means a record” for “includes bill of lading, dock warrant, dock receipt, warehouse receipt or order for the delivery of goods, and also any other document”, in (i)(A) near middle after “possession” inserted “or control”, after “receive” inserted “control”, and near end substituted “record and the goods the record covers” for “document and the goods it covers”, in (i)(B) substituted “that purports to be issued by or addressed to a bailee and to cover goods in the bailee’s possession which are either identified or are fungible portions of an identified mass” for “To be a document of title a document must purport to be issued by or addressed to a bailee and purport to cover goods in the bailee’s possession which are either identified or are fungible portions of an identified mass”, and inserted (ii) relating to inclusions and electronic and tangible documents; in definition of fault at end inserted “or default”; substituted fungible goods for fungible as defined term and before “means” deleted “or securities”, in (i) near beginning after “goods” deleted “or securities” and at end deleted “Goods which are not fungible shall be deemed fungible for the purposes of this code to the extent that under a particular”, and in (ii) at beginning substituted “goods which by agreement” for “agreement or document unlike units”; in definition of good faith at beginning inserted exception clause and at end substituted “and the observance of reasonable commercial standards of fair dealing” for “in the conduct or transaction concerned”; in definition of holder in (i) at beginning deleted “negotiable instrument, means”, after “possession” substituted “of a negotiable" for "if the", and near end substituted "payable either to bearer or to an identified person that is" for "payable to bearer or to", deleted former (b) that read: "(b) certified security, means the person in possession is the registered owner, the security has been indorsed to the person in possession by the registered owner, or the security is in bearer form", in (ii) at beginning substituted "a person in possession of a negotiable tangible document of title" for "document of title, means the person in possession" and after "deliverable" inserted "either", and inserted (iii) relating to person in control of electronic document; deleted definition of honor that read: "To "honor" is to pay or to accept and pay, or where a credit so engages to purchase or discount a draft complying with the terms of the credit"; in definition of insolvent in (i) at beginning substituted "having generally ceased" for "A person is "insolvent" who either has ceased" and at end inserted "other than as a result of bona fide dispute" and in (ii) at beginning substituted "unable to" for "cannot"; in definition of money in first sentence after "exchange" inserted "currently" and at beginning of second sentence inserted "The term includes a monetary unit of account established by an" and at end inserted "or by agreement between two or more countries"; deleted definition of notice that read: "A person has "notice" of a fact when:

(a) he has actual knowledge of it; or

(b) he has received a notice or notification of it; or

(c) from all the facts and circumstances known to him at the time in question he has reason to know that it exists. A person "knows" or has "knowledge" of a fact when he has actual knowledge of it. "Discover" or "learn" or a word or phrase of similar import refers to knowledge rather than to reason to know. The time and circumstances under which a notice or notification may cease to be effective are not determined by this code"; deleted definition of notifies or gives that read: "A person "notifies" or "gives" a notice or notification to another by taking such steps as may be reasonably required to inform the other in ordinary course whether or not such other actually comes to know of it. A person "receives" a notice or notification when:

(a) it comes to his attention; or

(b) it is duly delivered at the place of business through which the contract was made or at any other place held out by him as the place for receipt of such communications"; deleted definition of notice that read: "Notice, knowledge or a notice or notification received by an organization is effective for a particular transaction from the time when it is brought to the attention of the individual conducting that transaction, and in any event from the time when it would have been brought to his attention if the organization had exercised due diligence. An organization exercises due diligence if it maintains reasonable routines for communicating significant information to the person conducting the transaction and there is reasonable compliance with the routines. Due diligence does not require an individual acting for the organization to communicate information unless such communication is part of his regular duties or unless he has reason to know of the transaction and that the transaction would be materially affected by the information"; in definition of organization substituted "means a person other than an individual" for "includes a corporation, government or governmental subdivision or agency, business trust, estate, trust, partnership or association, two or more persons having a joint or common interest, or any other legal or commercial entity"; in definition of party after "agreement" substituted "subject to" for "within"; in definition of person substituted "means an individual, corporation, business trust, estate, trust, partnership, limited liability company, association, joint venture, government, governmental subdivision, agency, or instrumentality, public corporation, or any other legal or commercial entity" for "includes an individual or an organization"; in definition of purchase near beginning substituted "means taking by sale, lease" for "includes taking by sale"; inserted definition of record; in definition of security interest at end substituted "Whether a transaction in the form of a lease creates a "security interest" is determined pursuant to 30-1-211" for "Whether a transaction creates a lease or security interest is determined by the facts of each case; however, a transaction creates a security interest if the consideration the lessee is to pay the lessor for the right to possession and use of the goods is an obligation for the term of the lease not subject to termination by the lessee and:

(i) the original term of the lease is equal to or greater than the remaining economic life of the goods;

(ii) the lessee is bound to renew the lease for the remaining economic life of the goods or is bound to become the owner of the goods;

(iii) the lessee has an option to renew the lease for the remaining economic life of the goods for no additional consideration or nominal additional consideration upon compliance with the lease agreement; or

(iv) the lessee has an option to become the owner of the goods for no additional consideration or nominal additional consideration upon compliance with the lease agreement.

(b) A transaction does not create a security interest merely because it provides that:

(i) the present value of the consideration the lessee is obligated to pay the lessor for the right to possession and use of the goods is substantially equal to or is greater than the fair market value of the goods at the time the lease is entered into;

(ii) the lessee assumes risk of loss of the goods or agrees to pay taxes, insurance, filing, recording, or registration fees or service or maintenance costs with respect to the goods;

(iii) the lessee has an option to renew the lease or to become the owner of the goods;

(iv) the lessee has an option to renew the lease for a fixed rent that is equal to or greater than the reasonably predictable fair market value for the use of the goods for the term of the renewal at the time the option is to be performed; or

(v) the lessee has an option to become the owner of the goods for a fixed price that is equal to or greater than the reasonably predictable fair market value of the goods at the time the option is to be performed.

(c) For purposes of this subsection (37):

(i) additional consideration is not nominal if:

(A) when the option to renew the lease is granted to the lessee, the rent is stated to be the fair market rent for the use of the goods for the term of the renewal determined at the time the option is to be performed; or

(B) when the option to become the owner of the goods is granted to the lessee, the price is stated to be the fair market value of the goods determined at the time the option is to be performed;

(ii) additional consideration is nominal if it is less than the lessee's reasonably predictable cost of performing under the lease agreement if the option is not exercised;

(iii) "reasonably predictable" and "remaining economic life of the goods" are to be determined with reference to the facts and circumstances at the time the transaction is entered into; and

(iv) "present value" means the amount as of a date certain of one or more sums payable in the future, discounted to the date certain. The discount is determined by the interest rate specified by the parties if the rate is not manifestly unreasonable at the time the transaction is entered into; otherwise, the discount is determined by a commercially reasonable rate that takes into account the facts and circumstances of each case at the time the transaction was entered into"; in definition of send in introductory clause after "writing" inserted "record", in (i) at end deleted "The receipt of any writing or notice within the time at which it would have arrived if properly sent has the effect of a proper sending", and inserted (ii) relating to timely arrival; in definition of signed after "adopted" deleted "by a party" and near end substituted "adopt or accept" for "authenticate"; in definition of surety at end inserted "or other secondary obligor"; deleted definition of telegram that read: ""Telegram" includes a message transmitted by radio, teletype, cable, any mechanical method of transmission, or the like"; deleted definition of value that read: ""Value". Except as otherwise provided with respect to negotiable instruments and bank collections (30-3-303, 30-4-208, and 30-4-209), a person gives "value" for rights if he acquires them:

(a) in return for a binding commitment to extend credit or for the extension of immediately available credit whether or not drawn upon and whether or not a charge-back is provided for in the event of difficulties in collection; or

(b) as security for or in total or partial satisfaction of a preexisting claim; or

(c) by accepting delivery pursuant to a preexisting contract for purchase; or

(d) generally, in return for any consideration sufficient to support a simple contract"; in definition of warehouse receipt substituted "document of title" for "receipt"; substituted writing for written or writing as defined term and inserted second sentence relating to "written"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

2001 Amendment: Chapter 179 in definition of security interest at end of (a) inserted last sentence concerning determination by facts of each case, inserted (a)(i) through (a)(iv) concerning term of lease, option to renew lease, option to renew lease for nominal consideration, or option to become owner for nominal consideration, inserted (b) concerning when transaction does not create security interest, and inserted (c) specifying when additional consideration is or is not nominal and defining terms. Amendment effective July 1, 2001.

1999 Amendment: Chapter 305 substituted definition of buyer in ordinary course of business for former definition that read: ""Buyer in ordinary course of business" means a person who, in good faith and without knowledge that the sale to him is in violation of the ownership rights or security interest of a third party in the goods, buys in ordinary course from a person in the business of selling goods of that kind, but does not include a pawnbroker. All persons who sell minerals or the like (including oil and gas) at wellhead or minehead shall be considered to be persons in the business of selling goods of that kind. "Buying" may be for cash or by exchange of other property or on secured or unsecured credit and includes receiving goods or documents of title under a preexisting contract for sale but does not include a transfer in bulk or as security for or in total or partial satisfaction of a money debt"; substituted definition of security interest for former definition that read: "(a) "Security interest" means an interest in personal property or fixtures that secures payment or performance of an obligation. The retention or reservation of title by a seller of goods notwithstanding shipment or delivery to the buyer (30-2-401) is limited in effect to a reservation of a "security interest". The term also includes any interest of a buyer of accounts or chattel paper that is subject to chapter 9. The special property interest of a buyer of goods on identification of those goods to a contract for sale under 30-2-401 is not a "security interest", but a buyer may also acquire a "security interest" by complying with chapter 9. Unless a consignment is intended as security, reservation of title thereunder is not a "security interest", but a consignment in any event is subject to the provisions on consignment sales (30-2-326). Whether a transaction creates a lease or security interest is determined by the facts of each case; however, a transaction creates a security interest if the consideration the lessee is to pay the lessor for the right to possession and use of the goods is an obligation for the term of the lease not subject to termination by the lessee and:

(i) the original term of the lease is equal to or greater than the remaining economic life of the goods;

(ii) the lessee is bound to renew the lease for the remaining economic life of the goods or is bound to become the owner of the goods;

(iii) the lessee has an option to renew the lease for the remaining economic life of the goods for no additional consideration or nominal additional consideration upon compliance with the lease agreement; or

(iv) the lessee has an option to become the owner of the goods for no additional consideration or nominal additional consideration upon compliance with the lease agreement.

(b) A transaction does not create a security interest merely because it provides that:

(i) the present value of the consideration the lessee is obligated to pay the lessor for the right to possession and use of the goods is substantially equal to or is greater than the fair market value of the goods at the time the lease is entered into;

(ii) the lessee assumes risk of loss of the goods or agrees to pay taxes, insurance, filing, recording, or registration fees or service or maintenance costs with respect to the goods;

(iii) the lessee has an option to renew the lease or to become the owner of the goods;

(iv) the lessee has an option to renew the lease for a fixed rent that is equal to or greater than the reasonably predictable fair market value for the use of the goods for the term of the renewal at the time the option is to be performed; or

(v) the lessee has an option to become the owner of the goods for a fixed price that is equal to or greater than the reasonably predictable fair market value of the goods at the time the option is to be performed.

(c) For purposes of this subsection (37):

(i) additional consideration is not nominal if:

(A) when the option to renew the lease is granted to the lessee, the rent is stated to be the fair market rent for the use of the goods for the term of the renewal determined at the time the option is to be performed; or

(B) when the option to become the owner of the goods is granted to the lessee, the price is stated to be the fair market value of the goods determined at the time the option is to be performed;

(ii) additional consideration is nominal if it is less than the lessee's reasonably predictable cost of performing under the lease agreement if the option is not exercised;

(iii) "reasonably predictable" and "remaining economic life of the goods" are to be determined with reference to the facts and circumstances at the time the transaction is entered into; and

(iv) "present value" means the amount as of a date certain of one or more sums payable in the future, discounted to the date certain. The discount is determined by the interest rate specified by the parties if the rate is not manifestly unreasonable at the time the transaction is entered into; otherwise, the discount is determined by a commercially reasonable rate that takes into account the facts and circumstances of each case at the time the transaction was entered into"; and made minor changes in style. Amendment effective July 1, 2001.

1991 Amendment: Substituted definition of holder for former definition that read: ""Holder" means a person who is in possession of a document of title or an instrument or a certificated investment security drawn, issued, or endorsed to him or to his order or to bearer or in blank"; at end of definition of money substituted "or intergovernmental organization" for "as a part of its currency"; in definition of security interest, at end of (a), substituted language concerning creation of a lease or security interest and the tests contained in subsections (a)(i) through (a)(iv) for "Whether a lease is intended as security is to be determined by the facts of each case; however, (a) the inclusion of an option to purchase does not of itself make the lease one intended for security, and (b) an agreement that upon compliance with the terms of the lease the lessee shall become or has the option to become the owner of the property for no additional consideration or for a nominal consideration does make the lease one intended for security", inserted (b) concerning transactions that do not create, and inserted (c) concerning additional consideration; in definition of unauthorized, after "signature", deleted "or endorsement"; and made minor changes in style.

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

1983 Amendment: In (5), inserted "certificated" before "security"; in (9) inserted second sentence relating to minerals, oil, and gas; in (14) inserted "certificated" before "securities"; in (20) inserted "certificated" before "investment"; in (37) deleted "contract rights" before "which is subject to Chapter 9".

Source of 1983 Amendments: The source of the 1983 amendments was both the 1972 amendments to Article 9 and the 1977 amendments to Article 8 of the Uniform Commercial Code drafted by the National Conference of Commissioners on Uniform State Laws. The amendments are to section 1-201 of the Official Text of the Uniform Commercial Code.

Administrative Rules

ARM 42.12.205 Requirements when liquor license subject to lien.

Case Notes

IRS Form 1099-C — Not Discharge of Debt — Creditor Still Able to Collect: The Supreme Court adopted the majority position regarding the purpose of the Form 1099-C and held that the issuance of an IRS Form 1099-C is not prima facie evidence of a creditor's intent to discharge a debt; rather, it is a means of satisfying the agency's reporting requirements and does not, in and of itself, prevent a creditor from seeking collection of a debt. Flathead Bank of Bigfork v. Masonry by Muller, Inc., 2016 MT 269, 385 Mont. 214, 383 P.3d 215.

No Standing to Recover Damages by Party Not Owner of Property — Fax Not Considered Valid Assignment of Damage Claim: Koelzer owned an inn by a mining and power generation site near Colstrip. Koelzer discovered that mining activity had damaged the inn and filed a complaint in 1994 against the mining and power generation companies, but did not pursue the damage claim. In 1996, Dale and Shawonda Lewis approached Koelzer about purchasing the inn, and the issue of the damages and Koelzer's claim came up. The Lewises inspected the inn and discovered additional damages, which led Koelzer to reassert the damage claim, but the claim was again unresolved. Nevertheless, the Lewises offered to buy the inn, and title was eventually conveyed to Dale's parents, who were able to secure financing. Koelzer notified the companies by fax that the inn had been sold and requested that the companies work with Dale on the structural damage discussed in the past. About 1 year later, Dale received an estimate of $91,000 to repair the damages and filed a complaint seeking compensation from the companies. Dale's parents eventually filed for bankruptcy, and the Lewises finally became the owners of record in 1998. When the companies discovered that the Lewises were not the owners of the inn at the time that the suit was filed, they moved for summary judgment, which was granted by the District Court on grounds that the Lewises had no standing to assert a claim for damages arising before they acquired title. On appeal, the Supreme Court cited the general rule that persons cannot recover for damages to property that they do not own. Further, even though property damage claims have long been recognized as assignable, the fax did not meet the statutory requirements of a valid assignment and was unenforceable. Thus, on the issue of prepurchase damages, no material question of fact existed regarding ownership or assignment, so the Lewises had no standing to bring a claim for damages prior to their ownership of the inn. Summary judgment was affirmed. Lewis v. Puget Sound Power & Light Co., 2001 MT 145, 306 M 37, 29 P3d 1028 (2001).

Commercial Reasonableness of Notification of Sale: It is not required that a debtor receive actual notice of a sale, only that the creditor take reasonable steps to assure that the debtor is notified. When a bank sent notice to defendant at his last-known address, the bank satisfied the statutory requirements for notice. First Nat'l Bank of Lewistown v. Mork, 257 M 495, 850 P2d 954, 50 St. Rep. 379 (1993).

Seizure of Collateral by Bank Not Bad Faith: The plaintiffs sued the defendant bank for breach of the covenant of good faith and fair dealing. The Supreme Court held that the relationship between the parties was contractual and that the plaintiffs' assertion that they only signed blank documents rather than documents pledging collateral to secure bank loans was not supported by the evidence. The court ruled that the bank did not act in bad faith in seizing the collateral when the plaintiffs defaulted on their loans. Stott v. Fox, 246 M 301, 805 P2d 1305, 47 St. Rep. 2040 (1990).

Merchant Pawnbroker Held to Good Faith Requirement: Defendant pawnshop operator who sold stolen property to plaintiff refused to give plaintiff a refund after the property was recovered by police. Defendant argued that he disclaimed any warranty of title to goods sold in his business by posting a sign alerting buyers that merchandise is sold "as is" and by writing the same notation on his sales slips. Defendant clearly breached the warranty of clear title under 30-2-312 when he sold stolen goods because neither a thief nor his successor pass clear title to stolen goods. It was irrelevant that defendant claimed he did not know the goods were stolen. With respect to breach of warranty, defendant as a merchant is held to a higher standard of dealing than ordinary consumers. In addition, he is held to the obligatory good faith required in the performance of every contract under the U.C.C., which is defined under this section as "honesty in fact". Brokke v. Williams, 235 M 305, 766 P2d 1311, 46 St. Rep. 6 (1989).

Transaction Constitutes Lease — Not Installment Sales Contract: The facts of this case indicate that the lessee did not have the option to obtain title to the property at no further charge at the termination of the lease. Therefore, the court found the characterization of the transaction was a lease of equipment and was not governed by the provisions of the Uniform Commercial Code. (See 1991 enactment of chapter 2A.) IFG Leasing Co. v. Schultz, 217 M 434, 705 P2d 576, 42 St. Rep. 1307 (1985), following Diede v. Davis, 203 M 205, 661 P2d 838, 40 St. Rep. 394 (1983).

Generally Worded After-Acquired Property Security Interest: Security interest covered all goods used in rental business, including but not limited to machinery, equipment, and inventory held for sale or rent "existing or hereafter acquired". Lower court's conclusion that a general description of items covered was insufficient and that trailers, hoppers, mixer, and loader used by renters to make, haul, and pour cement were not covered was erroneous. Further, the conclusion that there could be no security interest because those items were not financed by the holder of the security interest was also erroneous. Taylor Rental Corp. v. Ted Godwin Leasing, Inc., 209 M 124, 681 P2d 691, 41 St. Rep. 594 (1984).

Oral Notice Sufficient: Plaintiff entered numerous financing arrangements with Tri-Mont. Plaintiff had blanket security interests in Tri-Mont's after-acquired assets. Defendant also financed acquisitions of inventory for Tri-Mont. Defendant filed a purchase money security interest in certain property. Although there was no formal agreement between the parties, they routinely contacted one another prior to financing an item. Upon Tri-Mont's filing a bankruptcy petition, a dispute arose as to whether the defendant's security interest had been properly noticed to plaintiff, thereby giving priority to defendant's interest. Under 30-9-312 [now repealed, see 30-9A-322 through 30-9A-324], prior to perfecting a purchase money security interest, notice must be given to known secured parties. Plaintiff contended this notice had to be in writing. It was held that under the definitions of "notice" and "notifies" in 30-1-201, notice may be given orally, as was the case here. The defendant's oral notification to plaintiff was sufficient to put plaintiff on notice of its intent to perfect a purchase money security interest. Credit Alliance Corp. v. First Nat'l Bank of Missoula, 40 St. Rep. 2095 (Bankr. 9th Cir. 1983) (apparently not reported in Federal Supplement).

Reasonable Steps to Notify: Plaintiff bought a photography business and executed a promissory note with defendant. As collateral he assigned stock in the business. Plaintiff sold the business to Wolfe. Wolfe was to make payments to defendant to discharge his obligations, and these payments were to be directly applied to plaintiff's obligation under the promissory note. Defendant was escrow agent. Plaintiff later signed a financing statement granting defendant a security interest in the stock held in escrow. The defendant filed the security agreement. Wolfe became delinquent in his payments, and defendant notified plaintiff his payments were therefore delinquent. A later letter was sent by certified mail to the same address advising plaintiff the stock would be sold and applied to plaintiff's past-due loan. At the sale Wolfe bought the stock for the amount due on plaintiff's note. Plaintiff contended that notice of the foreclosure was deficient because he had moved and had not received the letter. The Supreme Court held that a creditor must only take reasonable steps to notify the debtor. Plaintiff received notice when the letter was delivered to the address. The actions of defendant were those reasonably required to notify plaintiff. Dulan v. Mont. Nat'l Bank of Roundup, 203 M 177, 661 P2d 28, 40 St. Rep. 376 (1983).

Lease as Installment Sale: The parties entered into an agreement for the installation and maintenance of a fire alarm system that was termed a "lease agreement". Payments were to be made over a 5-year term at the expiration of which defendant had the option to renew for another 5-year term or to purchase the system for $1. The District Court found that the transaction was in effect a "sale". The Supreme Court affirmed, saying that in circumstances where the purported lease gives the lessee the option to purchase the goods upon expiration of the term of the lease for a nominal amount, the lease is commercially indistinguishable from an installment sales contract and the provisions of the U.C.C. apply. (See 1991 enactment of chapter 2A.) Fire Supply & Serv., Inc. v. Chico Hot Springs, 196 M 435, 639 P2d 1160, 39 St. Rep. 231 (1982).

Foreclosure of Mortgage Securing Note — Payment to Holder Required: The Dahls executed a note to Sythe and also executed a real estate mortgage in Sythe's favor. The note was placed in an escrow account in the Culbertson State Bank, and the bank was designated as the place where payment was to be made. Sythe assigned the note to the bank as security for a note obtained by him. Sythe later gave the bank a written assignment of the mortgage. Defendant Dahl was given written notice of this assignment. The bank did not receive any payments from Sythe on his notes or from Dahl on the note assigned to the bank. The bank brought an action for the foreclosure of the mortgage against Dahl. Dahl contended that the note was discharged because it was paid in full, with payments being made to Sythe. The bank was never able to make service of process on Sythe. The bank was a "holder" of the note since it was in possession of the note endorsed by Sythe. As a holder and having produced the note, the bank was entitled to recover unless the defendant established a defense. Defendant's sole defense was that he had paid the note to Sythe. The defense of payment only discharges the maker's liability on the instrument if payment is made to the holder. Defendant never attempted to prove payment to the holder. Since the bank was the holder of the note and a valid assignee of the mortgage securing the note, it was entitled to a decree of foreclosure. Culbertson St. Bank v. Dahl, 190 M 33, 617 P2d 1295, 37 St. Rep. 1752 (1980).

Disclaimer Not Conspicuous: The disclaimer of warranties in an agreement is ineffective to exclude an implied warranty of fitness for a particular purpose since the disclaimer is in the same typeface as the rest of the contract and is not indented, underlined, or inked in a contrasting color to comply with the provision of the Code requiring conspicuousness. Transcont. Refrigeration Co. v. Figgins, 179 M 12, 585 P2d 1301 (1978).

Notice by Ordinary Mail: Plaintiff complied with the notice provisions of subsection (26) of this section when he sent notice of foreclosure sale to debtor by ordinary mail, since in Montana the receipt of mail is presumed if the procedure of the mailing is carried out in a regular manner. James Talcott, Inc. v. Reynolds, 165 M 404, 529 P2d 352 (1974).

Course of Dealing From Which Agreement Implied: Payor bank's holding and paying of one check to each of two of the plaintiff-payees were not sufficient to form "a sequence of previous conduct" under 30-1-205 necessary to establish a course of dealing from which an agreement excusing noncompliance with "midnight rule" under 30-4-302 could be implied under subsection (3) of this section. Sun River Cattle Co., Inc. v. Miners Bank of Mont., 164 M 237, 521 P2d 679 (1974).

30-1-202. Prima facie evidence by third-party documents.

Official Comment

[*Corresponding U.C.C. Section:* Section 1-307, U.C.C.]

Source: Former Section 1-202 [30-1-202, 2003 MCA].

Changes From Former Law: No changes.

1. This section supplies judicial recognition for documents that are relied upon as trustworthy by commercial parties.

2. This section is concerned only with documents that have been given a preferred status by the parties themselves who have required their procurement in the agreement, and for this reason the applicability of the section is limited to actions arising out of the contract that authorized or required the document. The list of documents is intended to be illustrative and not exclusive.

3. The provisions of this section go no further than establishing the documents in question as prima facie evidence and leave to the court the ultimate determination of the facts where the accuracy or authenticity of the documents is questioned. In this connection the section calls for a commercially reasonable interpretation.

4. Documents governed by this section need not be writings if records in another medium are generally relied upon in the context.

Case Notes

Good Faith by Lender: The gravamen of the statutory good faith requirement is whether the terms of the agreement were carried out faithfully. Although the terms of loans as negotiated prior to execution of actual notes were disputed where the lender performed according to the actual notes signed by the parties, the lender did not act in bad faith. Shiplet v. First Sec. Bank of Livingston, Inc., 234 M 166, 762 P2d 242, 45 St. Rep. 1816 (1988).

30-1-203. Obligation of good faith.

Official Comment

[*Corresponding U.C.C. Section:* Section 1-304, U.C.C.]

Source: Former Section 1-203 [30-1-203, 2003 MCA].

Changes From Former Law: Except for changing the form of reference to the Uniform Commercial Code [Title 30, chapters 1 through 9A], this section is identical to former UCC Section 1-203 [30-1-203, 2003 MCA]. A Comment will make it clear that this section applies to the exercise of rights granted by the Uniform Commercial Code [Title 30, chapters 1 through 9A].

1. This section sets forth a basic principle running throughout the Uniform Commercial Code [Title 30, chapters 1 through 9A]. The principle is that in commercial transactions good faith is required in the performance and enforcement of all agreements or duties. While this duty is explicitly stated in some provisions of the Uniform Commercial Code [Title 30, chapters 1 through 9A], the applicability of the duty is broader than merely these situations and applies generally, as stated in this section, to the performance or enforcement of every contract or duty within this Act [Title 30, chapters 1 through 9A]. It is further implemented by Section 1-303 [30-1-205] on course of dealing, course of performance, and usage of trade. This section does not support an independent cause of action for failure to perform or enforce in good faith. Rather, this section means that a failure to perform or enforce, in good faith, a specific duty or obligation under the contract, constitutes a breach of that contract or makes unavailable, under the particular circumstances, a remedial right or power. This distinction makes it clear that the doctrine of good faith merely directs a court towards interpreting contracts within the commercial context in which they are created, performed, and enforced, and does not create a separate duty of fairness and reasonableness which can be independently breached.

2. "Performance and enforcement" of contracts and duties within the Uniform Commercial Code [Title 30, chapters 1 through 9A] include the exercise of rights created by the Uniform Commercial Code [Title 30, chapters 1 through 9A].

Case Notes

No Error in Ordering Foreclosure of Personal Real Property for Failure to Repay Business Loans — Deficiency Judgment Proper: Defendants, husband and wife, failed to make scheduled payments on two bank loans, and the bank filed for foreclosure of two deeds of trust. Defendants were in the process of obtaining a divorce. The husband failed to respond to the complaint, and a default judgment was entered against him. The District Court then granted summary judgment against the wife, ordered foreclosure and sale of the collateral real property, and entered a deficiency judgment holding the wife responsible for any deficiency following sale of the real property. The wife appealed on grounds that the District Court erroneously granted summary judgment by: (1) determining that any oral representations made by bank agents were merged into written documents; (2) holding that the bank was entitled to a deficiency judgment; and (3) finding that the bank had no fiduciary duty to the wife. The Supreme Court considered each argument in turn and affirmed. First, the written loan agreements expressed the entire agreement between the parties, and any alleged oral understandings that were not reduced to writing were invalid. Second, although a deficiency judgment may not issue if the secured property is a single-family residence, in this case, the security agreements provided that the collateral property be used for business purposes, so even though the property was defendants' primary residence, the trust indenture was not strictly residential, and the District Court did not err in ordering a deficiency judgment. Third, as stated in Coles Dept. Store v. First Bank, 240 M 226, 783 P2d 932 (1989), to establish a fiduciary relationship, in addition to a long history of bank dealings, a bank must act in some capacity other than that common in the usual arm's-length debtor-creditor relationship. Here, no prior banking relationship existed between the parties, and given the wife's extensive legal and marketing background, she would not have needed to rely on the bank to interpret the loan documents for her or to act as her adviser, so no fiduciary relationship or duty existed. First Sec. Bank v. Abel, 2008 MT 161, 343 M 313, 184 P3d 318 (2008), following First St. Bank of Forsyth v. Chunkapura, 226 M 54, 734 P2d 1203 (1987), and Trustees of the Wash.-Idaho-Mont. Carpenters-Employers Retirement Trust Fund v. Galleria Partnership, 239 M 250, 780 P2d 608 (1989).

Covenant of Good Faith at Issue Only if Breach of Contract Occurs — Summary Judgment Improper: Precision Theatrical Effects (PTE), a manufacturer of explosive pyrotechnical materials, and Nickel, PTE's former owner, obtained five loans from United Banks (United), secured by cash, accounts receivable, and assets. The governing documents securing the loans provided that PTE would be in default if PTE did or failed to do anything that caused United to believe that it would have difficulty in collecting on its loans. After PTE's business was raided and Nickel was arrested for possessing and selling dangerous drugs, United froze PTE's accounts despite their current status and notified PTE and Nickel that the loans were in default. After the District Court granted summary judgment to United, PTE and Nickel appealed, alleging that United breached the implied covenant of good faith when it declared a default and froze all bank accounts. United argued that it had legitimate reasons to believe that its ability to collect on the loans had been jeopardized, and therefore, under the terms of the security agreement, PTE and Nickel were in default. The Supreme Court, in reversing the District Court ruling, held that United's belief that it would have difficulty collecting on the loans and whether it acted with honesty when it froze the accounts must be read in conjunction with its obligation to deal in good faith. The breach of duty of good faith is a question of fact not susceptible to summary judgment. Precision Theatrical Effects, Inc. v. United Banks, N.A., 2006 MT 236, 333 M 505, 143 P3d 442 (2006).

Elements of "Special Relationship" Necessary to Support Tort Claim of Bad Faith: The essential elements of a special relationship necessary to support a tort claim of bad faith, as set out in Wallis v. Kroehler Mfg. Co., 207 Cal. Rep. 123 (1984), are: (1) the contract must be such that the parties are in inherently unequal bargaining positions; (2) the motivation for entering the contract must be a nonprofit motivation (i.e., to secure peace of mind, security, or future protection); (3) ordinary contract damages are not adequate because they do not require the party in the superior position to account for its actions and they do not make the inferior party whole; (4) one party is especially vulnerable because of the type of harm it may suffer and of necessity places trust in the other party to perform; and (5) the other party is aware of this vulnerability. If substantial evidence is not presented in support of each and all of the elements, the court shall direct that there is no special relationship. Simmons Oil Corp. v. Holly Corp., 258 M 79, 852 P2d 523, 50 St. Rep. 433 (1993). See also Story v. Bozeman, 242 M 436, 791 P2d 767 (1990), and Warrington v. Great Falls Clinic, LLP, 2019 MT 111, 395 Mont. 432, 443 P.3d 369. These elements were applied in Stephens v. Safeco Ins. Co. of America, 258 M 142, 852 P2d 565, 50 St. Rep. 467 (1993).

Tort of Bad Faith — Not Available for Most Contract Actions — Breach: In a contract action, the Supreme Court ruled that a breach of the implied covenant of good faith and fair dealing constituted a breach of the contract and that only contract damages would be available to the prevailing party. The court stated that tort-type damages would not be available for a breach of the covenant. The court also held that the tort of bad faith would apply only in exceptional circumstances to discourage oppression in contracts that necessarily give one party a superior position. Every contract, regardless of the type, contains an implied covenant of good faith and fair dealing. A breach of the covenant is a breach of the contract. Story v. Bozeman, 242 M 436, 791 P2d 767, 47 St. Rep. 850 (1990), followed in Keller v. Dooling, 248 M 535, 813 P2d 437, 48 St. Rep. 554 (1991), in McNeil v. Currie, 253 M 9, 830 P2d 1241, 49 St. Rep. 312 (1992), and Kneeland v. Luzenac America, Inc., 1998 MT 136, 289 M 201, 961 P2d 725, 55 St. Rep. 541 (1998).

Bank's "Action Plan" for Liquidation of Borrower's Business Not Breach of Obligation of Good Faith and Fair Dealing: The plaintiffs owned a department store that had received interim financing over the years from the bank. The business had been losing money for several years, and the bank informed the plaintiffs that it probably would not continue to provide the necessary financing. The plaintiffs thereafter liquidated their business and after it was sold learned that the bank had not disclosed to them that the bank had an "action plan" advocating the liquidation of the plaintiffs' business in order to ensure that the bank's loans be repaid. The Supreme Court held that the bank had never acted as a financial adviser to the plaintiffs. Therefore, no fiduciary duty existed. No contractual obligation existed requiring the bank to continue to loan money. The bank's failure to disclose its "action plan" was not a breach of the statutory obligation of good faith and fair dealing. Coles Dept. Store v. First Bank, 240 M 226, 783 P2d 932, 46 St. Rep. 2075 (1989).

Bank's Failure to Make Additional Loans Not Bad Faith: The bank had made a series of loans to the plaintiffs for their farming operation. Each loan was secured by a promissory note. The plaintiffs claimed that they had a reasonable expectation that the bank would continue to provide the necessary funds, and its failure to do so constituted bad faith. The Supreme Court ruled that no statutory or common-law duty existed that obligated the bank to continue to make loans to the plaintiffs; therefore, the bank's actions could not be characterized as arbitrary, capricious, or unreasonable, a showing of which is necessary to prove a breach of the covenant of good faith. Blome v. First Nat'l Bank of Miles City, 238 M 181, 776 P2d 525, 46 St. Rep. 1186 (1989).

Good Faith by Lender: The gravamen of the statutory good faith requirement is whether the terms of the agreement were carried out faithfully. Although the terms of loans as negotiated prior to execution of actual notes were disputed where the lender performed according to the actual notes signed by the parties, the lender did not act in bad faith. Shiplet v. First Sec. Bank of Livingston, Inc., 234 M 166, 762 P2d 242, 45 St. Rep. 1816 (1988).

Breach of Good Faith Obligation — Punitive Damages: A breach of the obligation of good faith imposed by this section, in and of itself, is not sufficient to support an award of punitive damages. There must be some oppressive, malicious, or fraudulent conduct, beyond a breach of the statutory good faith obligation, to support an award of punitive damages. This statement of dictum was made by the court in holding that the plaintiff bank properly foreclosed on a mortgage on real property pledged as collateral for business loans after the bank had refused to extend the note unless the principal balance was reduced substantially. Cent. Bank of Mont. v. Eystad, 219 M 69, 710 P2d 710, 42 St. Rep. 1850 (1985).

Lender's Failure to Honor Renegotiated Loan Payments: Bank's employee, Johnson, told defendants that their note with the bank would be renegotiated to allow further time for payment. Another employee then refused to renegotiate, and he offset defendants' checking account balance against the note without telling defendants, after defendants told him they had relied on Johnson and would not be able to pay on the note's due date. Several of defendants' checks were then dishonored due to insufficient funds. If a duty to exercise good faith is imposed by law rather than by a contract, breach of the duty is tortious and punitive damages are thus recoverable if the conduct is sufficiently culpable. Here, punitive damages could have been granted on the basis of malice, fraud, oppression, or all three, and a new trial was granted because the judge refused to submit the punitive damages issue to the jury. First Nat'l Bank of Libby v. Twombly, 213 M 66, 689 P2d 1226, 41 St. Rep. 1948 (1984). See also Bottrell v. Am. Bank, 237 M 1, 773 P2d 694, 46 St. Rep. 561 (1989).

Estoppel to Prevent Application of Statute of Frauds: In a contract action brought by the plaintiff buyer of seed potatoes against the seller, in which the evidence showed that the defendant had never signed a written contract for the potatoes, but by his active and passive conduct induced the plaintiff to change his position by agreeing to sell the potatoes that were the subject of the contract to other buyers, the Supreme Court held that the plaintiff had proved the elements of estoppel by silence or equitable estoppel and that the defendant would therefore be estopped in applying the Statute of Frauds to the oral contract. NW. Potato Sales, Inc. v. Beck, 208 M 310, 678 P2d 1138, 41 St. Rep. 362 (1984), followed, with regard to elements of estoppel, in CB&F Dev. Corp. v. Culbertson St. Bank, 256 M 1, 844 P2d 5, 49 St. Rep. 1122 (1992).

Good Faith Belief That Security Interest Impaired by Breach: Where security agreement between debtor and creditor provided that if debtor leased airplane without consent of creditor, creditor could, at its option, accelerate full payment of loan, where debtor leased airplane to plaintiffs and where creditor eventually repossessed airplane and sold it, plaintiffs were entitled to examination of fairness of acceleration. Trial court's failure to instruct jury that acceleration could only be done if creditor believed in good faith that his security interest was impaired by breach of security agreement was prejudicial error and warranted new trial of plaintiffs' conversion action. Brown v. AVEMCO Inv. Corp. 603 F2d 1367 (9th Cir. 1979).

30-1-204. Reasonable time — seasonableness.

Official Comment

[*Corresponding U.C.C. Section:* Section 1-205, U.C.C.]

Source: Former Section 1-204(2)-(3) [30-1-204(2 and (3), 2003 MCA].

Changes From Former Law: This section is derived from subsections (2) and (3) of former Section 1-204 [30-1-204(2 and (3), 2003 MCA]. Subsection (1) of that section [30-1-204(1)] is now incorporated in Section 1-302(b) [30-1-302(2)].

1. Subsection (a) [subsection (1)] makes it clear that requirements that actions be taken within a "reasonable" time are to be applied in the transactional context of the particular action.

2. Under subsection (b) [subsection (2)], the agreement that fixes the time need not be part of the main agreement, but may occur separately. Notice also that under the definition of "agreement" (Section 1-201) [30-1-201] the circumstances of the transaction, including course of dealing or usages of trade or course of performance may be material. On the question what is a reasonable time these matters will often be important.

Compiler's Comments

2005 Amendment: Chapter 575 in catchline at beginning deleted "Time" and at end substituted "seasonableness" for "seasonably"; in (1) at beginning inserted "Whether a time for taking an action required by", after "code" deleted "requires any action to be taken within a reasonable time, any time which is not manifestly unreasonable may be fixed by agreement. (2) What", and after "reasonable" deleted "time for taking any action"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-1-205. Course of performance, course of dealing, and usage of trade.

Official Comment

[*Corresponding U.C.C. Section:* Section 1-303, U.C.C.]

Source: Former Section 1-205, former Section 1-208, and Section 2A-207 [30-1-205, 30-1-208, and 30-2A-207, 2003 MCA].

Changes From Former Law: This section integrates the "course of performance" concept from Articles 2 [Title 30, chapter 2] and 2A [Title 30, chapter 2A] into the principles of former Section 1-205 [30-1-205, 2003 MCA], which deals with course of dealing and usage of trade. In so doing, the section slightly modifies the articulation of the course of performance rules to fit more comfortably with the approach and structure of former UCC Section 1-205 [30-1-205, 2003 MCA]. There are also slight modifications to be more consistent with the definition of "agreement" in former Section 1-201(3) [30-1-201(3), 2003 MCA]. It should be noted that a course of performance that might otherwise establish a defense to the obligation of a party to a negotiable instrument is not available as a defense against a holder in due course who took the instrument without notice of that course of performance.

1. The Uniform Commercial Code [Title 30, chapters 1 through 9A] rejects both the "lay-dictionary" and the "conveyancer's" reading of a commercial agreement. Instead the meaning of the agreement of the parties is to be determined by the language used by them and by their action, read and interpreted in the light of commercial practices and other surrounding circumstances. The measure and background for interpretation are set by the commercial context, which may explain and supplement even the language of a formal or final writing.

2. "Course of dealing," as defined in subsection (b) [subsection (2)], is restricted, literally, to a sequence of conduct between the parties previous to the agreement. A sequence of conduct after or under the agreement, however, is a "course of performance." "Course of dealing" may enter the agreement either by explicit provisions of the agreement or by tacit recognition.

3. The Uniform Commercial Code [Title 30, chapters 1 through 9A] deals with "usage of trade" as a factor in reaching the commercial meaning of the agreement that the parties have made. The language used is to be interpreted as meaning what it may fairly be expected to mean to parties involved in the particular commercial transaction in a given locality or in a given vocation or trade. By adopting in this context the term "usage of trade," the Uniform Commercial Code

[Title 30, chapters 1 through 9A] expresses its intent to reject those cases which see evidence of "custom" as representing an effort to displace or negate "established rules of law." A distinction is to be drawn between mandatory rules of law such as the Statute of Frauds provisions of Article 2 on Sales [Title 30, chapter 2] whose very office is to control and restrict the actions of the parties, and which cannot be abrogated by agreement, or by a usage of trade, and those rules of law (such as those in Part 3 of Article 2 on Sales) [Title 30, chapter 2, part 3] which fill in points which the parties have not considered and in fact agreed upon. The latter rules hold "unless otherwise agreed" but yield to the contrary agreement of the parties. Part of the agreement of the parties to which such rules yield is to be sought for in the usages of trade which furnish the background and give particular meaning to the language used, and are the framework of common understanding controlling any general rules of law which hold only when there is no such understanding.

4. A usage of trade under subsection (c) [subsection (3)] must have the "regularity of observance" specified. The ancient English tests for "custom" are abandoned in this connection. Therefore, it is not required that a usage of trade be "ancient or immemorial," "universal," or the like. Under the requirement of subsection (c) [subsection (3)] full recognition is thus available for new usages and for usages currently observed by the great majority of decent dealers, even though dissidents ready to cut corners do not agree. There is room also for proper recognition of usage agreed upon by merchants in trade codes.

5. The policies of the Uniform Commercial Code [Title 30, chapters 1 through 9A] controlling explicit unconscionable contracts and clauses (Sections 1-304, 2-302) [30-1-203, 30-2-302] apply to implicit clauses that rest on usage of trade and carry forward the policy underlying the ancient requirement that a custom or usage must be "reasonable." However, the emphasis is shifted. The very fact of commercial acceptance makes out a *prima facie* case that the usage is reasonable, and the burden is no longer on the usage to establish itself as being reasonable. But the anciently established policing of usage by the courts is continued to the extent necessary to cope with the situation arising if an unconscionable or dishonest practice should become standard.

6. Subsection (d) [subsection (4)], giving the prescribed effect to usages of which the parties "are or should be aware," reinforces the provision of subsection (c) [subsection (3)] requiring not universality but only the described "regularity of observance" of the practice or method. This subsection also reinforces the point of subsection (c) [subsection (3)] that such usages may be either general to trade or particular to a special branch of trade.

7. Although the definition of "agreement" in Section 1-201 [30-1-201] includes the elements of course of performance, course of dealing, and usage of trade, the fact that express reference is made in some sections to those elements is not to be construed as carrying a contrary intent or implication elsewhere. Compare Section 1-302(c) [30-1-302(3)].

8. In cases of a well established line of usage varying from the general rules of the Uniform Commercial Code [Title 30, chapters 1 through 9A] where the precise amount of the variation has not been worked out into a single standard, the party relying on the usage is entitled, in any event, to the minimum variation demonstrated. The whole is not to be disregarded because no particular line of detail has been established. In case a dominant pattern has been fairly evidenced, the party relying on the usage is entitled under this section to go to the trier of fact on the question of whether such dominant pattern has been incorporated into the agreement.

9. Subsection (g) [subsection (7)] is intended to insure that this Act's [Title 30, chapters 1 through 9A] liberal recognition of the needs of commerce in regard to usage of trade shall not be made into an instrument of abuse.

Compiler's Comments

2005 Amendment: Chapter 575 in catchline inserted "performance, course of"; inserted (1) relating to course of performance; in (2) substituted "conduct concerning previous transactions" for "previous conduct"; in (3) in last sentence near beginning after "embodied in a" deleted "written", after "similar" substituted "record" for "writing", and at end substituted "record is a question of law" for "writing is for the court"; in (4) in first sentence near beginning inserted "course of performance or" and at end substituted "is relevant in ascertaining the meaning of the parties' agreement and may supplement or qualify the terms of the agreement" for "give particular meaning to and supplement or qualify terms of an agreement" and inserted second sentence relating to usage of trade; in (5) in first sentence at beginning inserted exception clause and near middle substituted "any applicable course of performance" for "an applicable"; in (5)(a) substituted "prevail over course of performance" for "control both"; inserted (5)(b) relating to course of performance prevailing over course of dealing and usage of trade; in (6) substituted "Subject to 30-2-209, a course of performance is relevant to show a waiver or modification of any term inconsistent with the course" for "An applicable usage of trade in the place where any part of performance is to occur shall be used in interpreting the agreement as to that part"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

Case Notes

Terms of Price — Custom and Trade Usage at Variance With Contract: Where plaintiff and defendant entered into a written contract under which defendant was to purchase approximately 45 truckloads of crushed auto bodies from the plaintiff for $25 a net ton, the defendant would not be heard to contend that custom and usage in the crushed auto body business should allow him to pass along a price decrease from his purchaser to the plaintiff. The custom and usage alleged by the defendant could not have been as widespread and used with the regularity defendant contended or it would have been stated in the contract. It would be unreasonable for the court to negate the explicit terms of the contract. Weissman & Sons, Inc. v. Pepper, 480 F. Supp. 1364 (D.C. Mont. 1979).

Course of Dealing: Payor bank's holding and paying of one check to each of two of the plaintiff-payees were not sufficient to form "a sequence of previous conduct" necessary to establish a course of dealing from which an agreement excusing noncompliance with "midnight rule" under 30-4-302 could be implied under 30-1-201. Sun River Cattle Co., Inc. v. Miners Bank of Mont., 164 M 237, 521 P2d 679 (1974).

30-1-207. Performance or acceptance under reservation of rights.

Official Comment

[*Corresponding U.C.C. Section:* Section 1-308, U.C.C.]

Source: Former Section 1-207 [30-1-207, 2003 MCA].

Changes From Former Law: This section is identical to former UCC Section 1-207 [30-1-207, 2003 MCA].

1. This section provides machinery for the continuation of performance along the lines contemplated by the contract despite a pending dispute, by adopting the mercantile device of going ahead with delivery, acceptance, or payment "without prejudice," "under protest," "under reserve," "with reservation of all our rights," and the like. All of these phrases completely reserve all rights within the meaning of this section. The section therefore contemplates that limited as well as general reservations and acceptance by a party may be made "subject to satisfaction of our purchaser," "subject to acceptance by our customers," or the like.

2. This section does not add any new requirement of language of reservation where not already required by law, but merely provides a specific measure on which a party can rely as that party makes or concurs in any interim adjustment in the course of performance. It does not affect or impair the provisions of this Act [Title 30, chapters 1 through 9A] such as those under which the buyer's remedies for defect survive acceptance without being expressly claimed if notice of the defects is given within a reasonable time. Nor does it disturb the policy of those cases which restrict the effect of a waiver of a defect to reasonable limits under the circumstances, even though no such reservation is expressed.

The section is not addressed to the creation or loss of remedies in the ordinary course of performance but rather to a method of procedure where one party is claiming as of right something which the other believes to be unwarranted.

3. Subsection (b) [subsection (2)] states that this section does not apply to an accord and satisfaction. Section 3-311 [30-3-311] governs if an accord and satisfaction is attempted by tender of a negotiable instrument as stated in that section. If Section 3-311 [30-3-311] does not apply, the issue of whether an accord and satisfaction has been effected is determined by the law of contract. Whether or not Section 3-311 [30-3-311] applies, this section has no application to an accord and satisfaction.

Compiler's Comments

1991 Amendment: Inserted (2) concerning nonapplicability to accord and satisfaction; and made minor changes in style.

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

30-1-208. Option to accelerate at will.

Official Comment

[*Corresponding U.C.C. Section:* Section 1-309, U.C.C.]

Source: Former Section 1-208 [30-1-208, 2003 MCA].

Changes From Former Law: Except for minor stylistic changes, this section is identical to former UCC Section 1-208 [30-1-208, 2003 MCA].

1. The common use of acceleration clauses in many transactions governed by the Uniform Commercial Code [Title 30, chapters 1 through 9A], including sales of goods on credit, notes payable at a definite time, and secured transactions, raises an issue as to the effect to be given to a clause that seemingly grants the power to accelerate at the whim and caprice of one party. This section is intended to make clear that despite language that might be so construed and which further might be held to make the agreement void as against public policy or to make the contract illusory or too indefinite for enforcement, the option is to be exercised only in the good faith belief that the prospect of payment or performance is impaired.

Obviously this section has no application to demand instruments or obligations whose very nature permits call at any time with or without reason. This section applies only to an obligation of payment or performance which in the first instance is due at a future date.

Compiler's Comments

2005 Amendment: Chapter 575 near middle of first sentence substituted "means that the party has" for "shall be construed to mean that he shall have"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

Case Notes

Covenant of Good Faith at Issue Only if Breach of Contract Occurs — Summary Judgment Improper: Precision Theatrical Effects (PTE), a manufacturer of explosive pyrotechnical materials, and Nickel, PTE's former owner, obtained five loans from United Banks (United), secured by cash, accounts receivable, and assets. The governing documents securing the loans provided that PTE would be in default if PTE did or failed to do anything that caused United to believe that it would have difficulty in collecting on its loans. After PTE's business was raided and Nickel was arrested for possessing and selling dangerous drugs, United froze PTE's accounts despite their current status and notified PTE and Nickel that the loans were in default. After the District Court granted summary judgment to United, PTE and Nickel appealed, alleging that United breached the implied covenant of good faith when it declared a default and froze all bank accounts. United argued that it had legitimate reasons to believe that its ability to collect on the loans had been jeopardized, and therefore, under the terms of the security agreement, PTE and Nickel were in default. The Supreme Court, in reversing the District Court ruling, held that United's belief that it would have difficulty collecting on the loans and whether it acted with honesty when it froze the accounts must be read in conjunction with its obligation to deal in good faith. The breach of duty of good faith is a question of fact not susceptible to summary judgment. Precision Theatrical Effects, Inc. v. United Banks, N.A., 2006 MT 236, 333 M 505, 143 P3d 442 (2006).

Common-Law Right to Setoff Clarified: The right of setoff exists between any mutual debtors and creditors where the debts have matured and the parties mutually are debtors and creditors of and to each other. It is a general rule that when a depositor is indebted to a bank and the debts are mutual, the bank may apply deposits to a payment of the debt due it by the depositor, provided there is no express agreement to the contrary and the deposit is not specifically applicable to some other purpose. For a bank to establish the right to setoff, the fund to be set off must be owed by the bank to the debtor, the fund must be deposited without restrictions, and the existing indebtedness must be due and owing. Victor Werlhof Aviation Ins. v. Farmers St. Bank, 237 M 51, 771 P2d 962, 46 St. Rep. 613 (1989). See also Sec. St. Bank v. First Nat'l Bank, 78 M 389, 254 P 417 (1927).

Setoff at Time of Presentation of Writ of Execution: A judgment creditor claimed that because a bank took no action to exercise its right of setoff before a writ of execution was presented, the writ took precedence over the setoff. However, the bank acquired a right to setoff at the time payment became delinquent but chose instead to perform the setoff when presented with the writ. The judgment creditor had no greater right against the bank than did the debtor at that time, and because a judgment creditor seeking execution of a debtor's property in possession of a third party stands in the shoes of the debtor as far as the rights of the third party are concerned, the writ did not take precedence. Under these circumstances, 30-4-303 did not apply. The bank properly asserted the setoff at the time the writ was presented. Victor Werlhof Aviation Ins. v. Farmers St. Bank, 237 M 51, 771 P2d 962, 46 St. Rep. 613 (1989).

Setoff Improperly Applied Before Note Due or Default Occurs: A bank applied a setoff before any demand for payment was made or indebtedness matured under the theory of the general bank lien expressed in 71-3-1502 and the right to accelerate performance in good faith under this section. The argument was discounted by the Supreme Court, noting that the right of setoff does not arise simply from the lien and that under the long-established rule that when money is deposited in a bank to the credit of one of its debtors without an express agreement to the contrary or direction to apply to a specific purpose, the bank may apply the deposit only to satisfy past-due indebtedness. Bottrell v. Am. Bank, 237 M 1, 773 P2d 694, 46 St. Rep. 561 (1989), following Sec. St. Bank v. First Nat'l Bank, 78 M 389, 254 P 417 (1927).

Lender's Failure to Honor Renegotiated Loan Payments: Bank's employee, Johnson, told defendants that their note with the bank would be renegotiated to allow further time for payment. Another employee then refused to renegotiate, and he offset defendants' checking account balance against the note without telling defendants, after defendants told him they had relied on Johnson and would not be able to pay on the note's due date. Several of defendants' checks were then dishonored due to insufficient funds. If a duty to exercise good faith is imposed by law rather than by a contract, breach of the duty is tortious and punitive damages are thus recoverable if the conduct is sufficiently culpable. Here, punitive damages could have been granted on the basis of malice, fraud, oppression, or all three, and a new trial was granted because the judge refused to submit the punitive damages issue to the jury. First Nat'l Bank of Libby v. Twombly, 213 M 66, 689 P2d 1226, 41 St. Rep. 1948 (1984). See also Bottrell v. Am. Bank, 237 M 1, 773 P2d 694, 46 St. Rep. 561 (1989).

Invoking Acceleration Clause of Promissory Note Upon Death of Surety: Where deceased had previously cosigned a promissory note in favor of appellant, and appellant in submitting a claim against the deceased's estate sought the allowance of the claim but not the immediate payment of the note, the appellant may not on appeal raise the issue of its right to invoke the acceleration clause of the note and seek immediate payment. In re Estate of Harbaugh, 196 M 435, 639 P2d 495, 39 St. Rep. 84 (1982).

Actions — Fairness Required: Where security agreement between debtor and creditor provided that if debtor leased airplane without consent of creditor, creditor could, at its option, accelerate full payment of loan, where debtor leased airplane to plaintiffs and where creditor eventually repossessed airplane and sold it, plaintiffs were entitled to examination of fairness of acceleration. Trial court's failure to instruct jury that acceleration could only be done if creditor believed in good faith that his security interest was impaired by breach of security agreement was prejudicial error and warranted new trial of plaintiffs' conversion action. Brown v. AVEMCO Inv. Corp. 603 F2d 1367 (9th Cir. 1979).

30-1-209. Subordinated obligations.

Official Comment

[*Corresponding U.C.C. Section:* Section 1-310, U.C.C.]

Source: Former Section 1-209 [30-1-209, 2003 MCA].

Changes From Former Law: This section is substantively identical to former Section 1-209 [30-1-209, 2003 MCA]. The language in that section stating that it "shall be construed as declaring the law as it existed prior to the enactment of this section and not as modifying it" has been deleted.

1. Billions of dollars of subordinated debt are held by the public and by institutional investors. Commonly, the subordinated debt is subordinated on issue or acquisition and is evidenced by an investment security or by a negotiable or non-negotiable note. Debt is also sometimes subordinated after it arises, either by agreement between the subordinating creditor and the debtor, by agreement between two creditors of the same debtor, or by agreement of all three parties. The subordinated creditor may be a stockholder or other "insider" interested in the

common debtor; the subordinated debt may consist of accounts or other rights to payment not evidenced by any instrument. All such cases are included in the terms "subordinated obligation," "subordination," and "subordinated creditor."

2. Subordination agreements are enforceable between the parties as contracts; and in the bankruptcy of the common debtor dividends otherwise payable to the subordinated creditor are turned over to the superior creditor. This "turn-over" practice has on occasion been explained in terms of "equitable lien," "equitable assignment," or "constructive trust," but whatever the label the practice is essentially an equitable remedy and does not mean that there is a transaction "that creates a security interest in personal property . . . by contract" or a "sale of accounts, chattel paper, payment intangibles, or promissory notes" within the meaning of Section 9-109 [30-9A-109]. On the other hand, nothing in this section prevents one creditor from assigning his rights to another creditor of the same debtor in such a way as to create a security interest within Article 9 [Title 30, chapter 9A], where the parties so intend.

3. The enforcement of subordination agreements is largely left to supplementary principles under Section 1-103 [30-1-102(1) and 30-1-103]. If the subordinated debt is evidenced by a certificated security, Section 8-202(a) [30-8-212(1)] authorizes enforcement against purchasers on terms stated or referred to on the security certificate. If the fact of subordination is noted on a negotiable instrument, a holder under Sections 3-302 [30-3-302] and 3-306 [30-3-306] is subject to the term because notice precludes him from taking free of the subordination. Sections 3-302(3)(a) [30-3-302(3)], 3-306 [30-3-306], and 8-317 [30-8-317, now repealed], severely limit the rights of levying creditors of a subordinated creditor in such cases.

Compiler's Comments

2005 Amendment: Chapter 575 in first sentence in two places substituted "performance" for "payment"; deleted third sentence that read "This section shall be construed as declaring the law as it existed prior to the enactment of this section and not as modifying it"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

Optional Provision: The note accompanying UCC § 1-209 provided: "This new section is proposed as an optional provision to make it clear that a subordination agreement does not create a security interest unless so intended."

Case Notes

Breach of Subordination Agreement — Failure to Respond — Summary Judgment Proper: After submitting evidence in support of its motion, defendant moved for summary judgment because plaintiff breached a subordination agreement. The burden shifted to plaintiff to respond, but instead of filing a response brief, plaintiff filed two depositions and a set of discovery answers at the hearing and relied on oral argument. After consideration, the District Court granted summary judgment. Plaintiff appealed, contending that summary judgment was improper because the depositions and discovery answers proved the existence of an intercreditor agreement between defendant and a codefendant, establishing a question of fact whether defendant received all funds to which it was entitled and thus whether defendant had any claim against plaintiff. The Supreme Court disagreed. Breach of the subordination agreement occurred before the intercreditor agreement existed, so the facts presented by plaintiff did not establish a material fact regarding the subordination agreement, and summary judgment was appropriate. Mtn. W. Bank v. Mine & Mill Hydraulics, Inc., 2003 MT 35, 314 M 248, 64 P3d 1048 (2003).

30-1-210. Notice — knowledge.

Official Comments

[*Corresponding U.C.C. Section:* Section 1-202, U.C.C.]

Source: Derived from former Section 1-201(25)-(27) [30-1-201(25) through (27), 2003 MCA].

Changes From Former Law: These provisions are substantive rather than purely definitional. Accordingly, they have been relocated from Section 1-201 [30-1-201, 2003 MCA] to this section.

1. Under subsection (a) [subsection (1)], a person has notice when, *inter alia,* the person has received a notification of the fact in question. The subsection leaves open the time and

circumstances under which notice or notification may cease to be effective. Therefore such cases as *Graham v. White-Phillips Co.*, 296 U.S. 27, 56 S.Ct. 21, 80 L.Ed. 20 (1935), are not overruled.

2. As shown in subsection (d) [subsection (4)], the word "notifies" is used when the essential fact is the proper dispatch of the notice, not its receipt. Compare "Send." When the essential fact is the other party's receipt of the notice, that is stated. Subsection (e) [subsection (5)] states when a notification is received.

3. Subsection (f) [subsection (6)] makes clear that reason to know, knowledge, or a notification, although "received" for instance by a clerk in Department A of an organization, is effective for a transaction conducted in Department B only from the time when it was or should have been communicated to the individual conducting that transaction.

Compiler's Comments

Effective Date: This section is effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-1-211. Lease distinguished from security interest.

Official Comments

[*Corresponding U.C.C. Section:* Section 1-203, U.C.C.]

Source: Former Section 1-201(37) [30-1-201(37), 2003 MCA].

Changes From Former Law: This section is substantively identical to those portions of former UCC Section 1-201(37) [30-1-201(37), 2003 MCA] that distinguished "true" leases from security interests, except that the definition of "present value" formerly embedded in Section 1-201(37) [30-1-201(37), 2003 MCA] has been placed in UCC Section 1-201(30a) [not adopted].

1. An interest in personal property or fixtures which secures payment or performance of an obligation is a "security interest." See Section 1-201(37) [30-1-201(37), 2003 MCA]. Security interests are sometimes created by transactions in the form of leases. Because it can be difficult to distinguish leases that create security interests from those that do not, this section provides rules that govern the determination of whether a transaction in the form of a lease creates a security interest.

2. One of the reasons it was decided to codify the law with respect to leases was to resolve an issue that created considerable confusion in the courts: what is a lease? The confusion existed, in part, due to the last two sentences of the definition of security interest in the 1978 Official Text of the Act, Section 1-201(37) [30-1-201(37), 2003 MCA]. The confusion was compounded by the rather considerable change in the federal, state and local tax laws and accounting rules as they relate to leases of goods. The answer is important because the definition of lease determines not only the rights and remedies of the parties to the lease but also those of third parties. If a transaction creates a lease and not a security interest, the lessee's interest in the goods is limited to its leasehold estate; the residual interest in the goods belongs to the lessor. This has significant implications to the lessee's creditors. "On common law theory, the lessor, since he has not parted with title, is entitled to full protection against the lessee's creditors and trustee in bankruptcy . . . ." 1 G. Gilmore, *Security Interests in Personal Property* § 3.6, at 76 (1965).

Under pre-UCC chattel security law there was generally no requirement that the lessor file the lease, a financing statement, or the like, to enforce the lease agreement against the lessee or any third party; the Article on Secured Transactions (Article 9) [Title 30, chapter 9A] did not change the common law in that respect. Coogan, Leasing and the Uniform Commercial Code, in *Equipment Leasing—Leveraged Leasing* 681, 700 n.25, 729 n.80 (2d ed.1980). The Article on Leases (Article 2A) [Title 30, chapter 2A] did not change the law in that respect, except for leases of fixtures. Section 2A-309 [30-2A-309]. An examination of the common law will not provide an adequate answer to the question of what is a lease. The definition of security interest in Section 1-201(37) [30-1-201(37), 2003 MCA] of the 1978 Official Text of the Act provided that the Article on Secured Transactions (Article 9) [Title 30, chapter 9A] governs security interests disguised as leases, *i.e.*, leases intended as security; however, the definition became vague and outmoded.

Lease is defined in Article 2A [Title 30, chapter 2A] as a transfer of the right to possession and use of goods for a term, in return for consideration. Section 2A-103(1)(j) [30-2A-103(1)(j)].

The definition continues by stating that the retention or creation of a security interest is not a lease. Thus, the task of sharpening the line between true leases and security interests disguised as leases continues to be a function of this Article [Title 30, chapter 1].

This section begins where Section 1-201(37) [30-1-201(37), 2003 MCA] leaves off. It draws a sharper line between leases and security interests disguised as leases to create greater certainty in commercial transactions.

Prior to enactment of the rules in this section, the 1978 text of Section 1-201(37) [30-1-201(37), 2003 MCA] provided that whether a lease was intended as security (*i.e.*, a security interest disguised as a lease) was to be determined from the facts of each case; however, (a) the inclusion of an option to purchase did not itself make the lease one intended for security, and (b) an agreement that upon compliance with the terms of the lease the lessee would become, or had the option to become, the owner of the property for no additional consideration, or for a nominal consideration, did make the lease one intended for security.

Reference to the intent of the parties to create a lease or security interest led to unfortunate results. In discovering intent, courts relied upon factors that were thought to be more consistent with sales or loans than leases. Most of these criteria, however, were as applicable to true leases as to security interests. Examples include the typical net lease provisions, a purported lessor's lack of storage facilities or its character as a financing party rather than a dealer in goods. Accordingly, this section contains no reference to the parties' intent.

Subsections (a) and (b) [subsections (1) and (2)] are taken from Section 1(2) of the Uniform Conditional Sales Act (act withdrawn 1943), modified to reflect current leasing practice. Thus, reference to the case law prior to this Act will provide a useful source of precedent. Gilmore, *Security Law, Formalism and Article 9*, 47 Neb.L.Rev. 659, 671 (1968). Whether a transaction creates a lease or a security interest continues to be determined by the facts of each case. Subsection (b) [subsection (2)] further provides that a transaction creates a security interest if the lessee has an obligation to continue paying consideration for the term of the lease, if the obligation is not terminable by the lessee (thus correcting early statutory gloss, *e.g.*, *In re Royer's Bakery, Inc.*, 1 U.C.C. Rep.Serv. (Callaghan) 342 (Bankr.E.D.Pa.1963)) and if one of four additional tests is met. The first of these four tests, subparagraph (1) [subsection (2)(a)], is that the original lease term is equal to or greater than the remaining economic life of the goods. The second of these tests, subparagraph (2) [subsection (2)(b)], is that the lessee is either bound to renew the lease for the remaining economic life of the goods or to become the owner of the goods. *In re Gehrke Enters.*, 1 Bankr. 647, 651-52 (Bankr.W.D.Wis.1979). The third of these tests, subparagraph (3) [subsection (2)(c)], is whether the lessee has an option to renew the lease for the remaining economic life or the goods for no additional consideration or for nominal additional consideration, which is defined later in this section. *In re Celeryvale Transp.*, 44 Bankr. 1007, 1014-15 (Bankr.E.D.Tenn.1984). The fourth of these tests, subparagraph (4) [subsection (2)(d)], is whether the lessee has an option to become the owner of the goods for no additional consideration or for nominal additional consideration. All of these tests focus on economics, not the intent of the parties. *In re Berge*, 32 Bankr. 370, 371-73 (Bankr.W.D.Wis.1983).

The focus on economics is reinforced by subsection (c) [subsection (3)]. It states that a transaction does not create a security interest merely because the transaction has certain characteristics listed therein. Subparagraph (1) [subsection (3)(a)] has no statutory derivative; it states that a full payout lease does not *per se* create a security interest. *Rushton v. Shea*, 419 F.Supp. 1349, 1365 (D.Del.1976). Subparagraph (2) [subsection (3)(b)] provides the same regarding the provisions of the typical net lease. *Compare All-States Leasing Co. v. Ochs*, 42 Or.App. 319, 600 P.2d 899 (Ct. App.1979) *with In re Tillery*, 571 F.2d 1361 (5th Cir.1978). Subparagraph (3) [subsection (3)(c)] restates and expands the provisions of former Section 1-201(37) [30-1-201(37), 2003 MCA] to make clear that the option can be to buy or renew. Subparagraphs (4) and (5) [subsections (3)(d) and (3)(e)] treat fixed price options and provide that fair market value must be determined at the time the transaction is entered into. *Compare Arnold Mach. Co. v. Balls*, 624 P.2d 678 (Utah 1981), *with Aoki v. Shepherd Mach. Co.*, 665 F.2d 941 (9th Cir.1982).

The relationship of subsection (b) [subsection (2)] to subsection (c) [subsection (3)] deserves to be explored. The fixed price purchase option provides a useful example. A fixed price purchase option in a lease does not of itself create a security interest. This is particularly true if the fixed price is equal to or greater than the reasonably predictable fair market value of the goods at the time the option is to be performed. A security interest is created only if the option price is nominal and the conditions stated in the introduction to the second paragraph of this subsection are met. There is a set of purchase options whose fixed price is less than fair market value but greater than nominal that must be determined on the facts of each case to ascertain whether the transaction in which the option is included creates a lease or a security interest.

It was possible to provide for various other permutations and combinations with respect to options to purchase and renew. For example, this section could have stated a rule to govern the facts of *In re Marhoefer Packing Co.*, 674 F.2d 1139 (7th Cir.1982). This was not done because it would unnecessarily complicate the definition. Further development of this rule is left to the courts.

Subsections (d) [subsections (4)(a) and (4)(b)] and (e) [subsection (4)(c)] provide definitions and rules of construction.

Compiler's Comments

Effective Date: This section is effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-1-212. Value.

Official Comments

[*Corresponding U.C.C. Section:* Section 1-204, U.C.C.]

Source: Former Section 1-201(44) [30-1-201(44), 2003 MCA].

Changes From Former Law: Unchanged from former Section 1-201 [30-1-201(44), 2003 MCA], which was derived from Sections 25, 26, 27, 191, Uniform Negotiable Instruments Law; Section 76, Uniform Sales Act; Section 53, Uniform Bills of Lading Act; Section 58, Uniform Warehouse Receipts Act; Section 22(1), Uniform Stock Transfer Act; Section 1, Uniform Trust Receipts Act. These provisions are substantive rather than purely definitional. Accordingly, they have been relocated from former Section 1-201 [30-1-201(44), MCA] to this section.

1. All the Uniform Acts in the commercial law field (except the Uniform Conditional Sales Act) have carried definitions of "value." All those definitions provided that value was any consideration sufficient to support a simple contract, including the taking of property in satisfaction of or as security for a pre-existing claim. Subsections (1), (2), and (4) in substance continue the definitions of "value" in the earlier acts. Subsection (3) makes explicit that "value" is also given in a third situation: where a buyer by taking delivery under a pre-existing contract converts a contingent into a fixed obligation.

This definition is not applicable to Articles 3 and 4 [Title 30, chapters 3 and 4], but the express inclusion of immediately available credit as value follows the separate definitions in those Articles. See Sections 4-208, 4-209, 3-303 [30-4-215, 30-4-216, 30-3-303]. A bank or other financing agency which in good faith makes advances against property held as collateral becomes a bona fide purchaser of that property even though provision may be made for charge-back in case of trouble. Checking credit is "immediately available" within the meaning of this section if the bank would be subject to an action for slander of credit in case checks drawn against the credit were dishonored, and when a charge-back is not discretionary with the bank, but may only be made when difficulties in collection arise in connection with the specific transaction involved.

Compiler's Comments

Effective Date: This section is effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

Part 3
Territorial Applicability

Part Compiler's Comments

Effective Date: This part is effective October 1, 2005.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-1-301. Territorial applicability — parties power to choose applicable law.

Official Comments

[*Corresponding U.C.C. Section:* Section 1-301, U.C.C.]

Source: Former Section 1-105 [30-1-105, 2003 MCA]. [Montana substantially revised the uniform section and the Montana version more closely resembles the versions adopted in Minnesota and Idaho.]

Changes From Former Law: Section 1-301 [30-1-301], which replaces former UCC Section 1-105 [30-1-105, 2003 MCA], represents a significant rethinking of choice of law issues addressed in that section. The new section reexamines both the power of parties to select the jurisdiction whose law will govern their transaction and the determination of the governing law in the absence of such selection by the parties. With respect to the power to select governing law, the draft affords greater party autonomy than former Section 1-105 [30-1-105, 2003 MCA], but with important safeguards protecting consumer interests and fundamental policies. While the Drafting Committee considered addressing the related topic of forum selection clauses, it ultimately decided that Article 1 of the Uniform Commercial Code [Title 30, chapter 1] is not an appropriate vehicle for addressing this issue.

Revised UCC Section 1-301 [30-1-301] addresses contractual designation of governing law somewhat differently than does former Section 1-105 [30-1-105, 2003 MCA]. Former law allows the parties to any transaction to designate a jurisdiction whose law governs if the transaction bears a "reasonable relation" to that jurisdiction. Revised Article 1 [Title 30, chapter 1] deviates from this unified approach by providing different rules for consumer transactions than for "business to business" transactions.

In the context of consumer transactions, revised Article 1 [Title 30, chapter 1], unlike former law, generally protects consumers against the possibility of losing the protection of consumer protection laws of their home jurisdiction.

In the context of business-to-business transactions, revised Article 1 [Title 30, chapter 1] generally provides the parties with greater autonomy to designate a jurisdiction whose law will govern than does former Article 1 [Title 30, chapter 1], but also provides some safeguards against abuse that do not appear in former Article 1 [Title 30, chapter 1]. Following emerging international norms, greater autonomy is provided in subsections (b) and (c) [(b) not adopted and (c) partially adopted as 30-1-301(1)] by deleting the requirement that the transaction bear a "reasonable relation" to the jurisdiction designated in this non-consumer context. It should be noted in this regard that in the case of wholly domestic transactions the jurisdiction designated must be a State. An important safeguard not present in former law is provided in subsection (e) [not adopted]. Subsection (e) [not adopted] indicates that the designation of a jurisdiction's law is not effective (even if the transaction bears a reasonable relation to that jurisdiction) to the extent that application of that law would be contrary to a fundamental policy of the jurisdiction whose law would govern in the absence of contractual designation. Application of the law designated may be contrary to a fundamental policy of the State or country whose law would otherwise govern either because of the nature of the law designated or because of the "mandatory" nature of the law that would otherwise apply.

In the absence of an effective contractual designation of governing law, former UCC Section 1-105(1) [30-1-105(1), 2003 MCA] directs the forum to apply its own law if the transaction bears "an appropriate relation to this state." This provision, however, is frequently ignored by courts. Revised UCC Section 1-301(c) [partially 30-1-301(1)] provides simply that, in the absence of contractual designation, the court should apply the forum's choice of law principles.

1. **Applicability of section.** This section is neither a full Restatement of choice of law principles nor a free-standing choice of law statute. Rather, it is a provision of Article 1 of the

Uniform Commercial Code [Title 30, chapter 1]. As such, it is subject to Section 1-102 [30-1-101(4)], which states the scope of Article 1 [Title 30, chapter 1]. As that section [30-1-101(4)] indicates, Article 1 [Title 30, chapter 1], and the rules contained therein, apply to transactions to the extent that they are governed by one of the other Articles of the Uniform Commercial Code [Title 30, chapters 2 through 5, 7, 8, and 9A]. Thus, this section does not apply to a transaction outside the scope of the Uniform Commercial Code [Title 30, chapters 1 through 9A] such as a services contract or a contract for the sale of real estate. On the other hand, if the transaction is within the scope of a substantive Article of the Uniform Commercial Code [Title 30, chapters 1 through 9A], such as in the case of a sale or lease of goods, this section does apply.

In some cases, a transaction is neither completely within the scope of the Uniform Commercial Code [Title 30, chapters 1 through 9A] (as in the case of a sale or lease of goods) nor completely outside the scope of the Uniform Commercial Code [Title 30, chapters 1 through 9A] (as in the case of a contract for the sale of real estate). Rather, some aspects of the transaction are within the substantive scope of the Uniform Commercial Code [Title 30, chapters 1 through 9A] while other aspects are not. One example of this phenomenon is an agreement to loan money in which the borrower's obligation to repay the loan is secured by a security interest in personal property. The security agreement, and the security interest created thereby, are clearly within the scope of Article 9 [Title 30, chapter 9A]. The loan agreement, on the other hand, is governed not by the Uniform Commercial Code [Title 30, chapters 1 through 9A] but by the general law of contracts. Another example is provided by a real estate lease in which the lessee's obligation to pay the stated rent is backed by a standby letter of credit issued by a bank. The lease is governed by realty law outside the Uniform Commercial Code [Title 30, chapters 1 through 9A], while the letter of credit is governed by Article 5 [Title 30, chapter 5]. While this section, by its terms, only applies to the UCC aspect of such a "mixed transaction," it is within a court's discretion to decide in a particular case that bifurcation of the choice of law principles applicable to the transaction is inadvisable and, accordingly, to apply principles of this section to the non-UCC aspects of the transaction in order to have the law of the same State or country apply to the entire transaction. When the UCC aspects of such a "mixed transaction" predominate, such a decision may be particularly appropriate.

2. **Contractual choice of law.** This section allows parties broad autonomy, with several important limitations, to select the law governing their transaction, even if the transaction does not bear a relation to the State or country whose law is selected. This recognition of party autonomy with respect to governing law has already been established in several Articles of the Uniform Commercial Code (see UCC Sections 4A-507, 5-116, and 8-110) [30-4A-507, 30-5-136, and 30-8-120] and is consistent with international norms. *See, e.g.*, Inter-American Convention on the Law Applicable to International Contracts, Article 7 (Mexico City 1994); Convention on the Law Applicable to Contracts for the International Sale of Goods, Article 7(1) (The Hague 1986); EC Convention on the Law Applicable to Contractual Obligations, Article 3(1) (Rome 1980).

There are three important limitations on this party autonomy to select governing law. First, a different, and more protective, rule applies in the context of consumer transactions (see note *c*). Second, in an entirely domestic transaction, this section does not validate the selection of foreign law. (See note *d*.) Third, contractual choice of law will not be given effect to the extent that application of the law designated would be contrary to a fundamental policy of the State or country whose law would be applied in the absence of such contractual designation (see Comment 5).

The Drafting Committee considered whether this section should expressly provide for the ability of parties to designate non-legal codes such as trade codes as the set of rules governing their transaction, but decided that the principles of Section 1-302 [30-1-302] allowing parties broad freedom of contract to structure their relation are adequate for this purpose. A similar decision was made with respect to the ability of the parties to designate recognized bodies of rules or principles applicable to commercial transactions that are promulgated by intergovernmental authorities such as UNCITRAL or UNIDROIT. *See, e.g.*, UNIDROIT Principles of International Commercial Contracts.

3. **Consumer transactions.** If one of the parties is a consumer (as defined in Section 1-201(11a)) [30-1-201(2)(l)], subsection (d) [30-1-301(2), substantially modified] provides the parties less autonomy to designate the State or country whose law will govern. First, in a consumer transaction subsection (d)(1) [30-1-301(2), substantially modified] provides that the transaction must bear a reasonable relation to the State or country designated. Second, except as noted below, subsection (d)(2) [not adopted] provides that a designation of the law of a State or country other than that of the consumer's habitual residence, even if the transaction bears a

reasonable relation to that State or country, will not deprive the consumer of the protection of any rules of law of the consumer's habitual residence which are protective of consumers and are not variable by agreement. (It should be noted that the phrase "rule of law" is intended to refer to case law as well as statutes and administrative regulations.) Thus, for example, in the case of a sale of goods by a seller in Indiana to a consumer buyer in New York, in which transaction the contract designates Indiana law as governing, the New York buyer will retain the protection of nonwaivable New York rules of law that are protective of consumers.

There is one exception to this principle. In the case of a sale of goods to a consumer in which the consumer makes the contract and takes possession of the goods in a State or country other than the consumer's habitual residence, subsection (d)(2)(B) [not adopted] provides that it is the consumer protection rules of law of that State or country that cannot be eliminated by choice of law. Thus, for example, if a New York consumer, while on vacation in Indiana, buys goods and takes delivery of them at an Indiana branch of an Ohio retailer, and the contract designates Ohio law as governing, this choice of law may not deprive the New York consumer buyer of nonwaivable Indiana rules of law that are protective of consumers, but may deprive that buyer of analogous New York rules. This exception, adapted from UCC Section 2A-106 [30-2A-106] and Article 5 of the EC Convention on the Law Applicable to Contractual Obligations, enables a seller that engages in only face-to-face transactions to ascertain in advance which consumer protection law it is subject to. The reference in subsection (d)(2)(B) [not adopted] to the State or country in which the consumer makes the contract should not be read to incorporate formalistic concepts of where the last event necessary to conclude the contract took place; rather, the intent is to identify the State in which all material steps were taken by the consumer to enter into the contract.

In the absence of a contractual designation of governing law, application of the choice of law rules of the forum, as mandated by subsection (c) [partially 30-1-301(1)], could lead to application of the laws of a State or country other than that of the consumer's habitual residence. In such a case, subsection (d)(2) [not adopted] still applies to preserve consumer protection rules for the benefit of the consumer as described in the preceding paragraph.

4. **Wholly domestic transactions.** While this section provides parties broad autonomy to select governing law, that autonomy is limited in the case of wholly domestic transactions. In a "domestic transaction," subsection (b)(1) [not adopted] validates only the designation of the law of a State. A "domestic transaction" is a transaction that does not bear a reasonable relation to a country other than the United States. See subsection (a) [not adopted]. Thus, in a wholly domestic non-consumer transaction, parties may (subject to the limitations set out in subsections (e) and (f) [not adopted]) designate the law of any State but not the law of a foreign country.

5. **International transactions.** This section provides greater autonomy in the context of international transactions. As defined in subsection (a)(2) [not adopted], a transaction is an "international transaction" if it bears a reasonable relation to a country other than the United States. In a non-consumer international transaction, subsection (b)(2) [not adopted] provides that a designation of the law of any State or country is effective (subject, of course, to the limitations set out in subsections (e) and (f) [not adopted]). It is important to note that the transaction need not bear a relation to the State or country designated so long as the transaction is international. Thus, for example, in a non-consumer lease of goods in which the lessor is located in Mexico and the lessee is located in Louisiana, a designation of the law of Ireland to govern the transaction would be given effect under this section even though the transaction may bear no relation to Ireland. The ability to designate the law of any country in non-consumer international transactions is important in light of the common practice in many commercial contexts of designating the law of a "neutral" jurisdiction whose law is well-developed.

6. **Fundamental policy.** Subsection (e) [not adopted] provides that an agreement designating the governing law will not be given effect to the extent that application of the designated law would be contrary to a fundamental policy of the State or country whose law would otherwise govern. This rule provides a narrow exception to the broad autonomy afforded to parties in subsection (b) [not adopted]. One of the prime objectives of contract law is to protect the justified expectations of the parties and to make it possible for them to foretell with accuracy what will be their rights and liabilities under the contract. In this way, certainty and predictability of result are most likely to be secured. See Restatement (Second) Conflict of Laws, § 187, comment *e*.

Under the fundamental policy doctrine, a court should not refrain from applying the designated law merely because this would lead to a result different than would be obtained under the local law of the State or country whose law would otherwise govern. Rather, the difference must be contrary to a public policy that is so substantial that it justifies overriding the concerns for certainty and predictability underlying modern commercial law as well as concerns for judicial economy generally. Thus, application of the designated law will rarely be found to be contrary to a fundamental policy of the State or country whose law would otherwise govern when the difference between the two concerns a requirement, such as a statute of frauds, that relates to formalities, or general rules of contract law, such as those concerned with the need for consideration.

The opinion of Judge Cardozo in *Loucks v. Standard Oil Co. of New York*, 120 N.E. 198 (1918), regarding the related issue of when a state court may decline to apply the law of another State, is a helpful touchstone here:

Our own scheme of legislation may be different. We may even have no legislation on the subject. That is not enough to show that public policy forbids us to enforce the foreign right. A right of action is property. If a foreign statute gives the right, the mere fact that we do not give a like right is no reason for refusing to help the plaintiff in getting what belongs to him. We are not so provincial as to say that every solution of a problem is wrong because we deal with it otherwise at home. Similarity of legislation has indeed this importance; its presence shows beyond question that the foreign statute does not offend the local policy. But its absence does not prove the contrary. It is not to be exalted into an indispensable condition. The misleading word 'comity' has been responsible for much of the trouble. It has been fertile in suggesting a discretion unregulated by general principles.

The courts are not free to refuse to enforce a foreign right at the pleasure of the judges, to suit the individual notion of expediency or fairness. They do not close their doors, unless help would violate some fundamental principle of justice, some prevalent conception of good morals, some deep-rooted tradition of the common weal. 120 N.E. at 201-02 (citations to authorities omitted).

Analytically, one might conclude that application of the designated law is contrary to a fundamental policy of the State or country whose law would otherwise govern either (i) because the substance of the designated law violates a fundamental principle of justice of that State or country or (ii) because it differs from a rule of that State or country that is "mandatory" in that it *must* be applied in the courts of that State or country without regard to otherwise-applicable choice of law rules of that State or country and without regard to whether the designated law is otherwise offensive. This distinction, which may have more theoretical than practical significance, has been suggested in some international conventions in this area, although in some cases the concept is applied to authorize the *forum* State to apply *its* mandatory rules, rather than those of the State or country whose law would otherwise govern. The latter situation is not addressed by this section. See Comment 9.

In any event, it is obvious that a rule that is freely changeable by agreement of the parties under the law of the State or country whose law would otherwise govern can hardly be construed as a mandatory rule of that State or country. This does not mean, however, that rules that cannot be changed by agreement under that law are, for that reason alone, mandatory rules. Otherwise, contractual choice of law in the UCC context would be illusory and redundant; the parties would be able to accomplish by choice of law no more than can be accomplished under Section 1-302 (by agreeing to vary the rules that would otherwise govern their transaction by substituting for those rules the rules that would apply if the transaction were governed by the designated State or country) without designation of governing law. Indeed, other than cases in which a mandatory choice of law rule is established by statute (*see, e.g.*, UCC Sections 9-301 through 9-307 [30-9A-301 through 30-9A-307], explicitly preserved in subsection (f) [not adopted]), cases in which courts have declined to follow the designated law solely because a rule of the State or country whose law would otherwise govern is mandatory are rare.

7. **Choice of law in the absence of contractual designation.** Subsection (c) [partially 30-1-301(1)], which replaces the second sentence of former UCC Section 1-105(1) [30-1-105(1), 2003 MCA], determines which jurisdiction's law governs a transaction in the absence of an effective contractual choice by the parties. Former Section 1-105(1) [30-1-105(1), 2003 MCA], provided that the law of the forum (*i.e.*, the Uniform Commercial Code) applies if the transaction bears "an appropriate relation to this state." By using an "appropriate relation" test, rather than, say, requiring that the forum be the location of the "most significant" contact, Section 1-105(1) [30-1-105(1), 2003 MCA] expressed a bias in favor of applying the forum's law. This bias, while not universally respected by the courts, was justifiable in light of the uncertainty that existed at the time of drafting as to whether the Uniform Commercial Code [Title 30, chapters 1 through 9A] would be adopted by all the States; the pro-forum bias would assure that the Uniform Commercial Code [Title 30, chapters 1 through 9A] would be applied so long as the transaction bore an "appropriate" relation to the forum. Inasmuch as the Uniform Commercial Code [Title 30, chapters 1 through 9A] has been adopted, at least in part, in all U.S. jurisdictions, the vitality

of this point is minimal in the domestic context, and international comity concerns militate against continuing the pro-forum, pro-UCC bias in transnational transactions. When the choice is between the law of two jurisdictions that have adopted the Uniform Commercial Code [Title 30, chapters 1 through 9A], but whose law differs (whether because of differences in enacted language or differing judicial interpretations), there is no strong justification for directing a court to apply different choice of law rules to its determination than it would apply if the matter were not governed by the Uniform Commercial Code [Title 30, chapters 1 through 9A]. Similarly, given the wide variety of choice of law principles applied by the States, it would not be prudent to designate only one such principle as the proper one for transactions governed by the Uniform Commercial Code [Title 30, chapters 1 through 9A]. Accordingly, in cases in which the parties have not made an effective choice of law, Section 1-301(a) [not adopted] simply directs the forum to apply its ordinary choice of law principles to determine which jurisdiction's law governs.

8. **Primacy of other UCC choice of law rules.** Subsection (f) [subsection (3)], which is essentially identical to former UCC Section 1-105(2) [30-1-105(2), 2003 MCA], indicates that choice of law rules provided in the other Articles govern when applicable.

9. **Matters not addressed by this section.** As noted in Comment 1, this section is not a complete statement of conflict of laws doctrines applicable in commercial cases. In particular, this section does not address, and leaves to other law, two issues that relate to the forum and its law. First, a forum will occasionally decline to apply the law of a different jurisdiction selected by the parties when application of that law would be contrary to a fundamental policy of the forum jurisdiction, even if it would not be contrary to a fundamental policy of the State or country whose law would govern in the absence of contractual designation. Standards for application of this doctrine relate primarily to concepts of sovereignty rather than commercial law and are thus left to the courts. Second, in determining whether to give effect to the parties' agreement that the law of a particular State or country will govern their relationship, courts must, of necessity, address some issues as to the basic validity of that agreement. These issues might relate, for example, to capacity to contract and absence of duress. This section does not address these issues.

Compiler's Comments

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

30-1-302. Variation by agreement.

Official Comments

[*Corresponding U.C.C. Section:* Section 1-302, U.C.C.]

Source: Former Sections 1-102(3)-(4) and 1-204(1) [30-1-102(3) and (4) and 30-1-204(1), 2003 MCA].

Changes From Former Law: This section combines the rules from subsections (3) and (4) of former Section 1-102 [30-1-102(3) and (4)] and subsection (1) of former Section 1-204 [30-1-204(1)]. No substantive changes are made.

1. Subsection (a) [subsection (1)] states affirmatively at the outset that freedom of contract is a principle of the Uniform Commercial Code [Title 30, chapters 1 through 9A]: "the effect" of its provisions may be varied by "agreement." The meaning of the statute itself must be found in its text, including its definitions, and in appropriate extrinsic aids; it cannot be varied by agreement. But the Uniform Commercial Code [Title 30, chapters 1 through 9A] seeks to avoid the type of interference with evolutionary growth found in pre-Code cases such as *Manhattan Co. v. Morgan*, 242 N.Y. 38, 150 N.E. 594 (1926). Thus private parties cannot make an instrument negotiable within the meaning of Article 3 [Title 30, chapter 3] except as provided in Section 3-104 [30-3-104]; nor can they change the meaning of such terms as "bona fide purchaser," "holder in due course," or "due negotiation," as used in the Uniform Commercial Code [Title 30, chapters 1 through 9A]. But an agreement can change the legal consequences that would otherwise flow from the provisions of the Uniform Commercial Code [Title 30, chapters 1 through 9A]. "Agreement" here includes the effect given to course of dealing, usage of trade and course of performance by Sections 1-201 [30-1-201] and 1-303 [30-1-205]; the effect of an agreement on the rights of third parties is left to specific provisions of the Uniform Commercial Code and to supplementary principles applicable under Section 1-103 [30-1-102(1) and 30-1-103]. The rights of third parties under Section 9-317 [30-9A-317] when a security interest is unperfected, for example, cannot be destroyed by a clause in the security agreement.

This principle of freedom of contract is subject to specific exceptions found elsewhere in the Uniform Commercial Code [Title 30, chapters 1 through 9A] and to the general exception stated here. The specific exceptions vary in explicitness: the statute of frauds found in Section 2-201 [30-2-201], for example, does not explicitly preclude oral waiver of the requirement of a writing, but a fair reading denies enforcement to such a waiver as part of the “contract” made unenforceable; Section 9-602 [30-9A-602], on the other hand, is a quite explicit limitation on freedom of contract. Under the exception for “the obligations of good faith, diligence, reasonableness and care prescribed by [the Uniform Commercial Code] [Title 30, chapters 1 through 9A],” provisions of the Uniform Commercial Code [Title 30, chapters 1 through 9A] prescribing such obligations are not to be disclaimed. However, the section also recognizes the prevailing practice of having agreements set forth standards by which due diligence is measured and explicitly provides that, in the absence of a showing that the standards manifestly are unreasonable, the agreement controls. In this connection, Section 1-303 [30-1-205] incorporating into the agreement prior course of dealing and usages of trade is of particular importance.

Subsection (b) [subsection (2)] also recognizes that nothing is stronger evidence of a reasonable time than the fixing of such time by a fair agreement between the parties. However, provision is made for disregarding a clause which whether by inadvertence or overreaching fixes a time so unreasonable that it amounts to eliminating all remedy under the contract. The parties are not required to fix the most reasonable time but may fix any time which is not obviously unfair as judged by the time of contracting.

2. An agreement that varies the effect of provisions of the Uniform Commercial Code [Title 30, chapters 1 through 9A] may do so by stating the rules that will govern in lieu of the provisions varied. Alternatively, the parties may vary the effect of such provisions by stating that their relationship will be governed by recognized bodies of rules or principles applicable to commercial transactions. Such bodies of rules or principles may include, for example, those that are promulgated by intergovernmental authorities such as UNCITRAL or UNIDROIT (*see, e.g.*, UNIDROIT Principles of International Commercial Contracts), or non-legal codes such as trade codes.

3. Subsection (c) [subsection (3)] is intended to make it clear that, as a matter of drafting, phrases such as “unless otherwise agreed” have been used to avoid controversy as to whether the subject matter of a particular section does or does not fall within the exceptions to subsection (b) [subsection (2)], but absence of such words contains no negative implication since under subsection (b) [subsection (2)] the general and residual rule is that the effect of all provisions of the Uniform Commercial Code [Title 30, chapters 1 through 9A] may be varied by agreement.

Compiler’s Comments

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

CHAPTER 2
UNIFORM COMMERCIAL CODE
SALES

Chapter Compiler’s Comments

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Section Not Codified: Section 87A-10-101, R.C.M. 1947, an effective date, was not codified in the MCA. This clause has not been repealed and is still valid law. Citation may be made to sec. 10-101, Ch. 264, L. 1963.

Montana Compiler Changes: Compiler has changed the Official Comments by changing “Article” to “Chapter” wherever it appears, and by prefacing section numbers with Title 30 so as to reflect Montana’s codification of the U.C.C.

Part 1
Short Title, General Construction, and Subject Matter

30-2-101. Short title.

Official Comment

This Chapter is a complete revision and modernization of the Uniform Sales Act which was promulgated by the National Conference of Commissioners on Uniform State Laws in 1906 and has been adopted in 36 states and the District of Columbia.

The coverage of the present Chapter is much more extensive than that of the old Sales Act and extends to the various bodies of case law which have been developed both outside of and under the latter.

The arrangement of the present Chapter is in terms of contract for sale and the various steps of its performance. The legal consequences are stated as following directly from the contract and action taken under it without resorting to the idea of when property or title passed or was to pass as being the determining factor. The purpose is to avoid making practical issues between practical men turn upon the location of an intangible something, the passing of which no man can prove by evidence and to substitute for such abstractions proof of words and actions of a tangible character.

30-2-102. Scope — certain security and other transactions excluded from this chapter.

Official Comment

Prior Uniform Statutory Provision: Section 75, Uniform Sales Act.

Changes: Section 75 has been rephrased.

Purposes of Changes and New Matter: To make it clear that:

The Chapter leaves substantially unaffected the law relating to purchase money security such as conditional sale or chattel mortgage though it regulates the general sales aspects of such transactions. "Security transaction" is used in the same sense as in the Chapter on Secured Transactions (Chapter 9A).

Case Notes

Statute of Frauds and Parol Evidence Rule Not Bar to Alleged Oral Contract — Genuine Issue of Material Fact Regarding Intent — Written Agreement Did Not Clearly Evidence Final Expression — Uniform Commercial Code Applied: The District Court did not err in denying the defendant's motion for summary judgment based on the defendant's assertion that an alleged oral contract was barred by the statute of frauds or the parol evidence rule. The agreement between the parties involved the sale of brake linings from the defendant to the plaintiff and the sale of remanufactured brakes from the plaintiff to another party. The brake linings and remanufactured brakes constituted moveable goods under 30-2-105, making the alleged oral contract within the ambit of the Montana Uniform Commercial Code's statute of frauds provision in 30-2-201. Because the parties entered into a written agreement and one party asserted the existence of an additional oral contract, the parol evidence rule provided for in 30-2-202 was applied. After the District Court made an initial determination under 30-2-202 that the program agreement did not clearly evidence a final expression of the parties' agreement, it properly denied summary judgment and allowed the jury to consider evidence to elucidate the true nature of the parties' agreement. S & P Brake Supply, Inc. v. STEMCO LP, 2016 MT 324, 385 Mont. 488, 385 P.3d 567, following Norwest Bank Billings v. Murnion, 210 Mont. 417, 684 P.2d 1067 (1984).

Foreseeability Not Required in Breach of Contract Action Under Uniform Commercial Code When Injury Results From Breach of Warranty: A breach of contract action under the Uniform Commercial Code does not require foreseeability if injury to person or property proximately results from any breach of warranty. Rothing v. Kallestad, 2007 MT 109, 337 M 193, 159 P3d 222 (2007).

Lease Transaction Actually Sales Agreement Subject to U.C.C. Provisions: Vendees leased a printing press from vendor; after making numerous monthly payments, vendees would obtain title to the press on payment of a small sum. As agreement contains an option to purchase at the end of the lease agreement, it falls within the sale of goods provisions of the U.C.C. Beneficial Commercial Corp. v. Cottrell, 212 M 493, 688 P2d 1254, 41 St. Rep. 1888 (1984).

Breach of Contractual Warranties — Proper Parties — Statute of Frauds: Plaintiffs in an action for breach of express and implied warranties were farmers. Defendants manufactured farm implements. One of the plaintiffs had an arm severed in an accident involving the defendants' machinery. On appeal, the defendants argued that the injured plaintiff was not a party to the purchase contract. The plaintiff alleged the salesman knew that he and the party who actually signed the purchase order were to be co-owners of the hay baler in question. The signature was for the one co-owner for himself and as agent for the plaintiff as well. Because principal and agent law supplements the Montana U.C.C. which covers the purchase of the baler, the court considered applying 28-10-203, which prevents oral authorization to contract when the contract itself must be written, as here. It noted exceptions to the Statute of Frauds, however. The question of whether payment of the purchase price took this contract out of the Statute of Frauds was a genuine issue of material fact preventing a summary judgment for the defendants under the Federal Rules of Civil Procedure. Holding the question one of law, the court said it had to hold an evidentiary hearing on the issues. Schlenz v. John Deere Co., 511 F. Supp. 224, 38 St. Rep. 579 (D.C. Mont. 1981).

Scope of the Statute of Frauds — Section as Applying to Sale of Registered Horses: Appellant's contention, arguing that an oral contract for the purchase and sale of five registered horses is not within the scope of the Statute of Frauds (30-2-201) and is therefore enforceable despite the lack of a writing confirming the contract, is not supportable. The transaction does not come within any of the exclusions provided for in 30-2-102. Scott v. Hjelm, 188 M 375, 613 P2d 1385, 37 St. Rep. 1219 (1980).

30-2-103. Definitions and index of definitions.

Official Comment

[*Corresponding U.C.C. Section:* Section 2-103, U.C.C.]

[*Code Commissioner Note:* In 2005, Montana adopted Alternative B of the 2003 revision to Article 7 for this section.]

Prior Uniform Statutory Provision: Subsection (1): Section 76, Uniform Sales Act.

Changes:

The definitions of "buyer" and "seller" have been slightly rephrased, the reference in Section 76 of the prior Act to "any legal successor in interest of such person" being omitted. The definition of "receipt" is new.

Purposes of Changes and New Matter:

1. The phrase "any legal successor in interest of such person" has been eliminated since Section 30-2-210 of this Chapter, which limits some types of delegation of performance on assignment of a sales contract, makes it clear that not every such successor can be safely included in the definition. In every ordinary case, however, such successors are as of course included.

2. "Receipt" must be distinguished from delivery particularly in regard to the problems arising out of shipment of goods, whether or not the contract calls for making delivery by way of documents of title, since the seller may frequently fulfill his obligations to "deliver" even though the buyer may never "receive" the goods. Delivery with respect to documents of title is defined in Chapter 1 and requires transfer of physical delivery of a tangible document of title and transfer of control of an electronic document of title. Otherwise the many divergent incidents of delivery are handled incident by incident.

Compiler's Comments

1999 Amendment: Chapter 305 in (3) in reference to "consumer goods" substituted "30-9-122" (renumbered 30-9A-102) for "30-9-109". Amendment effective July 1, 2001.

1991 Amendment: In (3), in citation for "dishonor", substituted "30-3-512" for "30-3-507"; and made minor changes in style.

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

Tort of Bad Faith — Not Available for Most Contract Actions — Breach: In a contract action, the Supreme Court ruled that a breach of the implied covenant of good faith and fair dealing constituted a breach of the contract and that only contract damages would be available to the prevailing party. The court stated that tort-type damages would not be available for a breach of the covenant. The court also held that the tort of bad faith would apply only in exceptional circumstances to discourage oppression in contracts that necessarily give one party a superior position. Every contract, regardless of the type, contains an implied covenant of good faith and fair dealing. A breach of the covenant is a breach of the contract. Story v. Bozeman, 242 M 436, 791 P2d 767, 47 St. Rep. 850 (1990), followed in Keller v. Dooling, 248 M 535, 813 P2d 437, 48 St. Rep. 554 (1991), Haines Pipeline Constr., Inc. v. Mont. Power Co., 251 M 422, 830 P2d 1230, 48 St. Rep. 1102 (1991), in McNeil v. Currie, 253 M 9, 830 P2d 1241, 49 St. Rep. 312 (1992), and Kneeland v. Luzenac America, Inc., 1998 MT 136, 289 M 201, 961 P2d 725, 55 St. Rep. 541 (1998).

30-2-104. Definitions — "merchant" — "between merchants" — "financing agency".

Official Comment

Prior Uniform Statutory Provision: None. But see Sections 15(2), (5), 16(c), 45(2) and 71, Uniform Sales Act, and Sections 35 and 37, Uniform Bills of Lading Act for examples of the policy expressly provided for in this Chapter.

Purposes:

1. This Chapter assumes that transactions between professionals in a given field require special and clear rules which may not apply to a casual or inexperienced seller or buyer. It thus adopts a policy of expressly stating rules applicable "between merchants" and "as against a

merchant", wherever they are needed instead of making them depend upon the circumstances of each case as in the statutes cited above. This section lays the foundation of this policy by defining those who are to be regarded as professionals or "merchants" and by stating when a transaction is deemed to be "between merchants".

2. The term "merchant" as defined here roots in the "law merchant" concept of a professional in business. The professional status under the definition may be based upon specialized knowledge as to the goods, specialized knowledge as to business practices, or specialized knowledge as to both and which kind of specialized knowledge may be sufficient to establish the merchant status is indicated by the nature of the provisions.

The special provisions as to merchants appear only in this Chapter and they are of three kinds. Sections 30-2-201(2), 30-2-205, 30-2-207 and 30-2-209 dealing with the statute of frauds, firm offers, confirmatory memoranda and modification rest on normal business practices which are or ought to be typical of and familiar to any person in business. For purposes of these sections almost every person in business would, therefore, be deemed to be a "merchant" under the language "who . . . by his occupation holds himself out as having knowledge or skill peculiar to the practices . . . involved in the transaction . ." since the practices involved in the transaction are non-specialized business practices such as answering mail. In this type of provision, banks or even universities, for example, well may be "merchants." But even these sections only apply to a merchant in his mercantile capacity; a lawyer or bank president buying fishing tackle for his own use is not a merchant.

On the other hand, in Section 30-2-314 on the warranty of merchantability, such warranty is implied only "if the seller is a merchant with respect to goods of that kind." Obviously this qualification restricts the implied warranty to a much smaller group than everyone who is engaged in business and requires a professional status as to particular kinds of goods. The exception in Section 30-2-402(2) for retention of possession by a merchant-seller falls in the same class; as does Section 30-2-403(2) on entrusting of possession to a merchant "who deals in goods of that kind".

A third group of sections includes 30-2-103(1)(b), which provides that in the case of a merchant "good faith" includes observance of reasonable commercial standards of fair dealing in the trade; 30-2-327(1)(c), 30-2-603 and 30-2-605, dealing with responsibilities of merchant buyers to follow seller's instructions, etc.; 30-2-509 on risk of loss, and 30-2-609 on adequate assurance of performance. This group of sections applies to persons who are merchants under either the "practices" or the "goods" aspect of the definition of merchant.

3. The "or to whom such knowledge or skill may be attributed by his employment of an agent or broker . . ." clause of the definition of merchant means that even persons such as universities, for example, can come within the definition of merchant if they have regular purchasing departments or business personnel who are familiar with business practices and who are equipped to take any action required.

Compiler's Comments

2005 Amendment: Chapter 575 in (1) near beginning substituted "is held out by occupation" for "by his occupation holds himself out" and near end substituted "that is held out by occupation" for "who by his occupation holds himself out"; in (2) near end of first sentence after "accompany" inserted "or are associated with"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

Case Notes

Foreseeability Not Required in Breach of Contract Action Under Uniform Commercial Code When Injury Results From Breach of Warranty: A breach of contract action under the Uniform Commercial Code does not require foreseeability if injury to person or property proximately results from any breach of warranty. Rothing v. Kallestad, 2007 MT 109, 337 M 193, 159 P3d 222 (2007).

Average Farmer Not a "Merchant": Faced with the absence of controlling state precedent, the federal District Court assumed that the Montana courts would follow the majority of states in finding that the average farmer is not a "merchant" as defined by 30-2-104. The issue must be determined on a case-by-case basis to see if the farmer possesses a special skill or knowledge in the marketing of grain. Where a farmer's sole connection with the grain market was the sale of his annual crop to the local grain elevators, such special skill or knowledge did not exist. Pierson v. Arnst, 534 F. Supp. 360, 39 St. Rep. 676 (D.C. Mont. 1982).

State as Merchant: It may well be that a state may be a merchant in some circumstances. However, the plaintiff did not carry its burden of proof in demonstrating that the state was a merchant in this transaction. W. Sign, Inc. v. St., 180 M 278, 590 P2d 141 (1979).

30-2-105. Definitions — transferability — "goods" — "future" goods — "lot" — "commercial unit".

Official Comment

Prior Uniform Statutory Provision: Subsections (1), (2), (3) and (4)—Sections 5, 6 and 76, Uniform Sales Act; Subsections (5) and (6)—none.

Changes: Rewritten.

Purposes of Changes and New Matter:

1. Subsection (1) on "goods": The phraseology of the prior uniform statutory provision has been changed so that:

The definition of goods is based on the concept of movability and the term "chattels personal" is not used. It is not intended to deal with things which are not fairly identifiable as movables before the contract is performed.

Growing crops are included within the definition of goods since they are frequently intended for sale. The concept of "industrial" growing crops has been abandoned, for under modern practices fruit, perennial hay, nursery stock and the like must be brought within the scope of this Chapter. The young of animals are also included expressly in this definition since they, too, are frequently intended for sale and may be contracted for before birth. The period of gestation of domestic animals is such that the provisions of the section on identification can apply as in the case of crops to be planted. The reason of this definition also leads to the inclusion of a wool crop or the like as "goods" subject to identification under this Chapter.

The exclusion of "money in which the price is to be paid" from the definition of goods does not mean that foreign currency which is included in the definition of money may not be the subject matter of a sales transaction. Goods is intended to cover the sale of money when money is being treated as a commodity but not to include it when money is the medium of payment.

As to contracts to sell timber, minerals, or structures to be removed from the land Section 30-2-107(1) (Goods to be severed from Realty: recording) controls.

The use of the word "fixtures" is avoided in view of the diversity of definitions of that term. This Chapter in including within its scope "things attached to realty" adds the further test that they must be capable of severance without material harm thereto. As between the parties any identified things which fall within that definition become "goods" upon the making of the contract for sale.

"Investment securities" are expressly excluded from the coverage of this Chapter. It is not intended by this exclusion, however, to prevent the application of a particular section of this Chapter by analogy to securities (as was done with the Original Sales Act in Agar v. Orda, 264 N.Y. 248, 190 N.E. 479, 99 A.L.R. 269 (1934)) when the reason of that section makes such application sensible and the situation involved is not covered by the Chapter of this Act dealing specifically with such securities (Chapter 8).

2. References to the fact that a contract for sale can extend to future or contingent goods and that ownership in common follows the sale of a part interest have been omitted here as obvious without need for expression; hence no inference to negate these principles should be drawn from their omission.

3. Subsection (4) does not touch the question of how far an appropriation of a bulk of fungible goods may or may not satisfy the contract for sale.

4. Subsections (5) and (6) on "lot" and "commercial unit" are introduced to aid in the phrasing of later sections.

5. The question of when an identification of goods takes place is determined by the provisions of Section 30-2-501 and all that this section says is what kinds of goods may be the subject of a sale.

Case Notes

Statute of Frauds and Parol Evidence Rule Not Bar to Alleged Oral Contract — Genuine Issue of Material Fact Regarding Intent — Written Agreement Did Not Clearly Evidence Final Expression — Uniform Commercial Code Applied: The District Court did not err in denying the defendant's motion for summary judgment based on the defendant's assertion that an alleged oral contract was barred by the statute of frauds or the parol evidence rule. The agreement between the parties involved the sale of brake linings from the defendant to the plaintiff and the sale of remanufactured brakes from the plaintiff to another party. The brake linings and remanufactured brakes constituted moveable goods under 30-2-105, making the alleged oral contract within the ambit of the Montana Uniform Commercial Code's statute of frauds provision in 30-2-201. Because the parties entered into a written agreement and one party asserted the existence of an additional oral contract, the parol evidence rule provided for in 30-2-202 was applied. After the District Court made an initial determination under 30-2-202 that the program agreement did not clearly evidence a final expression of the parties' agreement, it properly denied summary judgment and allowed the jury to consider evidence to elucidate the true nature of the parties' agreement. S & P Brake Supply, Inc. v. STEMCO LP, 2016 MT 324, 385 Mont. 488, 385 P.3d 567, following Norwest Bank Billings v. Murnion, 210 Mont. 417, 684 P.2d 1067 (1984).

Foreseeability Not Required in Breach of Contract Action Under Uniform Commercial Code When Injury Results From Breach of Warranty: A breach of contract action under the Uniform Commercial Code does not require foreseeability if injury to person or property proximately results from any breach of warranty. Rothing v. Kallestad, 2007 MT 109, 337 M 193, 159 P3d 222 (2007).

Sale of Front-End Loader — Applicable Parol Evidence Rule: Front-end loader that buyer purchased from seller was within the definition of "goods" set out in 30-2-105. Therefore, the sale was governed by the Montana Uniform Commercial Code, and any Code provisions addressing a parol evidence question controlled the answer to the question, with the contract law parol evidence rule of 28-2-904 being used only to supplement the Code. Norwest Bank Billings v. Murnion, 210 M 417, 684 P2d 1067, 41 St. Rep. 1132 (1984).

Modular Home — Applicable Warranty Law: Sale of modular home manufactured at defendant's plant and delivered to plaintiffs' building site was governed by the U.C.C. warranty provisions and not the warranty provisions of Title 30, ch. 11, part 2, which are made inapplicable by 30-11-224. The fact that defendant had charge of the home until after it was affixed to plaintiffs' foundation and no longer had mobility did not affect the applicability of the U.C.C. warranty provisions, for the home was manufactured to plaintiffs' specifications, was thus identified to the contract under the U.C.C. at the time of the first step of its production, was movable at that time, and thus was "goods" the sale of which the U.C.C. applied. Little v. Grizzly Mfg., 195 M 419, 636 P2d 839, 38 St. Rep. 1994 (1981).

Breach of Contractual Warranties — Proper Parties — Statute of Frauds: Plaintiffs in an action for breach of express and implied warranties were farmers. Defendants manufactured farm implements. One of the plaintiffs had an arm severed in an accident involving the defendants' machinery. On appeal, the defendants argued that the injured plaintiff was not a party to the purchase contract. The plaintiff alleged the salesman knew that he and the party who actually signed the purchase order were to be co-owners of the hay baler in question. The signature was for the one co-owner for himself and as agent for the plaintiff as well. The purchase and sale of the round hay baler were transactions in goods covered by the U.C.C. Because principal and agent law supplements the Montana U.C.C. which covers the purchase of the baler, the court considered applying 28-10-203, which prevents oral authorization to contract when the contract itself must be written, as here. It noted exceptions to the Statute of Frauds, however. The question of whether payment of the purchase price took this contract out of the Statute of Frauds was a genuine issue of material fact preventing a summary judgment for the defendants under the Federal Rules of Civil Procedure. Holding the question one of law, the court said it had to hold an evidentiary hearing on the issues. Schlenz v. John Deere Co., 511 F. Supp. 224, 38 St. Rep. 579 (D.C. Mont. 1981).

Attorney General's Opinions

Sugar Refinery's Piled Sugar Beets Exempt From Tax — Business Inventory: If the products of a sugar refinery qualify as business inventory under 15-6-202, then the raw materials (sugar beets) used to produce such products also qualify for the exemption, since the definition of business inventory also includes "raw materials and work in progress with respect to such goods". While not defined by the Legislature, the term "raw materials" is generally defined as the material or substance out of which other products or the final product is made. 40 A.G. Op. 82 (1984).

30-2-106. Definitions — "contract" — "agreement" — "contract for sale" — "sale" — "present sale" — "conforming" to contract — "termination" — "cancellation".

Official Comment

Prior Uniform Statutory Provision: Subsection (1)—Section 1(1) and (2), Uniform Sales Act; Subsection (2)—none, but subsection generally continues policy of Sections 11, 44 and 69, Uniform Sales Act; Subsections (3) and (4)—none.

Changes: Completely rewritten.

Purposes of Changes and New Matter:

1. Subsection (1): "Contract for sale" is used as a general concept throughout this Chapter, but the rights of the parties do not vary according to whether the transaction is a present sale or a contract to sell unless the Chapter expressly so provides.

2. Subsection (2): It is in general intended to continue the policy of requiring exact performance by the seller of his obligations as a condition to his right to require acceptance. However, the seller is in part safeguarded against surprise as a result of sudden technicality on the buyer's part by the provisions of Section 30-2-508 on seller's cure of improper tender or delivery. Moreover usage of trade frequently permits commercial leeways in performance and the language of the agreement itself must be read in the light of such custom or usage and also, prior course of dealing, and in a long term contract, the course of performance.

3. Subsections (3) and (4): These subsections are intended to make clear the distinction carried forward throughout this Chapter between termination and cancellation.

Case Notes

Payment After Unilateral Price Increase as Termination of Contract and Formation of New Contract — Adequate Notice Found: Hansens ordered 30 truckloads of logs from Lumber Enterprises, Inc., at a special price. The parties agreed to ship and receive the logs over a longer period of time than originally agreed. After delivery of 18 truckloads, Lumber Enterprises raised the price of each load by about 50% and told Hansens to "take it or leave it". Hansens agreed to the increase under protest but refused to pay for the last three loads. Citing the official comment to 30-2-209 and testimony by the Lumber Enterprises manager that the company had to raise prices because it discovered it was losing money on each truckload at the agreed price, the Supreme Court held that the indefinite extension allowed the contract to be terminated at any time by either party. The Supreme Court held that when Lumber Enterprises raised its prices and the Hansens purchased logs more than 30 days after that increase, the former contract had been terminated and a new contract agreed to after reasonable notification. The District Court therefore did not abuse its discretion in applying 30-2-309. Lumber Enterprises, Inc. v. Hansen, 257 M 11, 846 P2d 1046, 50 St. Rep. 138 (1993).

Award of Damages for Delivery of Nonconforming Goods: Contract terms provided for a building 18 feet high, but Meland learned upon beginning construction that the building height would be less than 18 feet. He notified Intermountain of the problem, then altered the construction sequence to obtain the desired height. He later ran out of materials, necessitating expenditure of $4,085 for additional materials, labor, and temporary grain storage facilities. He then filed suit alleging breach of the sales contract. The District Court awarded Meland $4,085 in damages as a result of Intermountain's delivery of nonconforming goods. Under 30-2-106, goods are conforming when they are in accordance with the contract obligations. The Supreme Court affirmed the damage award, as the goods were not in accord with the contract terms. Meland v. Intermtn. Sys., Inc., 219 M 242, 712 P2d 1295, 42 St. Rep. 1987 (1985).

Lease Transaction Actually Sales Agreement Subject to U.C.C. Provisions: Vendees leased a printing press from vendor; after making numerous monthly payments, vendees would obtain title to the press on payment of a small sum. As agreement contains an option to purchase at the end of the lease agreement, it falls within the sale of goods provisions of the U.C.C. (See 1991 enactment of chapter 2A.) Beneficial Commercial Corp. v. Cottrell, 212 M 493, 688 P2d 1254, 41 St. Rep. 1888 (1984).

Railroad Right-of-Way Lease — Not Contract for Sale: Section 30-2-107 does not apply to a railroad right-of-way lease because the lease is not a contract for sale within the meaning of this section. (See 1991 enactment of chapter 2A.) Pac. Metal Co. v. NW. Bank of Helena, 205 M 323, 667 P2d 958, 40 St. Rep. 1301 (1983).

Lease as Installment Sale: The parties entered into an agreement for the installation and maintenance of a fire alarm system that was termed a "lease agreement". Payments were to be made over a 5-year term at the expiration of which defendant had the option to renew for another 5-year term or to purchase the system for $1. The District Court found that the transaction was in effect a "sale". The Supreme Court affirmed, saying that in circumstances where the purported lease gives the lessee the option to purchase the goods upon expiration of the term of the lease for a nominal amount, the lease is commercially indistinguishable from an installment sales contract and the provisions of the U.C.C. apply. (See 1991 enactment of chapter 2A.) Fire Supply & Serv., Inc. v. Chico Hot Springs, 196 M 435, 639 P2d 1160, 39 St. Rep. 231 (1982).

Implied Warranty of Merchantability Inapplicable to Lease: Defendant leased a truck from plaintiff. The truck was in the shop many times, and after an accident and long delays in obtaining parts, defendant defaulted on the lease. Plaintiff sued for amounts owing under the lease, and defendant counterclaimed for breach of the implied warranty of merchantability. The implied warranty of merchantability is only applicable in the event of a "sale" as defined in the Uniform Commercial Code. On the basis of the definition of sale and language contained in the lease agreement, the Supreme Court found that the implied warranty of merchantability was not applicable. (See 1991 enactment of chapter 2A.) R & W Leasing v. Mosher, 195 M 285, 636 P2d 832, 38 St. Rep. 1857 (1981).

"Lease" Construed as Sales Transaction: Although the contract between the parties stated that "The equipment is, and shall be and remain, the sole and exclusive personal property of the lessor; and the lessee shall have no right, title or interest therein except as expressly set forth in this lease", the agreement qualified as a sales transaction invoking the Montana Uniform Commercial Code when construed with the shipping order, which provided for title conveyance. (See 1991 enactment of chapter 2A.) Transcont. Refrigeration Co. v. Figgins, 179 M 12, 585 P2d 1301 (1978), followed in Westmont Tractor Co. v. Viking Exploration, Inc., 534 F. Supp. 1314, 39 St. Rep. 1398 (D.C Mont. 1982).

30-2-107. Goods to be severed from realty — recording.

Official Comment

Prior Uniform Statutory Provision: See Section 76, Uniform Sales Act on prior policy; Section 7, Uniform Conditional Sales Act.

Purposes:

1. Subsection (1). Notice that this subsection applies only if the minerals or structures "are to be severed by the seller". If the buyer is to sever, such transactions are considered contracts affecting land and all problems of the Statute of Frauds and of the recording of land rights apply to them. Therefore, the Statute of Frauds section of this Chapter does not apply to such contracts though they must conform to the Statute of Frauds affecting the transfer of interests in land.

2. Subsection (2). "Things attached" to the realty which can be severed without material harm are goods within this Chapter regardless of who is to effect the severance. The word "fixtures" has been avoided because of the diverse definitions of this term, the test of "severance without material harm" being substituted.

The provision in subsection (3) for recording such contracts is within the purview of this Chapter since it is a means of preserving the buyer's rights under the contract of sale.

3. The security phases of things attached to or to become attached to realty are dealt with in the Chapter on Secured Transactions (Chapter 9A) and it is to be noted that the definition of goods in that Chapter differs from the definition of goods in this Chapter.

However, both Chapters treat as goods growing crops and also timber to be cut under a contract of severance.

Reasons for 1972 Change: Several timber-growing states have changed the 1962 Code to make timber to be cut under a contract of severance goods, regardless of the question who is to sever them. The section is revised to adopt this change. Financing of the transaction is facilitated if the timber is treated as goods instead of real estate. A similar change is made in the definition of "goods" in Section 30-9-105 [now repealed, see 30-9A-102]. To protect persons dealing with timberlands, filing on timber to be cut is required in Part 4 of Chapter 9 (renumbered, see 30-9A-501) to be made in real estate records in a manner comparable to fixture filing.

Compiler's Comments

1983 Amendment: Near beginning of (1), deleted "timber" before "minerals"; in (1) inserted "(including oil and gas)"; in (2) inserted "or of timber to be cut" after "not described in subsection (1)".

Source of 1983 Amendment: The source of the 1983 amendment was the 1972 amendments to Article 9 of the Uniform Commercial Code drafted by the National Conference of Commissioners on Uniform State Laws. The amendment was to Section 2-107 of the Official Text of the Uniform Commercial Code.

Case Notes

Unenforceable Timber Sale by Agent Without Written Authority: Gebert Logging contracted in writing with Palin to remove timber from certain land. This was a contract under this section of the U.C.C. for goods to be severed from realty. The contract price was over $500, so under 30-2-201 of the U.C.C., the contract had to be in writing. Under 28-10-203 relating to agency, authority to enter into a contract that the law requires to be written can only be given by an instrument that is itself written. Since Palin did not own the land and did not have written authority from his wife, the owner, to execute the contract as her agent, the contract was unenforceable because it was not signed by or with the written authority of the owner of the land. Gebert Logging was thus entitled to receive back its land damage bond, and Palin was not entitled to damages for alleged unrepaired injury to the land. The court denied Palin's claims that part performance took the contract out of the Statute of Frauds and that the contract should not be invalidated because he had altered his position to his detriment. The court also held that his wife could not retroactively ratify his acts without the consent of Gebert Logging, which was not given. Gebert Logging, Inc. v. Palin, 220 M 405, 716 P2d 200, 43 St. Rep. 481 (1986).

Section Inapplicable to Railroad Right-of-Way Lease: This section does not apply to a railroad right-of-way lease because the lease is not a contract for sale as defined by 30-2-106. (See 1991 enactment of chapter 2A.) Pac. Metal Co. v. NW. Bank of Helena, 205 M 323, 667 P2d 958, 40 St. Rep. 1301 (1983).

U.C.C. — Application to Timber Contracts: Defendant was to selectively cut diseased trees on plaintiff's land under a contract entered by the parties. Defendant clearcut several stands of timber. He contended that this was the best management practice to control the spread of the disease. He argued that this established a "usage of trade" under 30-2-208, which should be used in construing the contract. Section 30-2-107(1) establishes that a contract for the sale of timber is subject to the Uniform Commercial Code (U.C.C.) only if the timber is to be "severed by the seller". This was not the case here, so the provisions of the U.C.C. did not apply. Madison Fork Ranch v. L&B Lodge Pole Timber Prod., 189 M 292, 615 P2d 900, 37 St. Rep. 1468 (1980).

Notice: A contract for sale of standing timber is enforceable against a subsequent buyer of the land only to the extent that he has or is chargeable with notice thereof. Pegg v. Mid-State Dev. Corp., 164 M 525, 529 P2d 1399 (1974).

Timber: A contract for sale of standing timber may be enforced under the provisions of the Uniform Commercial Code or under general contract law of realty. Pegg v. Mid-State Dev. Corp., 164 M 525, 529 P2d 1399 (1974).

Part 2
Form, Formation, and Readjustment of Contract

30-2-201. Formal requirements — statute of frauds.

Official Comment

Prior Uniform Statutory Provision: Section 4, Uniform Sales Act (which was based on Section 17 of the Statute of 29 Charles II).

Changes: Completely rephrased; restricted to sale of goods. See also Sections 30-1-206 [now repealed], 30-8-319 [now repealed, see 30-8-123] and 30-9-203 [now repealed, see 30-9A-203].

Purposes of Changes: The changed phraseology of this section is intended to make it clear that:

1. The required writing need not contain all the material terms of the contract and such material terms as are stated need not be precisely stated. All that is required is that the writing afford a basis for believing that the offered oral evidence rests on a real transaction. It may be written in lead pencil on a scratch pad. It need not indicate which party is the buyer and which the seller. The only term which must appear is the quantity term which need not be accurately stated but recovery is limited to the amount stated. The price, time and place of payment or delivery, the general quality of the goods, or any particular warranties may all be omitted.

Special emphasis must be placed on the permissibility of omitting the price term in view of the insistence of some courts on the express inclusion of this term even where the parties have contracted on the basis of a published price list. In many valid contracts for sale the parties do not mention the price in express terms, the buyer being bound to pay and the seller to accept a reasonable price which the trier of the fact may well be trusted to determine. Again, frequently the price is not mentioned since the parties have based their agreement on a price list or catalogue known to both of them and this list serves as an efficient safeguard against perjury. Finally, "market" prices and valuations that are current in the vicinity constitute a similar check. Thus if the price is not stated in the memorandum it can normally be supplied without danger of fraud. Of course if the "price" consists of goods rather than money the quantity of goods must be stated.

Only three definite and invariable requirements as to the memorandum are made by this subsection. First, it must evidence a contract for the sale of goods; second, it must be "signed", a word which includes any authentication which identifies the party to be charged; and third, it must specify a quantity.

2. "Partial performance" as a substitute for the required memorandum can validate the contract only for the goods which have been accepted or for which payment has been made and accepted.

Receipt and acceptance either of goods or of the price constitutes an unambiguous overt omission by both parties that a contract actually exists. If the court can make a just apportionment, therefore, the agreed price of any goods actually delivered can be recovered without a writing or, if the price has been paid, the seller can be forced to deliver an apportionable part of the goods. The overt actions of the parties make admissible evidence of the other terms of the contract necessary to a just apportionment. This is true even though the actions of the parties are not in themselves inconsistent with a different transaction such as a consignment for resale or a mere loan of money.

Part performance by the buyer requires the delivery of something by him that is accepted by the seller as such performance. Thus, part payment may be made by money or check, accepted by the seller. If the agreed price consists of goods or services, then they must also have been delivered and accepted.

3. Between merchants, failure to answer a written confirmation of a contract within ten days of receipt is tantamount to a writing under subsection (2) and is sufficient against both parties under subsection (1). The only effect, however, is to take away from the party who fails to answer the defense of the Statute of Frauds; the burden of persuading the trier of fact that a contract was in fact made orally prior to the written confirmation is unaffected. Compare the effect of a failure to reply under Section 30-2-207.

4. Failure to satisfy the requirements of this section does not render the contract void for all purposes, but merely prevents it from being judicially enforced in favor of a party to the contract. For example, a buyer who takes possession of goods as provided in an oral contract which the seller has not meanwhile repudiated, is not a trespasser. Nor would the Statute of Frauds provisions of this section be a defense to a third person who wrongfully induces a party to refuse to perform an oral contract, even though the injured party cannot maintain an action for damages against the party so refusing to perform.

5. The requirement of "signing" is discussed in the comment to Section 30-1-201.

6. It is not necessary that the writing be delivered to anybody. It need not be signed or authenticated by both parties but it is, of course, not sufficient against one who has not signed it. Prior to a dispute no one can determine which party's signing of the memorandum may be necessary but from the time of contracting each party should be aware that to him it is signing by the other which is important.

7. If the making of a contract is admitted in court, either in a written pleading, by stipulation or by oral statement before the court, no additional writing is necessary for protection against fraud. Under this section it is no longer possible to admit the contract in court and still treat the Statute as a defense. However, the contract is not thus conclusively established. The admission so made by a party is itself evidential against him of the truth of the facts so admitted and of nothing more; as against the other party, it is not evidential at all.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

DECISIONS UNDER U.C.C.

Partial Performance Principle Displaced by Montana Uniform Commercial Code: The District Court erred in denying the defendant's motion for judgment as a matter of law to the extent that it relied on the part performance exception. Unlike estoppel, the principle of partial performance is displaced by the particular provisions of the Montana Uniform Commercial Code. The part performance exception to the Montana UCC statute of frauds is much more limited than the part performance doctrine outside the Montana UCC context. As such, the plaintiff could not rely on a partial performance exception to exempt an alleged oral contract from the Montana UCC statute of frauds. S & P Brake Supply, Inc. v. STEMCO LP, 2016 MT 324, 385 Mont. 488, 385 P.3d 567.

Promissory Estoppel Not Displaced by Montana Uniform Commercial Code: The District Court did not err in denying the defendant's summary judgment motion and allowing the question of whether the plaintiff could satisfy the promissory estoppel exception to proceed to trial. Like other forms of estoppel, promissory estoppel is not displaced by the particular provisions of the Montana Uniform Commercial Code. Promissory estoppel may apply to remove a transaction from the Montana UCC statute of frauds. S & P Brake Supply, Inc. v. STEMCO LP, 2016 MT 324, 385 Mont. 488, 385 P.3d 567. See also NW. Potato Sales, Inc. v. Beck, 208 Mont. 310, 678 P.2d 1138 (1984).

Statute of Frauds and Parol Evidence Rule Not Bar to Alleged Oral Contract — Genuine Issue of Material Fact Regarding Intent — Written Agreement Did Not Clearly Evidence Final Expression — Uniform Commercial Code Applied: The District Court did not err in denying the defendant's motion for summary judgment based on the defendant's assertion that an alleged oral contract was barred by the statute of frauds or the parol evidence rule. The agreement between the parties involved the sale of brake linings from the defendant to the plaintiff and the sale of remanufactured brakes from the plaintiff to another party. The brake linings and remanufactured brakes constituted moveable goods under 30-2-105, making the alleged oral contract within the ambit of the Montana Uniform Commercial Code's statute of frauds provision in 30-2-201. Because the parties entered into a written agreement and one party asserted the existence of an additional oral contract, the parol evidence rule provided for in 30-2-202 was applied. After the District Court made an initial determination under 30-2-202 that the program agreement did not clearly evidence a final expression of the parties' agreement, it properly denied summary judgment and allowed the jury to consider evidence to elucidate the true nature of the parties' agreement. S & P Brake Supply, Inc. v. STEMCO LP, 2016 MT 324, 385 Mont. 488, 385 P.3d 567, following Norwest Bank Billings v. Murnion, 210 Mont. 417, 684 P.2d 1067 (1984).

Failure to Bring Fraud Action Within Time Claim Accrues — Statute of Limitations Precluding Fraud Action: Plaintiff discovered or reasonably should have discovered within 6 months of purchasing a trailer park in May 2003 that a fraud may have been perpetrated regarding the profitability of the park and the condition of the park water system, but plaintiff did not bring a fraud or misrepresentation claim until 2007. The actual and constructive fraud claims were therefore precluded by the statute of limitations in 27-2-203, which requires an action for fraud to be commenced within 2 years. Plaintiff's claims were properly dismissed as untimely. Deschamps v. Treasure St. Trailer Ct., Ltd., 2010 MT 74, 356 Mont. 1, 230 P.3d 800.

Failure to Notify Grain Buyer of Intent to Breach Oral Agreement Within Reasonable Time — Oral Contract Enforceable: ConAgra, Inc. (ConAgra), contended that it had an oral telephone contract with Nierenberg to purchase 12,500 bushels of wheat and filed an action to recover losses incurred when Nierenberg sold the wheat to someone else, requiring ConAgra to purchase other wheat for resale at a higher price to fulfill its sale obligations pursuant to its purchase of Nierenberg's wheat. The District Court determined that Nierenberg was a merchant within the context of the Uniform Commercial Code and that, although both parties were merchants, the written sale confirmation received by Nierenberg 10 days after the telephone conversation was not within a reasonable time. Nierenberg never objected in writing to the written confirmation. The Supreme Court noted that the merchant exception in this section does not dictate which party must send the written confirmation, but rather that in order to create an enforceable oral contract and avoid the signed writing requirement, one of the parties must send written confirmation to the other party. A farmer as well as a buyer may lock in an oral contract price as the market fluctuates up or down, and both parties equally possess the power to bind the other party. In this case, ConAgra did not immediately mail a written agreement, but instead waited about 6 days for Nierenberg to come to the elevator and sign the contract in person before mailing it. Although a court must look at the broad nature, purpose, and circumstances in determining whether written confirmation was received within a reasonable time, two specific factors may be examined: (1) the merchant's usual practice or policy following such transactions; and (2) the merchant's excuse for not following its practice or policy. The slight delay in Nierenberg's receipt of the confirmation because of an apparent misunderstanding was not seen as an unreasonable deviation from ConAgra's usual practices under the circumstances. However, Nierenberg chose to simply not honor his contractual obligation without notifying ConAgra of his true intentions. Nierenberg's mistake was to act outside of accepted commercial grain sales practices and not give ConAgra prompt notice of his breach so that his obligation for expectancy damages would be fixed. The written confirmation became an enforceable binding contract when Nierenberg failed to respond in writing with his objections within the stated 10-day period. The Supreme Court reversed the District Court's finding that the oral agreement could not be enforced. ConAgra, Inc. v. Nierenberg, 2000 MT 213, 301 M 55, 7 P3d 369, 57 St. Rep. 842 (2000).

Rules for Determining Whether Judicial Admission Made to Establish Oral Contract for Sale of Grain: ConAgra, Inc. (ConAgra), contended that it had an oral telephone contract with Nierenberg to purchase 12,500 bushels of wheat and filed an action to recover losses incurred when Nierenberg sold the wheat to someone else, requiring ConAgra to purchase other wheat for resale at a higher price to fulfill its sale obligations pursuant to its purchase of Nierenberg's wheat. The District Court determined that Nierenberg was a merchant within the context of the Uniform Commercial Code, based on the fact that Nierenberg had been selling grain for many years and was familiar with grain prices through periodic visits to local grain elevators. The court also concluded that, although both parties were merchants, the written sale confirmation received by Nierenberg 10 days after the telephone conversation was not within a reasonable time. Noting that the rules governing sales agreements under the Uniform Commercial Code are far more permissive than general contract rules under the common law, the Supreme Court found that the District Court erred in determining that a contract was not formed because Nierenberg did not unambiguously testify to the necessary elements of a contract. Under this section, a contract that does not satisfy the signed writing requirements, but that is valid in other respects, is enforceable if the party against whom enforcement is sought admits that a contract for sale was made. For a judicial admission to be binding, the admission must be an unequivocal statement of fact rather than a conclusion of law or the expression of an opinion. Prodding a party while on the witness stand or while testifying during a deposition to say certain magical words that may indicate that a contract was formed will be viewed with disfavor. Instead, the Supreme Court cited Thomas v. Prewitt, 355 S2d 657 (Miss. 1978), for the five-part rule for testing the sufficiency of a claimed judicial admission: (1) the declaration relied on was made during the course of a judicial proceeding; (2) the statement was contradictory to an essential fact embraced in the theory of recovery or defense asserted by the person giving the testimony; (3) the statement was deliberate, clear, and unequivocal; (4) giving of conclusive effect to the declaration is consistent with public policy; and (5) the testimony must be such as relates to a fact upon which a judgment for the opposing party may be based. The Supreme Court's review will adhere to the outward objective manifestations test expressed in Miller v. Walter, 165 M 221, 527 P2d 240 (1974), namely whether intent that a contract existed must be gathered from the outward objective manifestations of the parties and not by the subjective undisclosed intent of one of the parties. In Nierenberg's case, his testimony indicated that most of his grain sales involved signing a contract shortly after oral discussions with ConAgra—an apparent contradiction to an outright admission that he was orally bound to sell the grain. The fact that Nierenberg was willing to further negotiate the quantity of grain was not the objective conduct of a person who was contractually bound without a signed writing. The testimonial facts concerning Nierenberg's postphone conversation conduct were ambiguous, and the District Court did not err in holding that Nierenberg did not make a judicial admission that a contract was made, even though that conclusion was not dispositive of the ultimate determination of whether an enforceable contract was made. ConAgra, Inc. v. Nierenberg, 2000 MT 213, 301 M 55, 7 P3d 369, 57 St. Rep. 842 (2000).

Farmer May Be Merchant in Grain Sale — Oral Contract Upheld: Jack, acting as personal representative of his brother's estate, was considered a merchant for purposes of this section because he had operative knowledge of the grain marketing system and was familiar with all facets of marketing grain, including knowledge of the product, how to produce it, and how to negotiate the best terms for its sale. When he made a contract over the phone for sale of grain and the other party sent a confirmation, which Jack did not sign or return, the contract was enforceable under the merchant exception to the statute of frauds. General Mills was entitled to withhold $15,000 under a subsequent contract as an offset of the difference on the two contracts. Smith v. Gen. Mills, Inc., 1998 MT 280, 291 M 426, 968 P2d 723, 55 St. Rep. 1151 (1998).

Oral Contract Enforceable — Statute of Frauds Defense Inapplicable: Defendants orally agreed to sell 6,500 bushels of wheat to Columbia Grain International (Columbia Grain) at $4.05 a bushel. Relying on the oral agreement, Columbia Grain sold the wheat in open market. When defendants refused to deliver the wheat, Columbia Grain purchased wheat from another seller for $4.68 a bushel. In an action to recover damages for breach of contract, the District Court awarded Columbia Grain the difference between the contract price of $4.05 and the replacement price of $4.68. On appeal, defendants claimed that the District Court erred in recognizing the existence of a contract, in failing to apply the statute of frauds defense, and in calculating damages. The Supreme Court affirmed, finding that an oral contract existed based on the parties' prior course of dealings and general industry practices and that defendants had waived their right to rely on the statute of frauds defense by not affirmatively pleading the defense. Damages are properly based on the cost of Columbia Grain to cover the undelivered grain. Columbia Grain Int'l v. Cereck, 258 M 414, 852 P2d 676, 50 St. Rep. 591 (1993).

Unenforceable Timber Sale by Agent Without Written Authority: Gebert Logging contracted in writing with Palin to remove timber from certain land. This was a contract under 30-2-107 of the U.C.C. for goods to be severed from realty. The contract price was over $500, so under 30-2-201 of the U.C.C., the contract had to be in writing. Under 28-10-203 relating to agency, authority to enter into a contract that the law requires to be written can only be given by an instrument that is itself written. Since Palin did not own the land and did not have written authority from his wife, the owner, to execute the contract as her agent, the contract was unenforceable because it was not signed by or with the written authority of the owner of the land. Gebert Logging was thus entitled to receive back its land damage bond, and Palin was not entitled to damages for alleged unrepaired injury to the land. The court denied Palin's claims that part performance took the contract out of the Statute of Frauds and that the contract should not be invalidated because he had altered his position to his detriment. The court also held that his wife could not retroactively ratify his acts without the consent of Gebert Logging, which was not given. Gebert Logging, Inc. v. Palin, 220 M 405, 716 P2d 200, 43 St. Rep. 481 (1986).

Transaction Constitutes Lease — Not Installment Sales Contract: The facts of this case indicate that the lessee did not have the option to obtain title to the property at no further charge at the termination of the lease. Therefore, the court found the characterization of the transaction was a lease of equipment and was not governed by the provisions of the Uniform Commercial Code. (See 1991 enactment of chapter 2A.) IFG Leasing Co. v. Schultz, 217 M 434, 705 P2d 576, 42 St. Rep. 1307 (1985), following Diede v. Davis, 203 M 205, 661 P2d 838, 40 St. Rep. 394 (1983).

Estoppel to Prevent Application of Statute of Frauds: In a contract action brought by the plaintiff buyer of seed potatoes against the seller, in which the evidence showed that the defendant had never signed a written contract for the potatoes, but by his active and passive conduct induced the plaintiff to change his position by agreeing to sell the potatoes that were the subject of the contract to other buyers, the Supreme Court held that the plaintiff had proved the elements of estoppel by silence or equitable estoppel and that the defendant would therefore be estopped in applying the Statute of Frauds to the oral contract. NW. Potato Sales, Inc. v. Beck, 208 M 310, 678 P2d 1138, 41 St. Rep. 362 (1984), followed, with regard to elements of estoppel, in CB&F Dev. Corp. v. Culbertson St. Bank, 256 M 1, 844 P2d 5, 49 St. Rep. 1122 (1992).

Written Bid Ripens Into Contract — Writing Held Sufficient: Where the Commissioners of the defendant county attempted to reject a written bid, after first voting to accept it, arguing that there was no written contract sufficient to satisfy the Statute of Frauds, the Supreme Court held that the written bid accepted by the Commission ripened into a contract. Thus, there was a valid contract, not barred by the Statute of Frauds. Modern Mach. v. Flathead County, 202 M 140, 656 P2d 206, 39 St. Rep. 2383 (1982).

Equitable Principles — Estopped From Invalidating Agreement Under Statute of Frauds: Agreement between plaintiff and defendant to sell property was valid under the Statute of Frauds even though the written instrument was signed only by the plaintiff and defendant's wife when plaintiff had made an irretrievable change in position and defendant had secured an unconscionable advantage or inflicted an unjust or unconscionable loss upon the plaintiff. Bolz v. Myers, 200 M 286, 651 P2d 606, 39 St. Rep. 1747 (1982).

Average Farmer Not a "Merchant": Faced with the absence of controlling state precedent, the federal District Court assumed that the Montana courts would follow the majority of states in finding that the average farmer is not a "merchant" as defined by 30-2-104. The issue must be determined on a case-by-case basis to see if the farmer possesses a special skill or knowledge in the marketing of grain. Where a farmer's sole connection with the grain market was the sale of his annual crop to the local grain elevators, such special skill or knowledge did not exist. Pierson v. Arnst, 534 F. Supp. 360, 39 St. Rep. 676 (D.C. Mont. 1982).

Oral "Futures" Contract Not Enforceable: The plaintiff sought damages for an alleged breach of an oral "futures" contract whereby the plaintiff agreed to purchase and the defendant farmer agreed to sell a sunflower seed crop. The contract was held unenforceable because it failed to comply with the requirement of subsection (1) that it be in writing. Subsection (2), the exception to the writing requirement, was inapplicable because the defendant farmer was not a "merchant". Pierson v. Arnst, 534 F. Supp. 360, 39 St. Rep. 676 (D.C. Mont. 1982).

Acquiescence in Modification as Precluding Defense of Statute of Frauds: The parties entered into an agreement for the installation and maintenance of a fire alarm system that was termed a "lease agreement". Payments were to be made over a 5-year term at the expiration of which defendant had the option to renew for another 5-year term or to purchase the system for $1. The original contract was rescinded, and an identical one was executed, except that payments were to begin at a later date. Defendant contended the contract was later further modified by an oral agreement to allow double payments during the summer months and no payments during some of the winter months. Plaintiff denied that this oral agreement was made, but this schedule was tolerated for 3 years. The contract was within the Statute of Frauds; however, an attempted oral modification can operate as a waiver of the right to assert the Statute of Frauds as a defense. The payment schedule followed was a sequence of conduct between the parties establishing a common basis of understanding for interpreting their expressions and conduct. As such, it constituted a course of performance, the acquiescence in which effectively modified the agreement. The Statute of Frauds defense was not applicable. Fire Supply & Serv., Inc. v. Chico Hot Springs, 196 M 435, 639 P2d 1160, 39 St. Rep. 231 (1982).

Breach of Contractual Warranties — Proper Parties — Statute of Frauds: Plaintiffs in an action for breach of express and implied warranties were farmers. Defendants manufactured farm implements. One of the plaintiffs had an arm severed in an accident involving the defendants' machinery. On appeal, the defendants argued that the injured plaintiff was not a party to the purchase contract. The plaintiff alleged the salesman knew that he and the party who actually signed the purchase order were to be co-owners of the hay baler in question. The signature was for the one co-owner for himself and as agent for the plaintiff as well. Because principal and agent law supplement the Montana UCC which covers the purchase of the baler, the court considered applying 28-10-203, which prevents oral authorization to contract when the contract itself must be written, as here. It noted exceptions to the Statute of Frauds, however. The question of whether payment of the purchase price took this contract out of the Statute of Frauds was a genuine issue of material fact preventing a summary judgment for the defendants under the Federal Rules of Civil Procedure. Holding the question one of law, the court said it had to hold an evidentiary hearing on the issues. Schlenz v. John Deere Co., 511 F. Supp. 224, 38 St. Rep. 579 (D.C. Mont. 1981).

Scope of the Statute of Frauds — Section as Applying to Sale of Registered Horses: Appellant's contention, arguing that an oral contract for the purchase and sale of five registered horses is not within the scope of the Statute of Frauds (30-2-201) and is therefore enforceable despite the lack of a writing confirming the contract, is not supportable. The transaction does not come within any of the exclusions provided for in 30-2-102. Scott v. Hjelm, 188 M 375, 613 P2d 1385, 37 St. Rep. 1219 (1980).

Statute of Frauds Not Pleaded: Defendant failed to raise the Statute of Frauds defense in his pleadings, therefore he could not maintain it on appeal. Mont. Seeds, Inc. v. Holliday, 178 M 119, 582 P2d 1223 (1978).

Exceptions — Admissions: When a party to litigation regarding an oral agreement for the sale of wheat of a value of more than $500 did not deny the existence of the agreement, the contract was valid under the "judicial admission" exception to the Statute of Frauds. Farmers Elev. Co. v. Anderson, 170 M 175, 552 P2d 63 (1976).

Oral Contract — Memorandum in Writing: When the parties made an oral agreement for the sale of wheat over the telephone, the buyer wrote a memorandum of the transaction and signed the seller's name to it, and the buyer later acknowledged the written memorandum and accepted payments under it, there was a sufficient memorandum to satisfy the Statute of Frauds. Cargill Inc. v. Wilson, 166 M 346, 532 P2d 988 (1975).

DECISIONS UNDER FORMER STATUTE OF FRAUDS

Receipt or Acceptance of Thing Sold:

Where the goods are already in the buyer's possession under a written lease, such possession is not such a receipt as required by Statute of Frauds, absent an affirmative act by the seller assenting to such receipt by the buyer. W. River Equip. Co. v. Holzworth Constr. Co., 134 M 582, 335 P2d 298 (1959).

The receipt and acceptance of property sold need not be concurrent with the time of sale, but may occur at any time thereafter. Where the buyer accepts and receives the thing sold, such acceptance and receipt by one who assumes the buyer's contract is sufficient. Slater Brick Co. v. Shackleton, 30 M 390, 76 P 805 (1904).

Complaint — Essentials of Agreement: Where complaint shows on its face that memorandum of agreement does not contain all essentials of agreement and such essentials cannot be ascertained without resort to oral evidence, demurrer to complaint was properly sustained. Dineen v. Sullivan, 123 M 195, 213 P2d 241 (1949).

Sufficiency of Note or Memorandum:
In order to take an oral contract for the sale of personal property out of the Statute of Frauds, the note or memorandum thereof referred to in section 74-201, R.C.M. 1947 (since repealed), must be so drawn that the essentials of the contract may be ascertained without resort to oral evidence, the rule being complied with if the material elements of the contract are stated in general terms. Lewis v. Aronow, 77 M 348, 251 P 146 (1926).

For the purpose of enabling the Court to interpret the abbreviations "No. 1 D. N. S." used in a memorandum evidencing the sale of wheat to a wheat buyer, where the oral contract of sale was attacked on the ground that it was void under the Statute of Frauds, parol evidence was admissible to show their customary meaning in the business of dealing in wheat. Lewis v. Aronow, 77 M 348, 251 P 146 (1926).

Part Payment:
When acceptance and receipt of a part of goods or payment of a portion of the purchase price at the time of the sale by an agent of the buyer is relied upon to take the case out of the Statute of Frauds, it must be by one having specific authority or by a general agent having all authority, and the authority of the former cannot depend upon the same oral agreement which is sought to be rendered valid by the act of the agent. Mahoney Bros. v. Hansen Packing Co., 67 M 120, 215 P 506 (1923).

In an action for breach of contract of sale of cattle where defendant company was sought to be held liable under an arrangement made over the telephone by a third person who had never been its agent and was not specifically authorized by it to act for it, and who after completion of the conversation assured the buyer that defendant would take the cattle and thereupon paid a part of the purchase price, defendant never making any payment whatever, the payment was not made by the buyer and the case was not taken out of the Statute of Frauds by such part payment. Mahoney Bros. v. Hansen Packing Co., 67 M 120, 215 P 506 (1923).

Part payment of the purchase price upon a contract for the sale of cattle brought the transaction within the exception provided for in section 74-201, R.C.M. 1947 (since repealed). Case v. Kramer, 34 M 142, 85 P 878 (1906).

Building Contract: A contract between tenants in common for the erection of a house on the common property by one at his own expense, and requiring him to make an equal division of the rents between them when the rents received equaled one-half the cost, is not within section 74-201, R.C.M. 1947 (since repealed). Ayotte v. Nadeau, 32 M 498, 81 P 145 (1905).

Burden of Proof: Where the value of property involved in a sale was sufficient to bring the contract of sale within the provisions of section 74-201, R.C.M. 1947 (since repealed), the burden is on plaintiff, in an action for breach of the contract, to establish by a preponderance of evidence that a valid contract under the statutes was entered into between the parties, together with a breach of such contract, and the consequent damages. Brophy v. Idaho Prod. & Prov. Co., 31 M 279, 78 P 493 (1904).

Valid Verbal Contract: Where a person leaves a message with a clerk, to the effect that if the plaintiff would buy in certain property to be sold under a chattel mortgage, and let a certain person buy it from him, that he would pay the plaintiff $500, and the plaintiff acted accordingly, the transaction was not within the Statute of Frauds and constituted a valid verbal contract. Frank v. Murray, 7 M 4, 14 P 654 (1887).

Law Review Articles

Electronic Contracting Under the 2003 Revisions to Article 2 of the Uniform Commercial Code: Clarification or Chaos?, Daniel, 20 Santa Clara Computer & High Tech. L.J. 319 (2004).

30-2-202. Final written expression — parol or extrinsic evidence.

Official Comment

Prior Uniform Statutory Provision: None.

Purposes:

1. This section definitely rejects:

(a) Any assumption that because a writing has been worked out which is final on some matters, it is to be taken as including all the matters agreed upon;

(b) The premise that the language used has the meaning attributable to such language by rules of construction existing in the law rather than the meaning which arises out of the commercial context in which it was used; and

(c) The requirement that a condition precedent to the admissibility of the type of evidence specified in paragraph (a) is an original determination by the court that the language used is ambiguous.

2. Paragraph (a) makes admissible evidence of course of dealing, usage of trade and course of performance to explain or supplement the terms of any writing stating the agreement of the parties in order that the true understanding of the parties as to the agreement may be reached. Such writings are to be read on the assumption that the course of prior dealings between the parties and the usages of trade were taken for granted when the document was phrased. Unless carefully negated they have become an element of the meaning of the words used. Similarly, the course of actual performance by the parties is considered the best indication of what they intended the writing to mean.

3. Under paragraph (b) consistent additional terms, not reduced to writing, may be proved unless the court finds that the writing was intended by both parties as a complete and exclusive statement of all the terms. If the additional terms are such that, if agreed upon, they would certainly have been included in the document in the view of the court, then evidence of their alleged making must be kept from the trier of fact.

Case Notes

Statute of Frauds and Parol Evidence Rule Not Bar to Alleged Oral Contract — Genuine Issue of Material Fact Regarding Intent — Written Agreement Did Not Clearly Evidence Final Expression — Uniform Commercial Code Applied: The District Court did not err in denying the defendant's motion for summary judgment based on the defendant's assertion that an alleged oral contract was barred by the statute of frauds or the parol evidence rule. The agreement between the parties involved the sale of brake linings from the defendant to the plaintiff and the sale of remanufactured brakes from the plaintiff to another party. The brake linings and remanufactured brakes constituted moveable goods under 30-2-105, making the alleged oral contract within the ambit of the Montana Uniform Commercial Code's statute of frauds provision in 30-2-201. Because the parties entered into a written agreement and one party asserted the existence of an additional oral contract, the parol evidence rule provided for in 30-2-202 was applied. After the District Court made an initial determination under 30-2-202 that the program agreement did not clearly evidence a final expression of the parties' agreement, it properly denied summary judgment and allowed the jury to consider evidence to elucidate the true nature of the parties' agreement. S & P Brake Supply, Inc. v. STEMCO LP, 2016 MT 324, 385 Mont. 488, 385 P.3d 567, following Norwest Bank Billings v. Murnion, 210 Mont. 417, 684 P.2d 1067 (1984).

Error in Failing to Consider Estoppel Related to Waiver of Right to Declare Contract Forfeiture — Summary Judgment Improper: When plaintiffs began experiencing financial problems, they notified defendants that they would not be able to make the annual payment on their property. Defendants allegedly told plaintiffs that they would have whatever time they needed to come up with the money, as long as they paid any additional interest and other expenses. Defendants subsequently sent plaintiffs a default notice and terminated the contract for deed. Plaintiffs contended that defendants waived the right to terminate the contract and should be estopped from forfeiting the contract. The District Court dismissed the waiver and estoppel arguments as an attempt to offer parol evidence to amend the contract and granted summary judgment to defendants. However, plaintiffs were not trying to amend the contract, but rather were simply trying to show that defendants waived the right to foreclose for at least a period of time, that plaintiffs relied on the waiver, and that defendants should be estopped from foreclosure. Because material questions remained as to whether a waiver occurred, summary judgment was improper and the case was remanded for further proceedings. Danelson v. Robinson, 2003 MT 271, 317 M 462, 77 P3d 1010 (2003).

Contract for Elk Sale — Telephone Conversations Occurring After Contract Admissible — Oral Agreement Extending Contract Cutoff Dates Inadmissible but Promise Enforced: Seller appealed a District Court judgment awarding buyer damages after seller breached contracts for the sale of elk. Seller entered into contracts agreeing to deliver elk before April 1 and May 1 and in subsequent telephone conversations promised to deliver elk after these contract cutoff dates. While the parol evidence rule bars prior or contemporaneous oral agreements, the Supreme Court affirmed the District Court decision allowing testimony regarding telephone conversations that occurred after the written agreements. The buyer, to his detriment, entered into third-party contracts to resell the elk in reliance on the seller's promise that the elk would be available and delivered after the contract cutoff dates. The Supreme Court ruled that enforcing the oral agreement extending the cutoff dates of the contract avoided an injustice to the buyer. Trad Indus., Ltd. v. Brogan, 246 M 439, 805 P2d 54, 48 St. Rep. 51 (1991).

Improper Reliance on Statute as Parol Evidence Instruction: A jury instruction that used this section as a source was properly refused upon a finding that a "written agreement" was merely a purchase order for goods and made no reference to additional promises made by the seller. The purchase order was not intended to be a final expression of the agreement, and a parol evidence instruction disallowing evidence of any prior agreement or contemporaneous agreement was improper. Webcor Electronics, Inc. v. Home Electronics, Inc., 231 M 377, 754 P2d 491, 45 St. Rep. 695 (1988).

Unambiguous Contract Description — Applicability of Parol Evidence Rule — Unilateral Mistake: Since a 1971 written agreement was not ambiguous with respect to the land it affected, the parol evidence rule prevented admission of evidence of a 1967 oral agreement to show intent of the parties as to what land was involved. Admission of the oral agreement would only have provided evidence of unilateral mistake, which is not grounds for reforming a written contract. Haggerty v. Gallatin County, 221 M 109, 717 P2d 550, 43 St. Rep. 674 (1986).

Final Expression of Agreement Implied: The lower court found that buyer, seller, and bank, which was seller's assignee with full recourse, had agreed to the terms stated in a written contract and that buyer's promise to pay was stated in plain and unequivocal terms and referred to no antecedent or contemporaneous agreement not reduced to writing. By implication, the court indicated that there was an appropriate degree of finality respecting the terms of the written contract. Norwest Bank Billings v. Murnion, 210 M 417, 684 P2d 1067, 41 St. Rep. 1132 (1984).

Parol Evidence Rules Substantive, Not Procedural — Subject to Rules of Evidence and Common-Law Exceptions: The Montana Uniform Commercial Code's parol evidence rule contained in 30-2-202 continues the operation of the traditional law of contracts parol evidence rule, though with some modifications. Each is a principle of substantive law, not a procedural rule of evidence. Thus, the admissibility of any evidence is ultimately subject to the provisions of the Montana Rules of Evidence, and the traditional common-law exceptions to the contract law parol evidence rule, such as proof of fraud, misrepresentation, or mistake, remain exceptions to the parol evidence rule in the Montana Uniform Commercial Code. Norwest Bank Billings v. Murnion, 210 M 417, 684 P2d 1067, 41 St. Rep. 1132 (1984). See also Webcor Electronics, Inc. v. Home Electronics, Inc., 231 M 377, 754 P2d 491, 45 St. Rep. 695 (1988).

Partial Final Expression of Agreement — Inclusion of Entire Agreement Not Implied: Evidence that a writing is final as to some matters must not necessarily be construed to mean that the writing must be taken as including all the matters on which agreed. Norwest Bank Billings v. Murnion, 210 M 417, 684 P2d 1067, 41 St. Rep. 1132 (1984).

Sale of Front-End Loader — Applicable Parol Evidence Rule: Front-end loader that buyer purchased from seller was within the definition of "goods" set out in 30-2-105. Therefore, the sale was governed by the Montana Uniform Commercial Code, and any Code provisions addressing a parol evidence question controlled the answer to the question, with the contract law parol evidence rule of 28-2-904 being used only to supplement the Code. Norwest Bank Billings v. Murnion, 210 M 417, 684 P2d 1067, 41 St. Rep. 1132 (1984).

Written Promise to Pay — Contradicted by Oral Agreement Excusing Payment: Alleged contemporaneous oral agreement excusing buyer from paying for front-end loader he purchased to the extent of any deficiency due under the written contract, primarily because of alleged misrepresentations of the seller regarding the loader, was inadmissible under the Uniform Commercial Code's parol evidence rule as a matter of law because it definitely contradicted the clear promise to pay stated in the written contract. In addition, the buyer's testimony was uncorroborated and contradictory and could be excluded on that ground and was hearsay testimony and could also be excluded on that ground. Norwest Bank Billings v. Murnion, 210 M 417, 684 P2d 1067, 41 St. Rep. 1132 (1984).

Parol Evidence on Month and Day of Contract Admissible Where Parties Themselves Presented Parol Evidence on Year of Contract: Buyer failed to pay entire purchase price for irrigation system, and seller sued. Since buyer counterclaimed for crop losses allegedly resulting from seller's failure to install system within a reasonable time of contract, the exact date of the contract was an issue at trial. Seller submitted a copy of the contract dated May 20, 1976. Both parties agreed that the year was incorrect, as the transaction had actually taken place in 1977. However, the buyer claimed that the contract had been made in April, not May, and the District Court permitted him to present evidence in support of this. Seller appealed, claiming it was improper to allow the admission of parol evidence in contradiction of the terms of the contract. The Supreme Court held that since parol evidence had been allowed on the year of the contract, it was allowable for the month and day also. Ag Sales v. Klose, 199 M 400, 649 P2d 447, 39 St. Rep. 1482 (1982).

Documents Incorporated as Contract — Waiver of Condition Precedent: Plaintiff negotiated to sell two-wheel loaders to defendant. The terms of the sale were contained on the purchase order and included a 30-day warranty. Later, a lease agreement covering the same equipment was executed with plaintiff as lessor and defendant as lessee. One of the loaders broke down and required repair. Plaintiff contended the date of the warranty was from the date the purchase order was executed. Defendant refused to pay for the repair, contending the warranty began on the date of the lease agreement. Plaintiff claimed breach and took possession of the loaders. By its own admission, plaintiff conceded that the initial agreement was transformed into the lease agreement. This in effect was a modification of the contract. The terms contained in the purchase order were incorporated into and became part of the lease agreement. The two writings together constituted the final written expression of the agreement. The terms were unambiguous and could not be contradicted by evidence of any prior agreement. Plaintiff was responsible for repair under the warranty provision. Defendant contended refusal to honor this warranty constituted breach of the agreement, while plaintiff contended that a provision for advance payment, not rendered by defendant, was a condition precedent to the formation of the lease contract. The only logical interpretation of the events which transpired was that plaintiff waived the advance payment by delivering the loaders prior to receipt of the payment. Plaintiff could not rely on failure to receive the advance payment in claiming breach of contract under 30-2-706. Defendant was entitled to summary judgment. Westmont Tractor Co. v. Viking Exploration, Inc., 543 F. Supp. 1314, 39 St. Rep. 1398 (D.C. Mont. 1982).

Sale of a Business Not Within Scope of Section: In the sale of a barber shop, parol evidence that the parties intended to include goodwill in the purchase price is not admissible under 30-2-202. This section of the Uniform Commercial Code is applicable only to the sale of "goods" and affords plaintiff no relief upon the sale of a business. Baldwin v. Stuber, 182 M 501, 597 P2d 1135 (1979).

Waiver of Parol Evidence Rule: Assignee's failure to object to the admission of parol evidence regarding assignor's prior oral promise to repair, establishing a breach and rendering unenforceable buyer's contract with assignor in failing to perform promise to repair renders such evidence admissible because an objection to the admission of parol evidence is waived when no effort is made to preserve it at the time it is offered. Massey-Ferguson Credit Corp. v. Brown, 169 M 396, 547 P2d 846 (1976).

Relation to Other Statutes: Section 28-3-602, which provides that time is not considered of the essence in a contract unless such a provision is expressly provided, was more specific than this section and controlled to prohibit parol evidence regarding the delivery date under an agreement for purchase and sale. Martel Constr., Inc. v. Gleason Equip., Inc., 166 M 479, 534 P2d 883 (1975).

Law Review Articles

A Picture Imperfect: The Rights of Art Consignor-Collectors When Their Art Dealer Files for Bankruptcy, Jay, 58 Duke L.J. 1859 (2009).

30-2-203. Seals inoperative.

Official Comment

Prior Uniform Statutory Provision: Section 3, Uniform Sales Act.

Changes: Portion pertaining to "seals" rewritten.

Purposes of Changes:

1. This section makes it clear that every effect of the seal which relates to "sealed instruments" as such is wiped out insofar as contracts for sale are concerned. However, the substantial effects of a seal, except extension of the period of limitations, may be had by appropriate drafting as in the case of firm offers (see Section 30-2-205).

2. This section leaves untouched any aspects of a seal which relate merely to signatures or to authentication of execution and the like. Thus, a statute providing that a purported signature gives prima facie evidence of its own authenticity or that a signature gives prima facie evidence of consideration is still applicable to sales transactions even though a seal may be held to be a signature within the meaning of such a statute. Similarly, the authorized affixing of a corporate seal bearing the corporate name to a contractual writing purporting to be made by the corporation may have effect as a signature without any reference to the law of sealed instruments.

30-2-204. Formation in general.

Official Comment

Prior Uniform Statutory Provision: Sections 1 and 3, Uniform Sales Act.

Changes: Completely rewritten by this and other sections of this Chapter.

Purposes of Changes:

Subsection (1) continues without change the basic policy of recognizing any manner of expression of agreement, oral, written or otherwise. The legal effect of such an agreement is, of course, qualified by other provisions of this Chapter.

Under subsection (1) appropriate conduct by the parties may be sufficient to establish an agreement. Subsection (2) is directed primarily to the situation where the interchanged correspondence does not disclose the exact point at which the deal was closed, but the actions of the parties indicate that a binding obligation has been undertaken.

Subsection (3) states the principle as to "open terms" underlying later sections of the Chapter. If the parties intend to enter into a binding agreement, this subsection recognizes that agreement as valid in law, despite missing terms, if there is any reasonably certain basis for granting a remedy. The test is not certainty as to what the parties were to do nor as to the exact amount of damages due the plaintiff. Nor is the fact that one or more terms are left to be agreed upon enough of itself to defeat an otherwise adequate agreement. Rather, commercial standards on the point of "indefiniteness" are intended to be applied, this Act making provision elsewhere for missing terms needed for performance, open price, remedies and the like.

The more terms the parties leave open, the less likely it is that they have intended to conclude a binding agreement, but their actions may be frequently conclusive on the matter despite the omissions.

Case Notes

Son of Sole Shareholder Signed for Purchases — Ostensible Agent — Binding Contract Formed: A fertilizer company sued the defendants, a Montana corporation and its sole shareholder, for a past due account on the purchase of its goods. The shareholder's son had signed for the goods, and the defendants alleged there was no binding contract between the parties because the son did not have the authority to bind the corporation. The District Court disagreed and issued an order in favor of the plaintiff. On appeal, the Supreme Court affirmed, agreeing that the son was the ostensible agent of the defendant corporation and that a binding contract therefore existed between the parties. Fitterer Sales Montana, Inc. v. Mullin, 2015 MT 272, 381 Mont. 107, 358 P.3d 885.

30-2-205. Firm offers.

Official Comment

Prior Uniform Statutory Provision: Sections 1 and 3, Uniform Sales Act.

Changes: Completely rewritten by this and other sections of this Chapter.

Purposes of Changes:

1. This section is intended to modify the former rule which required that "firm offers" be sustained by consideration in order to bind, and to require instead that they must merely be characterized as such and expressed in signed writings.

2. The primary purpose of this section is to give effect to the deliberate intention of a merchant to make a current firm offer binding. The deliberation is shown in the case of an individualized document by the merchant's signature to the offer, and in the case of an offer included on a form supplied by the other party to the transaction by the separate signing of the particular clause which contains the offer. "Signed" here also includes authentication but the reasonableness of the authentication herein allowed must be determined in the light of the purpose of the section. The circumstances surrounding the signing may justify something less than a formal signature or initialing but typically the kind of authentication involved here would consist of a minimum of initialing of the clause involved. A handwritten memorandum on the writer's letterhead purporting in its terms to "confirm" a firm offer already made would be enough to satisfy this section, although not subscribed, since under the circumstances it could not be considered a memorandum of mere negotiation and it would adequately show its own authenticity. Similarly, an authorized telegram will suffice, and this is true even though the original draft contained only a typewritten signature. However, despite settled courses of dealing or usages of the trade whereby firm offers are made by oral communication and relied upon without more evidence, such offers remain revocable under this Chapter since authentication by a writing is the essence of this section.

3. This section is intended to apply to current "firm" offers and not to long term options, and an outside time limit of three months during which such offers remain irrevocable has been set. The three month period during which firm offers remain irrevocable under this section need not be stated by days or by date. If the offer states that it is "guaranteed" or "firm" until the happening of a contingency which will occur within the three month period, it will remain irrevocable until that event. A promise made for a longer period will operate under this section to bind the offeror only for the first three months of the period but may of course be renewed. If supported by consideration it may continue for as long as the parties specify. This section deals only with the offer which is not supported by consideration.

4. Protection is afforded against the inadvertent signing of a firm offer when contained in a form prepared by the offeree by requiring that such a clause be separately authenticated. If the offer clause is called to the offeror's attention and he separately authenticates it, he will be bound; Section 30-2-302 may operate, however, to prevent an unconscionable result which otherwise would flow from other terms appearing in the form.

5. Safeguards are provided to offer relief in the case of material mistake by virtue of the requirement of good faith and the general law of mistake.

Case Notes

Failure to Notify Grain Buyer of Intent to Breach Oral Agreement Within Reasonable Time — Oral Contract Enforceable: ConAgra, Inc. (ConAgra), contended that it had an oral telephone contract with Nierenberg to purchase 12,500 bushels of wheat and filed an action to recover losses incurred when Nierenberg sold the wheat to someone else, requiring ConAgra to purchase other wheat for resale at a higher price to fulfill its sale obligations pursuant to its purchase of Nierenberg's wheat. The District Court determined that Nierenberg was a merchant within the context of the Uniform Commercial Code and that, although both parties were merchants, the written sale confirmation received by Nierenberg 10 days after the telephone conversation was not within a reasonable time. Nierenberg never objected in writing to the written confirmation. The Supreme Court noted that the merchant exception in 30-2-201 does not dictate which party must send the written confirmation, but rather that in order to create an enforceable oral contract and avoid the signed writing requirement, one of the parties must send written confirmation to the other party. A farmer as well as a buyer may lock in an oral contract price as the market fluctuates up or down, and both parties equally possess the power to bind the other party. In this case, ConAgra did not immediately mail a written agreement, but instead waited about 6 days for Nierenberg to come to the elevator and sign the contract in person before mailing it. Although a court must look at the broad nature, purpose, and circumstances in determining whether written confirmation was received within a reasonable time, two specific factors may be examined: (1) the merchant's usual practice or policy following such transactions; and (2) the merchant's excuse for not following its practice or policy. The slight delay in Nierenberg's receipt of the confirmation because of an apparent misunderstanding was not seen as an unreasonable deviation from ConAgra's usual practices under the circumstances. However, Nierenberg chose to simply not honor his contractual obligation without notifying ConAgra of his true intentions. Nierenberg's mistake was to act outside of accepted commercial grain sales practices and not give ConAgra prompt notice of his breach so that his obligation for expectancy damages would be fixed. The written confirmation became an enforceable binding contract when Nierenberg failed to respond in writing with his objections within the stated 10-day period. The Supreme Court reversed the District Court's finding that the oral agreement could not be enforced. ConAgra, Inc. v. Nierenberg, 2000 MT 213, 301 M 55, 7 P3d 369, 57 St. Rep. 842 (2000).

Rules for Determining Whether Judicial Admission Made to Establish Oral Contract for Sale of Grain: ConAgra, Inc. (ConAgra), contended that it had an oral telephone contract with Nierenberg to purchase 12,500 bushels of wheat and filed an action to recover losses incurred when Nierenberg sold the wheat to someone else, requiring ConAgra to purchase other wheat for resale at a higher price to fulfill its sale obligations pursuant to its purchase of Nierenberg's wheat. The District Court determined that Nierenberg was a merchant within the context of the Uniform Commercial Code, based on the fact that Nierenberg had been selling grain for many years and was familiar with grain prices through periodic visits to local grain elevators. The court also concluded that, although both parties were merchants, the written sale confirmation received by Nierenberg 10 days after the telephone conversation was not within a reasonable time. Noting that the rules governing sales agreements under the Uniform Commercial Code are far more permissive than general contract rules under the common law, the Supreme Court found that the District Court erred in determining that a contract was not formed because Nierenberg did not unambiguously testify to the necessary elements of a contract. Under 30-2-201, a contract that does not satisfy the signed writing requirements, but that is valid in other respects, is enforceable if the party against whom enforcement is sought admits that a contract for sale was made. For a judicial admission to be binding, the admission must be an unequivocal statement of fact rather than a conclusion of law or the expression of an opinion. Prodding a party while on the witness stand or while testifying during a deposition to say certain magical words that may indicate that a contract was formed will be viewed with disfavor. Instead, the Supreme Court cited Thomas v. Prewitt, 355 S2d 657 (Miss. 1978), for the five-part rule for testing the sufficiency of a claimed judicial admission: (1) the declaration relied on was made during the course of a judicial proceeding; (2) the statement was contradictory to an essential fact embraced in the theory of recovery or defense asserted by the person giving the testimony; (3) the statement was deliberate, clear, and unequivocal; (4) giving of conclusive effect to the declaration is consistent with public policy; and (5) the testimony must be such as relates to a fact upon which a judgment for the opposing party may be based. The Supreme Court's review will adhere to the outward objective manifestations test expressed in Miller v. Walter, 165 M 221, 527 P2d 240 (1974), namely whether intent that a contract existed must be gathered from the outward objective manifestations of the parties and not by the subjective undisclosed intent of one of the parties. In Nierenberg's case, his testimony indicated that most of his grain sales involved signing a contract shortly after oral discussions with ConAgra—an apparent contradiction to an outright admission that he was orally bound to sell the grain. The fact that Nierenberg was willing to further negotiate the quantity of grain was not the objective conduct of a person who was contractually bound without a signed writing. The testimonial facts concerning Nierenberg's postphone conversation conduct were ambiguous, and the District Court did not err in holding that Nierenberg did not make a judicial admission that a contract was made, even though that conclusion was not dispositive of the ultimate determination of whether an enforceable contract was made. ConAgra, Inc. v. Nierenberg, 2000 MT 213, 301 M 55, 7 P3d 369, 57 St. Rep. 842 (2000).

Offer to Buy: Tender to a farmer of a copy of a standard grain purchase contract, executed by a dealer, constituted at least an offer by the dealer to buy the stated quantity of grain from the farmer. Cargill Inc. v. Wilson, 166 M 346, 532 P2d 988 (1975).

30-2-206. Offer and acceptance in formation of contract.

Official Comment

Prior Uniform Statutory Provision: Sections 1 and 3, Uniform Sales Act.

Changes: Completely rewritten in this and other sections of this Chapter.

Purposes of Changes: To make it clear that:

1. Any reasonable manner of acceptance is intended to be regarded as available unless the offeror has made quite clear that it will not be acceptable. Former technical rules as to acceptance, such as requiring that telegraphic offers be accepted by telegraphed acceptance, etc., are rejected and a criterion that the acceptance be "in any manner and by any medium reasonable under the circumstances," is substituted. This section is intended to remain flexible and its applicability to be enlarged as new media of communication develop or as the more time-saving present day media come into general use.

2. Either shipment or a prompt promise to ship is made a proper means of acceptance of an offer looking to current shipment. In accordance with ordinary commercial understanding the section interprets an order looking to current shipment as allowing acceptance either by actual shipment or by a prompt promise to ship and rejects the artificial theory that only a single mode of acceptance is normally envisaged by an offer. This is true even though the language of the offer happens to be "ship at once" or the like. "Shipment" is here used in the same sense as in Section 30-2-504; it does not include the beginning of delivery by the seller's own truck or by messenger. But loading on the seller's own truck might be a beginning of performance under subsection (2).

3. The beginning of performance by an offeree can be effective as acceptance so as to bind the offeror only if followed within a reasonable time by notice to the offeror. Such a beginning of performance must unambiguously express the offeree's intention to engage himself. For the protection of both parties it is essential that notice follow in due course to constitute acceptance. Nothing in this section however bars the possibility that under the common law performance begun may have an intermediate effect of temporarily barring revocation of the offer, or at the offeror's option, final effect in constituting acceptance.

4. Subsection (1)(b) deals with the situation where a shipment made following an order is shown by a notification of shipment to be referable to that order but has a defect. Such a non-conforming shipment is normally to be understood as intended to close the bargain, even though it proves to have been at the same time a breach. However, the seller by stating that the shipment is non-conforming and is offered only as an accommodation to the buyer keeps the shipment or notification from operating as an acceptance.

Case Notes

Failure to Notify Grain Buyer of Intent to Breach Oral Agreement Within Reasonable Time — Oral Contract Enforceable: ConAgra, Inc. (ConAgra), contended that it had an oral telephone contract with Nierenberg to purchase 12,500 bushels of wheat and filed an action to recover losses incurred when Nierenberg sold the wheat to someone else, requiring ConAgra to purchase other wheat for resale at a higher price to fulfill its sale obligations pursuant to its purchase of

Nierenberg's wheat. The District Court determined that Nierenberg was a merchant within the context of the Uniform Commercial Code and that, although both parties were merchants, the written sale confirmation received by Nierenberg 10 days after the telephone conversation was not within a reasonable time. Nierenberg never objected in writing to the written confirmation. The Supreme Court noted that the merchant exception in 30-2-201 does not dictate which party must send the written confirmation, but rather that in order to create an enforceable oral contract and avoid the signed writing requirement, one of the parties must send written confirmation to the other party. A farmer as well as a buyer may lock in an oral contract price as the market fluctuates up or down, and both parties equally possess the power to bind the other party. In this case, ConAgra did not immediately mail a written agreement, but instead waited about 6 days for Nierenberg to come to the elevator and sign the contract in person before mailing it. Although a court must look at the broad nature, purpose, and circumstances in determining whether written confirmation was received within a reasonable time, two specific factors may be examined: (1) the merchant's usual practice or policy following such transactions; and (2) the merchant's excuse for not following its practice or policy. The slight delay in Nierenberg's receipt of the confirmation because of an apparent misunderstanding was not seen as an unreasonable deviation from ConAgra's usual practices under the circumstances. However, Nierenberg chose to simply not honor his contractual obligation without notifying ConAgra of his true intentions. Nierenberg's mistake was to act outside of accepted commercial grain sales practices and not give ConAgra prompt notice of his breach so that his obligation for expectancy damages would be fixed. The written confirmation became an enforceable binding contract when Nierenberg failed to respond in writing with his objections within the stated 10-day period. The Supreme Court reversed the District Court's finding that the oral agreement could not be enforced. ConAgra, Inc. v. Nierenberg, 2000 MT 213, 301 M 55, 7 P3d 369, 57 St. Rep. 842 (2000).

Rules for Determining Whether Judicial Admission Made to Establish Oral Contract for Sale of Grain: ConAgra, Inc. (ConAgra), contended that it had an oral telephone contract with Nierenberg to purchase 12,500 bushels of wheat and filed an action to recover losses incurred when Nierenberg sold the wheat to someone else, requiring ConAgra to purchase other wheat for resale at a higher price to fulfill its sale obligations pursuant to its purchase of Nierenberg's wheat. The District Court determined that Nierenberg was a merchant within the context of the Uniform Commercial Code, based on the fact that Nierenberg had been selling grain for many years and was familiar with grain prices through periodic visits to local grain elevators. The court also concluded that, although both parties were merchants, the written sale confirmation received by Nierenberg 10 days after the telephone conversation was not within a reasonable time. Noting that the rules governing sales agreements under the Uniform Commercial Code are far more permissive than general contract rules under the common law, the Supreme Court found that the District Court erred in determining that a contract was not formed because Nierenberg did not unambiguously testify to the necessary elements of a contract. Under 30-2-201, a contract that does not satisfy the signed writing requirements, but that is valid in other respects, is enforceable if the party against whom enforcement is sought admits that a contract for sale was made. For a judicial admission to be binding, the admission must be an unequivocal statement of fact rather than a conclusion of law or the expression of an opinion. Prodding a party while on the witness stand or while testifying during a deposition to say certain magical words that may indicate that a contract was formed will be viewed with disfavor. Instead, the Supreme Court cited Thomas v. Prewitt, 355 S2d 657 (Miss. 1978), for the five-part rule for testing the sufficiency of a claimed judicial admission: (1) the declaration relied on was made during the course of a judicial proceeding; (2) the statement was contradictory to an essential fact embraced in the theory of recovery or defense asserted by the person giving the testimony; (3) the statement was deliberate, clear, and unequivocal; (4) giving of conclusive effect to the declaration is consistent with public policy; and (5) the testimony must be such as relates to a fact upon which a judgment for the opposing party may be based. The Supreme Court's review will adhere to the outward objective manifestations test expressed in Miller v. Walter, 165 M 221, 527 P2d 240 (1974), namely whether intent that a contract existed must be gathered from the outward objective manifestations of the parties and not by the subjective undisclosed intent of one of the parties. In Nierenberg's case, his testimony indicated that most of his grain sales involved signing a contract shortly after oral discussions with ConAgra—an apparent contradiction to an outright admission that he was orally bound to sell the grain. The fact that Nierenberg was willing to further negotiate the quantity of grain was not the objective conduct of a person who was contractually bound without a signed writing. The testimonial facts concerning Nierenberg's postphone conversation conduct were ambiguous, and the District Court did not err in holding that Nierenberg did not make a judicial admission that a contract was made, even though that conclusion was not dispositive of the ultimate determination of whether an enforceable contract was made. ConAgra, Inc. v. Nierenberg, 2000 MT 213, 301 M 55, 7 P3d 369, 57 St. Rep. 842 (2000).

Jury Instruction Based on Statute Inapplicable: The trial court correctly refused to advise the jury on when an agreement could arise by performance because the contention was not whether a contract was entered into to buy goods, but rather that defendant made untrue oral representations that caused plaintiffs to enter into an agreement they would not otherwise have entered. Webcor Electronics, Inc. v. Home Electronics, Inc., 231 M 377, 754 P2d 491, 45 St. Rep. 695 (1988).

Acceptance of Offer: Farmer accepted dealer's offer to buy stated quantity of grain by receiving without objection an executed copy of standard grain purchase contract, by receiving and endorsing an advance payment check to which was attached a memorandum referring by number to the grain purchase contract, and by failing to object for 4 months to quantity stated. Cargill Inc. v. Wilson, 166 M 346, 532 P2d 988 (1975).

30-2-207. Additional terms in acceptance or confirmation.

Official Comment

Prior Uniform Statutory Provision: Sections 1 and 3, Uniform Sales Act.

Changes: Completely rewritten by this and other sections of this Chapter.

Purposes of Changes:

1. This section is intended to deal with two typical situations. The one is the written confirmation, where an agreement has been reached either orally or by informal correspondence between the parties and is followed by one or both of the parties sending formal memoranda embodying the terms so far as agreed upon and adding terms not discussed. The other situation is offer and acceptance, in which a wire or letter expressed and intended as an acceptance or the closing of an agreement adds further minor suggestions or proposals such as "ship by Tuesday," "rush," "ship draft against bill of lading inspection allowed," or the like. A frequent example of the second situation is the exchange of printed purchase order and acceptance (sometimes called "acknowledgment") forms. Because the forms are oriented to the thinking of the respective drafting parties, the terms contained in them often do not correspond. Often the seller's form contains terms different from or additional to those set forth in the buyer's form. Nevertheless, the parties proceed with the transaction.

2. Under this Chapter a proposed deal which in commercial understanding has in fact been closed is recognized as a contract. Therefore, any additional matter contained in the confirmation or in the acceptance falls within subsection (2) and must be regarded as a proposal for an added term unless the acceptance is made conditional on the acceptance of the additional or different terms.

3. Whether or not additional or different terms will become part of the agreement depends upon the provisions of subsection (2). If they are such as materially to alter the original bargain, they will not be included unless expressly agreed to by the other party. If, however, they are terms which would not so change the bargain they will be incorporated unless notice of objection to them has already been given or is given within a reasonable time.

4. Examples of typical clauses which would normally "materially alter" the contract and so result in surprise or hardship if incorporated without express awareness by the other party are: a clause negating such standard warranties as that of merchantability or fitness for a particular purpose in circumstances in which either warranty normally attaches; a clause requiring a guaranty of 90% or 100% deliveries in a case such as a contract by cannery, where the usage of the trade allows greater quantity leeways; a clause reserving to the seller the power to cancel upon the buyer's failure to meet any invoice when due; a clause requiring that complaints be made in a time materially shorter than customary or reasonable.

5. Examples of clauses which involve no element of unreasonable surprise and which therefore are to be incorporated in the contract unless notice of objection is seasonably given are: a clause setting forth and perhaps enlarging slightly upon the seller's exemption due to supervening causes beyond his control, similar to those covered by the provision of this Chapter on merchant's excuse by failure of presupposed conditions or a clause fixing in advance any reasonable formula of proration under such circumstances; a clause fixing a reasonable time for complaints within customary limits, or in the case of a purchase for sub-sale, providing for inspection by the sub-purchaser; a clause providing for interest on overdue invoices or fixing the seller's standard credit terms where they are within the range of trade practice and do not limit

any credit bargained for; a clause limiting the right of rejection for defects which fall within the customary trade tolerances for acceptance "with adjustment" or otherwise limiting remedy in a reasonable manner (see Sections 30-2-718 and 30-2-719).

6. If no answer is received within a reasonable time after additional terms are proposed, it is both fair and commercially sound to assume that their inclusion has been assented to. Where clauses on confirming forms sent by both parties conflict each party must be assumed to object to a clause of the other conflicting with one on the confirmation sent by himself. As a result the requirement that there be notice of objection which is found in subsection (2) is satisfied and the conflicting terms do not become a part of the contract. The contract then consists of the terms originally expressly agreed to, terms on which the confirmations agree, and terms supplied by this Act, including subsection (2). The written confirmation is also subject to Section 30-2-201. Under that section a failure to respond permits enforcement of a prior oral agreement; under this section a failure to respond permits additional terms to become part of the agreement.

7. In many cases, as where goods are shipped, accepted and paid for before any dispute arises, there is no question whether a contract has been made. In such cases, where the writings of the parties do not establish a contract, it is not necessary to determine which act or document constituted the offer and which the acceptance. See Section 30-2-204. The only question is what terms are included in the contract, and subsection (3) furnishes the governing rule.

Compiler's Comments

1983 Amendment: Near beginning of (2), inserted "or different" after "The additional".

Unofficial Amendment: The 1983 amendment to this section was not an official amendment to the Uniform Commercial Code drafted by the National Conference of Commissioners on Uniform State Laws.

Case Notes

Jury Instruction Based on Statute Inapplicable: The trial court correctly refused to advise the jury on when additional terms become part of a contract because there was no claim that defendant's alleged untrue oral representations were additional terms within the meaning of this section. Webcor Electronics, Inc. v. Home Electronics, Inc., 231 M 377, 754 P2d 491, 45 St. Rep. 695 (1988).

Exchange of Purchase Order and Acknowledgment: Defendant Volk, by purchase order dated December 1, 1977, made an offer to Morin, which Morin accepted on December 5, 1977. A confirmation document was also signed by Morin dated January 5, 1978. Volk's terms of sale became part of the subsequent contract with the additional term that materials supplied be in accordance with Morin's proposal document. No other material terms contained in Morin's proposal became part of the contract between the parties. Morin Bldg. Prod. Co., Inc. v. Volk Constr., Inc., 500 F. Supp. 82, 37 St. Rep. 1803 (D.C. Mont. 1980).

Contract for Scrap Metal — Alteration of Writing: Where plaintiff and defendant entered into a written contract under which the defendant was to purchase scrap auto bodies from the plaintiff and defendant struck certain terms of the proposed contract relating to the weight of truckloads to be delivered and termination of the contract but accepted delivery of some of the scrap auto bodies without a response from the plaintiff approving or disapproving the stricken contract terms, both parties by their conduct recognized the existence of a binding contract. Weissman & Sons, Inc. v. Pepper, 480 F. Supp. 1364 (D.C. Mont. 1979).

Law Review Articles

A Comparative Analysis of the "Battle of the Forms", Stemp, 15 Transnat'l L. & Contemp. Probs. 243 (2005).

30-2-208. Course of performance or practical construction.

Official Comment

Prior Uniform Statutory Provision: No such general provision but concept of this section recognized by terms such as "course of dealing", "the circumstances of the case," "the conduct of the parties," etc., in Uniform Sales Act.

Purposes:

1. The parties themselves know best what they have meant by their words of agreement and their action under that agreement is the best indication of what that meaning was. This section thus rounds out the set of factors which determines the meaning of the "agreement" and therefore also of the "unless otherwise agreed" qualification to various provisions of this Chapter.

2. Under this section a course of performance is always relevant to determine the meaning of the agreement. Express mention of course of performance elsewhere in this Chapter carries no contrary implication when there is a failure to refer to it in other sections.

3. Where it is difficult to determine whether a particular act merely sheds light on the meaning of the agreement or represents a waiver of a term of the agreement, the preference is in favor of "waiver" whenever such construction, plus the application of the provisions on the reinstatement of rights waived (see Section 30-2-209), is needed to preserve the flexible character of commercial contracts and to prevent surprise or other hardship.

4. A single occasion of conduct does not fall within the language of this section but other sections such as the ones on silence after acceptance and failure to specify particular defects can affect the parties' rights on a single occasion (see Sections 30-2-605 and 30-2-607).

Case Notes

Sales — Guaranty of Buyer's Payment by Guarantor's Agent: Jacobs sold the uniform sales part of his business to K&M Sports, which in turn sold it to another, who defaulted on the sale. Jacobs, as secured party, repossessed the inventory and sold it to Snick Sports. Dirkson, who worked for K&M and then Snick, told Powers, plaintiff, that Jacobs would guarantee Snick's payment of goods sold to Snick by Powers. There was disagreement as to whether Dirkson worked for Jacobs. For 2 years Powers mailed merchandise, statements, and invoices to Jacobs, who forwarded them to Snick, who paid the bills. When some bills went unpaid, Powers sued Jacobs when he failed to pay the bills on request. The mailings to Jacobs put him on reasonable notice that something was wrong. His failure to investigate and take action was want of ordinary care that caused or allowed Powers to believe an authorized agency existed between Jacobs and Dirkson. Thus, there was an ostensible agency and ostensible authority. For the same reason, a valid guaranty existed and Jacobs was estopped from defending against it on the basis of the Statute of Frauds. A jury verdict for Powers was affirmed. Powers Mfg. Co. v. Leon Jacobs Enterprises, 216 M 407, 701 P2d 1377, 42 St. Rep. 906 (1985).

Acquiescence in Modification as Precluding Defense of Statute of Frauds: The parties entered into an agreement for the installation and maintenance of a fire alarm system that was termed a "lease agreement". Payments were to be made over a 5-year term at the expiration of which defendant had the option to renew for another 5-year term or to purchase the system for $1. The original contract was rescinded, and an identical one was executed, except that payments were to begin at a later date. Defendant contended the contract was later further modified by an oral agreement to allow double payments during the summer months and no payments during some of the winter months. Plaintiff denied that this oral agreement was made, but this schedule was tolerated for 3 years. The contract was within the Statute of Frauds; however, an attempted oral modification can operate as a waiver of the right to assert the Statute of Frauds as a defense. The payment schedule followed was a sequence of conduct between the parties establishing a common basis of understanding for interpreting their expressions and conduct. As such, it constituted a course of performance, the acquiescence in which effectively modified the agreement. The Statute of Frauds defense was not applicable. Fire Supply & Serv., Inc. v. Chico Hot Springs, 196 M 435, 639 P2d 1160, 39 St. Rep. 231 (1982).

U.C.C. — Application to Timber Contracts: Defendant was to selectively cut diseased trees on plaintiff's land under a contract entered by the parties. Defendant clearcut several stands of timber. He contended that this was the best management practice to control the spread of the disease. He argued that this established a "usage of trade" under 30-2-208, which should be used in construing the contract. Section 30-2-107(1) establishes that a contract for the sale of timber is subject to the Uniform Commercial Code (U.C.C.) only if the timber is to be "severed by the seller". This was not the case here, so the provisions of the U.C.C. did not apply. Madison Fork Ranch v. L&B Lodge Pole Timber Prod., 189 M 292, 615 P2d 900, 37 St. Rep. 1468 (1980).

What Constitutes "Course of Performance": When there was an agreement for the sale and delivery of wheat at a specified time and the seller delivered the wheat after the agreed delivery date, there was a course of performance acquiesced to which operated to modify the agreement as to delivery date. Farmers Elev. Co. v. Anderson, 170 M 175, 552 P2d 63 (1976).

30-2-209. Modification, rescission and waiver.

Official Comment

Prior Uniform Statutory Provision: Subsection (1)—Compare Section 1, Uniform Written Obligations Act; Subsections (2) to (5)—none.

Purposes of Changes and New Matter:

1. This section seeks to protect and make effective all necessary and desirable modifications of sales contracts without regard to the technicalities which at present hamper such adjustments.

2. Subsection (1) provides that an agreement modifying a sales contract needs no consideration to be binding.

However, modifications made thereunder must meet the test of good faith imposed by this Act. The effective use of bad faith to escape performance on the original contract terms is barred, and the extortion of a "modification" without legitimate commercial reason is ineffective as a violation of the duty of good faith. Nor can a mere technical consideration support a modification made in bad faith.

The test of "good faith" between merchants or as against merchants includes "observance of reasonable commercial standards of fair dealing in the trade" (Section 30-2-103), and may in some situations require an objectively demonstrable reason for seeking a modification. But such matters as a market shift which makes performance come to involve a loss may provide such a reason even though there is no such unforeseen difficulty as would make out a legal excuse from performance under Sections 30-2-615 and 30-2-616.

3. Subsections (2) and (3) are intended to protect against false allegations of oral modifications. "Modification or rescission" includes abandonment or other change by mutual consent, contrary to the decision in Green v. Doniger, 300 N.Y. 238, 90 N.E. 2d 56 (1949); it does not include unilateral "termination" or "cancellation" as defined in Section 30-2-106.

The Statute of Frauds provisions of this Chapter are expressly applied to modifications by subsection (3). Under those provisions the "delivery and acceptance" test is limited to the goods which have been accepted, that is, to the past. "Modification" for the future cannot therefore be conjured up by oral testimony if the price involved is $500.00 or more since such modification must be shown at least by an authenticated memo. And since a memo is limited in its effect to the quantity of goods set forth in it there is safeguard against oral evidence.

Subsection (2) permits the parties in effect to make their own Statute of Frauds as regards any future modification of the contract by giving effect to a clause in a signed agreement which expressly requires any modification to be by signed writing. But note that if a consumer is to be held to such a clause on a form supplied by a merchant it must be separately signed.

4. Subsection (4) is intended, despite the provisions of subsections (2) and (3), to prevent contractual provisions excluding modification except by a signed writing from limiting in other respects the legal effect of the parties' actual later conduct. The effect of such conduct as a waiver is further regulated in subsection (5).

Case Notes

Payment After Unilateral Price Increase as Termination of Contract and Formation of New Contract — Adequate Notice Found: Hansens ordered 30 truckloads of logs from Lumber Enterprises, Inc., at a special price. The parties agreed to ship and receive the logs over a longer period of time than originally agreed. After delivery of 18 truckloads, Lumber Enterprises raised the price of each load by about 50% and told Hansens to "take it or leave it". Hansens agreed to the increase under protest but refused to pay for the last three loads. Citing the official comment to this section and testimony by the Lumber Enterprises manager that the company had to raise prices because it discovered it was losing money on each truckload at the agreed price, the Supreme Court held that the indefinite extension allowed the contract to be terminated at any time by either party. The Supreme Court held that when Lumber Enterprises raised its prices and the Hansens purchased logs more than 30 days after that increase, the former contract had been terminated and a new contract agreed to after reasonable notification. The District Court therefore did not abuse its discretion in applying 30-2-309. Lumber Enterprises, Inc. v. Hansen, 257 M 11, 846 P2d 1046, 50 St. Rep. 138 (1993).

Challenge of Validity of Release on Basis of Unconscionability — Summary Judgment Improper: Plaintiff signed a release for personal injuries with an insurance company in exchange for $8,900. Plaintiff later sued insureds, who were granted summary judgment after pleading the affirmative defense of release. However, a release is governed by contract law and may be rescinded for the same reasons that allow rescission of a contract. Therefore, the validity of a release may be challenged on the basis of unconscionability. The Supreme Court reversed the grant of summary judgment after finding the release was unconscionable based on: (1) plaintiff's dire financial situation, lack of education and legal advice, and vulnerability; (2) substantial uncertainty as to the extent of injury and future prognosis at the time of settlement; and (3) haste in executing the release. Taken together, the circumstances raised an issue of fact whether justice was done, precluding summary judgment. Kelly v. Widner, 236 M 523, 771 P2d 142, 46 St. Rep. 591 (1989).

Documents Incorporated as Contract — Waiver of Condition Precedent: Plaintiff negotiated to sell two-wheel loaders to defendant. The terms of the sale were contained on the purchase order and included a 30-day warranty. Later, a lease agreement covering the same equipment was executed with plaintiff as lessor and defendant as lessee. One of the loaders broke down and required repair. Plaintiff contended the date of the warranty was from the date the purchase order was executed. Defendant refused to pay for the repair, contending the warranty began on the date of the lease agreement. Plaintiff claimed breach and took possession of the loaders. By its own admission, plaintiff conceded that the initial agreement was transformed into the lease agreement. This in effect was a modification of the contract. The terms contained in the purchase order were incorporated into and became part of the lease agreement. The two writings together constituted the final written expression of the agreement. The terms were unambiguous and could not be contradicted by evidence of any prior agreement. Plaintiff was responsible for repair under the warranty provision. Defendant contended refusal to honor this warranty constituted breach of the agreement, while plaintiff contended that a provision for advance payment, not rendered by defendant, was a condition precedent to the formation of the lease contract. The only logical interpretation of the events which transpired was that plaintiff waived the advance payment by delivering the loaders prior to receipt of the payment. Plaintiff could not rely on failure to receive the advance payment in claiming breach of contract under 30-2-706. Defendant was entitled to summary judgment. Westmont Tractor Co. v. Viking Exploration, Inc., 543 F. Supp. 1314, 39 St. Rep. 1398 (D.C. Mont. 1982).

Acquiescence in Modification as Precluding Defense of Statute of Frauds: The parties entered into an agreement for the installation and maintenance of a fire alarm system that was termed a "lease agreement". Payments were to be made over a 5-year term at the expiration of which defendant had the option to renew for another 5-year term or to purchase the system for $1. The original contract was rescinded, and an identical one was executed, except that payments were to begin at a later date. Defendant contended the contract was later further modified by an oral agreement to allow double payments during the summer months and no payments during some of the winter months. Plaintiff denied that this oral agreement was made, but this schedule was tolerated for 3 years. The contract was within the Statute of Frauds; however, an attempted oral modification can operate as a waiver of the right to assert the Statute of Frauds as a defense. The payment schedule followed was a sequence of conduct between the parties establishing a common basis of understanding for interpreting their expressions and conduct. As such, it constituted a course of performance, the acquiescence in which effectively modified the agreement. The Statute of Frauds defense was not applicable. Fire Supply & Serv., Inc. v. Chico Hot Springs, 196 M 435, 639 P2d 1160, 39 St. Rep. 231 (1982).

Waiver of Defenses: When an agreement to deliver wheat at a specified time was orally modified as to the time of delivery and the plaintiff made deliveries of wheat after the set date, he waived his right to assert a defense that the modification did not satisfy the Statute of Frauds. Farmers Elev. Co. v. Anderson, 170 M 175, 552 P2d 63 (1976), followed in Trad Indus., Ltd. v. Brogan, 246 M 439, 805 P2d 54, 48 St. Rep. 51 (1991).

30-2-210. Delegation of performance — assignment of rights.

Official Comment

Prior Uniform Statutory Provision: None.

Purposes:

1. Generally, this section recognizes both delegation of performance and assignability as normal and permissible incidents of a contract for the sale of goods.

2. Delegation of performance, either in conjunction with an assignment or otherwise, is provided for by subsection (1) where no substantial reason can be shown as to why the delegated performance will not be as satisfactory as personal performance.

3. Under subsection (2) rights which are no longer executory such as a right to damages for breach may be assigned although the agreement prohibits assignment. In such cases no question of delegation of any performance is involved. Subsection (2) is subject to Section 30-9A-406, which makes rights to payment for goods sold ("accounts"), whether or not earned, freely alienable notwithstanding a contrary agreement or rule of law.

4. The nature of the contract or the circumstances of the case, however, may bar assignment of the contract even where delegation of performance is not involved. This Chapter and this section are intended to clarify this problem, particularly in cases dealing with output requirement and exclusive dealing contracts. In the first place the section on requirements and exclusive dealing removes from the construction of the original contract most of the "personal discretion" element by substituting the reasonably objective standard of good faith operation of the plant or business to be supplied. Secondly, the section on insecurity and assurances, which is specifically referred to in subsection (5) of this section, frees the other party from the doubts and uncertainty which may afflict him under an assignment of the character in question by permitting him to demand adequate assurance of due performance without which he may suspend his own performance.

Subsection (5) is not in any way intended to limit the effect of the section on insecurity and assurances and the word "performance" includes the giving of orders under a requirements contract. Of course, in any case where a material personal discretion is sought to be transferred, effective assignment is barred by subsection (2).

5. Subsection (4) lays down a general rule of construction distinguishing between a normal commercial assignment, which substitutes the assignee for the assignor both as to rights and duties, and a financing assignment in which only the assignor's rights are transferred.

This Chapter takes no position on the possibility of extending some recognition or power to the original parties to work out normal commercial readjustments of the contract in the case of financing assignments even after the original obligor has been notified of the assignment. This question is dealt with in the Chapter on Secured Transactions (Chapter 9A).

6. Subsection (5) recognizes that the non-assigning original party has a stake in the reliability of the person with whom he has closed the original contract, and is, therefore, entitled to due assurance that any delegated performance will be properly forthcoming.

7. This section is not intended as a complete statement of the law of delegation and assignment but is limited to clarifying a few points doubtful under the case law. Particularly, neither this section nor this Chapter touches directly on such questions as the need or effect of notice of the assignment, the rights of successive assignees, or any question of the form of an assignment, either as between the parties or as against any third parties. Some of these questions are dealt with in Chapter 9A.

Compiler's Comments

1999 Amendment: Chapter 305 inserted (3) concerning security interest; and made minor changes in style. Amendment effective July 1, 2001.

Case Notes

Enforcement of Agricultural Lien Following Sale or Transfer of Farm Products — Assignment of Inchoate or Unperfected Lien Interests Allowed: A crop of sugar beets was sold, and a pesticide sprayer that held an agricultural lien sought to enforce the lien after the sale. Plaintiff bank also held a secured interest on the proceeds of the crop. The buyer issued checks made payable jointly to the bank and the sprayer, honoring the agricultural lien, and the lienholder's unconditioned negotiation of the check acknowledged satisfaction and release of its lien. The bank asserted that, not being an agricultural supplier, the sprayer had no right to file the lien and further contended that because inchoate or unperfected liens are not assignable, any argument that the supplier had assigned its lien right to the sprayer must fail as a matter of law. The sprayer argued that the supplier was clearly eligible to file an agricultural lien and that all actions taken by the sprayer were taken in an agency capacity for the supplier, as indicated in the lien filing, so the payment was not an assignment. Alternatively, the sprayer contended that the transaction was a pass-through between related entities constituting a limited assignment for collection purposes only and that even if the bank's evidence was sufficient to demonstrate that the transaction was a full assignment supported by consideration, inchoate lien interests are nonetheless assignable. The Supreme Court concluded that the dispute was best resolved on the issue of the assignability of inchoate lien interests, noting that generally property of any kind may be transferred, that a right arising out of an obligation is the property of the person to whom it is due and may be transferred, and that Montana's general policy supports the free assignability of rights and obligations stemming from contractual obligations. An agricultural lien is a security and ought to follow the debt or contract to which it pertains, and the free assignability of the right to perfect an agricultural lien comports with lien statutes as well as modern business practices. Thus, even though the supplier's lien was not yet perfected when transferred to the sprayer, it was assignable, and the sprayer validly proceeded to perfect and enforce the lien and was entitled to funds in the amount stipulated by the parties as payment for the chemicals sold by the supplier to the farm and applied by the sprayer and was entitled to the interest on the funds to be credited on that sum. Stockman Bank of Mont. v. Mon-Kota, Inc., 2008 MT 74, 342 M 115, 180 P3d 1125 (2008).

Part 3
General Obligation and Construction of Contract

Part Case Notes

Investment Agreement Containing Arbitration Clause Considered Contract of Adhesion — Remand for Consideration of Investor's Reasonable Expectations and Potential Contract Formation Defenses: Zigrang entered an investment agreement with defendant investment company. The agreement contained an arbitration provision. When Zigrang learned that defendant frequently traded securities in Zigrang's account without permission, Zigrang filed a complaint, which was one of 23 suits filed by investors alleging defendant's mismanagement of accounts. Defendant moved to compel arbitration pursuant to the agreement. A panel of three judges sat en banc to hear evidence common to all 23 cases. Defendant's motion to compel arbitration was denied, but the order contained common findings of fact that did not apply to Zigrang, including a mischaracterization of Zigrang's investment agreement. Defendant appealed. The Supreme Court noted that the agreement constituted a contract of adhesion that supported other contract formation defenses, but did not in itself constitute a sufficient basis for invalidating the agreement. The Supreme Court was unable to completely examine Zigrang's contract formation defenses, including unconscionability, waiver, and reasonable expectations, because the District Court's order relied on the mistaken finding of fact. Thus, the court remanded for further findings of fact related to Zigrang's investment agreement, noting that an inquiry into Zigrang's expectations should consist only of an analysis of Zigrang's objectively reasonable expectations regarding the agreement from Zigrang's perspective and that Zigrang's expectations might negate the arbitration provisions. Zigrang v. U.S. Bancorp Piper Jaffray, Inc., 2005 MT 282, 329 M 239, 123 P3d 237 (2005). See also Iwen v. U.S. W. Direct, 1999 MT 63, 293 M 512, 977 P2d 989 (1999), and Kloss v. Edward D. Jones & Co., 2002 MT 129, 310 M 123, 54 P3d 1 (2002).

30-2-301. General obligations of parties.

Official Comment

Prior Uniform Statutory Provision: Sections 11 and 41, Uniform Sales Act.

Changes: Rewritten.

Purposes of Changes:

This section uses the term "obligation" in contrast to the term "duty" in order to provide for the "condition" aspects of delivery and payment insofar as they are not modified by other sections of this Chapter such as those on cure of tender. It thus replaces not only the general provisions of the Uniform Sales Act on the parties' duties, but also the general provisions of that Act on the effect of conditions. In order to determine what is "in accordance with the contract" under this Chapter usage of trade, course of dealing and performance, and the general background of circumstances must be given due consideration in conjunction with the lay meaning of the words used to define the scope of the conditions and duties.

Case Notes

Sufficient Evidence Required to Show Issue of Material Fact — Contracts: The plaintiff entered into a contract with the defendant to provide the defendant with crushed aggregate material from his gravel pit. The defendant no longer needed the aggregate material and refused to pay the final invoices. The Supreme Court held that the District Court properly granted summary judgment to the plaintiff because the defendant failed to present sufficient evidence to establish that an issue of material fact existed regarding the amount of material extracted by the defendant. In addition, the Supreme Court awarded reasonable attorney fees, trial costs, and appeal costs to the plaintiff under 28-2-2105 and remanded the case to determine the fees and costs. Moore v. Goran, LLC, 2017 MT 208, 388 Mont. 340, 400 P.3d 729.

Buyer Entitled to Damages for Shipment of Damaged Plants: Reed owned a greenhouse and ordered a shipment of poinsettias from McCalif for Christmas. When the plants arrived, many were damaged. Reed refused to pay $3,027.09 for the marketable plants that he kept and resold, contending that he had lost $8,683.95 on the damaged plants for which he had already received purchase orders from other buyers. The Supreme Court held that the record proved that there was no other source for replacement of the damaged plants and that McCalif was aware of that fact and the fact that Reed had entered into contracts for the resale of the plants. The Supreme Court ruled that Reed had the right to accept part of the plants received and reject the rest and that Reed was entitled to incidental and consequential damages because of McCalif's breach. The measure of damages was the difference between what Reed owed for the plants that he kept and what he lost on the orders that he could not fill. McCalif Grower Supplies, Inc. v. Reed, 272 M 254, 900 P2d 880, 52 St. Rep. 659 (1995).

30-2-302. Unconscionable contract or clause.

Official Comment

Prior Uniform Statutory Provision: None.

Purposes:

1. This section is intended to make it possible for the courts to police explicitly against the contracts or clauses which they find to be unconscionable. In the past such policing has been

accomplished by adverse construction of language, by manipulation of the rules of offer and acceptance or by determinations that the clause is contrary to public policy or to the dominant purpose of the contract. This section is intended to allow the court to pass directly on the unconscionability of the contract or particular clause therein and to make a conclusion of law as to its unconscionability. The basic test is whether, in the light of the general commercial background and the commercial needs of the particular trade or case, the clauses involved are so one-sided as to be unconscionable under the circumstances existing at the time of the making of the contract. Subsection (2) makes it clear that it is proper for the court to hear evidence upon these questions. The principle is one of the prevention of oppression and unfair surprise (Cf. Campbell Soup Co. v. Wentz, 172 F.2d 80, 3d Cir. 1948) and not of disturbance of allocation of risks because of superior bargaining power. The underlying basis of this section is illustrated by the results in cases such as the following:

Kansas City Wholesale Grocery Co. v. Weber Packing Corporation, 93 Utah 414, 73 P.2d 1272 (1937), where a clause limiting time for complaints was held inapplicable to latent defects in a shipment of catsup which could be discovered only by microscopic analysis; Hardy v. General Motors Acceptance Corporation, 38 Ga.App. 463, 144 S.E. 327 (1928), holding that a disclaimer of warranty clause applied only to express warranties, thus letting in a fair implied warranty; Andrews Bros. v. Singer & Co. (1934 CA) 1 K.B. 17, holding that where a car with substantial mileage was delivered instead of a "new" car, a disclaimer of warranties, including those "implied," left unaffected an "express obligation" on the description, even though the Sale of Goods Act called such an implied warranty; New Prague Flouring Mill Co. v. G.A. Spears, 194 Iowa 417, 189 N.W. 815 (1922), holding that a clause permitting the seller, upon the buyer's failure to supply shipping instructions, to cancel, ship, or allow delivery date to be indefinitely postponed 30 days at a time by the inaction, does not indefinitely postpone the date of measuring damages for the buyer's breach, to the seller's advantage; and Kansas Flour Mills Co. v. Dirks, 100 Kan. 376, 164 P. 273 (1917), where under a similar clause in a rising market the court permitted the buyer to measure his damages for non-delivery at the end of only one 30 day postponement; Green v. Arcos, Ltd. (1931 CA) 47 T.L.R. 336, where a blanket clause prohibiting rejection of shipments by the buyer was restricted to apply to shipments where discrepancies represented merely mercantile variations; Meyer v. Packard Cleveland Motor Co., 106 Ohio St. 328, 140 N.E. 118 (1922), in which the court held that a "waiver" of all agreements not specified did not preclude implied warranty of fitness of a rebuilt dump truck for ordinary use as a dump truck; Austin Co. v. J.H. Tillman Co., 104 Or. 541, 209 P. 131 (1922), where a clause limiting the buyer's remedy to return was held to be applicable only if the seller had delivered a machine needed for a construction job which reasonably met the contract description; Bekkevold v. Potts, 173 Minn. 87, 216 N.W. 790, 59 A.L.R. 1164 (1927), refusing to allow warranty of fitness for purpose imposed by law to be negated by clause excluding all warranties "made" by the seller; Robert A. Munroe & Co. v. Meyer (1930) 2 K.B. 312, holding that the warranty of description overrides a clause reading "with all faults and defects" where adulterated meat not up to the contract description was delivered.

2. Under this section the court, in its discretion, may refuse to enforce the contract as a whole if it is permeated by the unconscionability, or it may strike any single clause or group of clauses which are so tainted or which are contrary to the essential purpose of the agreement, or it may simply limit unconscionable clauses so as to avoid unconscionable results.

3. The present section is addressed to the court, and the decision is to be made by it. The commercial evidence referred to in subsection (2) is for the court's consideration, not the jury's. Only the agreement which results from the court's action on these matters is to be submitted to the general triers of the facts.

Case Notes

Arbitration Clause in Standardized Form Advertising Agreement — Lack of Mutuality of Obligation and Meaningful Choice Considered Unconscionable Contract of Adhesion: Iwen sued U.S. West Direct for damages for negligent construction of a yellow pages advertisement, infliction of emotional distress, and punitive damages. The District Court held that the parties were bound by the arbitration clause in the directory advertising order. The advertising order was a standardized form, the terms of which Iwen was unable to negotiate and for which Iwen's only choice was to accept or reject, constituting an agreement of adhesion. The arbitration provision lacked mutuality of obligation, was one-sided, and contained terms that were unreasonably favorable to U.S. West Direct, leaving Iwen, as the weaker bargaining party, no meaningful choice regarding acceptance of its provisions. Viewed from the perspective of consumer Iwen, the arbitration clause was held to be unconscionable, and the Supreme Court reversed, striking the arbitration clause, pursuant to this section, and remanding for further proceedings. Iwen v. U.S. W. Direct, 1999 MT 63, 293 M 512, 977 P2d 989, 56 St. Rep. 263 (1999), following Passage v. Prudential-Bache Sec., Inc., 223 M 60, 727 P2d 1298, 43 St. Rep. 1532 (1986), and Leibrand v. Nat'l Farmers Union Property & Cas. Co., 272 M 1, 898 P2d 1220, 52 St. Rep. 557 (1995), and distinguishing Snap-on Tools Corp. v. Vetter, 838 F. Supp. 468 (D.C. Mont. 1993). See also Global Client Solutions, LLC v. Ossello, 2016 MT 50, 382 Mont. 345, 367 P.3d 361.

Challenge of Validity of Release on Basis of Unconscionability — Summary Judgment Improper: Plaintiff signed a release for personal injuries with an insurance company in exchange for $8,900. Plaintiff later sued insureds, who were granted summary judgment after pleading the affirmative defense of release. However, a release is governed by contract law and may be rescinded for the same reasons that allow rescission of a contract. Therefore, the validity of a release may be challenged on the basis of unconscionability. The Supreme Court reversed the grant of summary judgment after finding the release was unconscionable based on: (1) plaintiff's dire financial situation, lack of education and legal advice, and vulnerability; (2) substantial uncertainty as to the extent of injury and future prognosis at the time of settlement; and (3) haste in executing the release. Taken together, the circumstances raised an issue of fact whether justice was done, precluding summary judgment. Kelly v. Widner, 236 M 523, 771 P2d 142, 46 St. Rep. 591 (1989).

No Unconscionability When Implications Based on Opinions: The burden of proof was on plaintiff to raise facts from which reasonable men might conclude that there was oppression, prejudice, or unfair surprise. The plaintiff's opinions alone did not provide sufficient evidence; therefore, summary judgment in favor of defendants was proper on this issue. Westlake v. Osborne, 220 M 91, 713 P2d 548, 43 St. Rep. 200 (1986).

Application of Section to Leases: This section can, at least by analogy, be applied to lease transactions and should guide the Supreme Court in determining whether a lease is unconscionable. (See 1991 enactment of chapter 2A.) All-States Leasing Co. v. Top Hat Lounge, 198 M 1, 649 P2d 1250, 39 St. Rep. 425 (1982).

Unconscionability — Leases Between Businessmen: Courts have readily applied the doctrine of unconscionability of contracts as between consumers and businessmen but are reluctant to rewrite the terms of a contract between businessmen. When, as in instant case, all provisions of a lease are agreed to by businessmen on both sides, none of the surrounding circumstances suggest oppression of lessee's freedom to select another lessor, nothing on the record suggests disparity of bargaining power, and lessee selected both the equipment leased and the supplier of the equipment to the lessor and notified lessor of lessee's desire to make the lease, the lease cannot be considered unconscionable. (See 1991 enactment of chapter 2A.) All-States Leasing Co. v. Top Hat Lounge, 198 M 1, 649 P2d 1250, 39 St. Rep. 425 (1982).

Unconscionability — Success of Unsupported Claim: The mere unsupported claim that equipment lease under which appellants were sued was unconscionable and that a more oppressive lease was hard to imagine could not succeed on appeal from summary judgment for delinquent payments under the lease. All-States Leasing Co. v. Top Hat Lounge, 198 M 1, 649 P2d 1250, 39 St. Rep. 425 (1982).

When Limitation of Remedies Permissible — Equipment Sales — Factors: In a case stemming from an accident involving a hay baler, one issue on appeal was the limitation of remedies. Although limitation of damages for personal injuries in the case of consumer goods is prima facie unconscionable under 30-2-719, farm equipment is defined as "equipment". The limitation of remedy provisions could as a matter of law be found unconscionable. Accordingly, the court ordered an evidentiary hearing on the remedy limitations. Factors under 30-2-302 were to be considered at the hearing. Schlenz v. John Deere Co., 511 F. Supp. 224, 38 St. Rep. 579 (D.C. Mont. 1981).

30-2-303. Allocation or division of risks.

Official Comment

Prior Uniform Statutory Provision: None.

Purposes:

1. This section is intended to make it clear that the parties may modify or allocate "unless otherwise agreed" risks or burdens imposed by this Chapter as they desire, always subject, of course, to the provisions on unconscionability.

Compare Section 30-1-102(4).

2. The risk or burden may be divided by the express terms of the agreement or by the attending circumstances, since under the definition of "agreement" in this Act the circumstances

surrounding the transaction as well as the express language used by the parties enter into the meaning and substance of the agreement.

30-2-304. Price payable in money, goods, realty, or otherwise.

Official Comment

Prior Uniform Statutory Provision: Subsections (2) and (3) of Section 9, Uniform Sales Act.

Changes: Rewritten.

Purposes of Changes:

1. This section corrects the phrasing of the Uniform Sales Act so as to avoid misconstruction and produce greater accuracy in commercial result. While it continues the essential intent and purpose of the Uniform Sales Act it rejects any purely verbalistic construction in disregard of the underlying reason of the provisions.

2. Under subsection (1) the provisions of this Chapter are applicable to transactions where the "price" of goods is payable in something other than money. This does not mean, however, that this whole Chapter applies automatically and in its entirety simply because an agreed transfer of title to goods is not a gift. The basic purposes and reasons of the Chapter must always be considered in determining the applicability of any of its provisions.

3. Subsection (2) lays down the general principle that when goods are to be exchanged for realty, the provisions of this Chapter apply only to those aspects of the transaction which concern the transfer of title to goods but do not affect the transfer of the realty since the detailed regulation of various particular contracts which fall outside the scope of this Chapter is left to the courts and other legislation. However, the complexities of these situations may be such that each must be analyzed in the light of the underlying reasons in order to determine the applicable principles. Local statutes dealing with realty are not to be lightly disregarded or altered by language of this Chapter. In contrast, this Chapter declares definite policies in regard to certain matters legitimately within its scope though concerned with real property situations, and in those instances the provisions of this Chapter control.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-2-305. Open price term.

Official Comment

Prior Uniform Statutory Provision: Sections 9 and 10, Uniform Sales Act.

Changes: Completely rewritten.

Purposes of Changes:

1. This section applies when the price term is left open on the making of an agreement which is nevertheless intended by the parties to be a binding agreement. This Chapter rejects in these instances the formula that "an agreement to agree is unenforceable" if the case falls within subsection (1) of this section, and rejects also defeating such agreements on the ground of "indefiniteness". Instead this Chapter recognizes the dominant intention of the parties to have the deal continue to be binding upon both. As to future performance, since this Chapter recognizes remedies such as cover (Section 30-2-712), resale (Section 30-2-706) and specific performance (Section 30-2-716) which go beyond any mere arithmetic as between contract price and market price, there is usually a "reasonably certain basis for granting an appropriate remedy for breach" so that the contract need not fail for indefiniteness.

2. Under some circumstances the postponement of agreement on price will mean that no deal has really been concluded, and this is made express in the preamble of subsection (1) ("The parties *if they so intend*") and in subsection (4). Whether or not this is so is, in most cases, a question to be determined by the trier of fact.

3. Subsection (2), dealing with the situation where the price is to be fixed by one party rejects the uncommercial idea that an agreement that the seller may fix the price means that he may fix any price he may wish by the express qualification that the price so fixed must be fixed in good faith. Good faith includes observance of reasonable commercial standards of fair dealing in the trade if the party is a merchant. (Section 30-2-103). But in the normal case a "posted price" or a future seller's or buyer's "given price," "price in effect," "market price," or the like satisfies the good faith requirement.

4. The section recognizes that there may be cases in which a particular person's judgment is not chosen merely as a barometer or index of a fair price but is an essential condition to the parties' intent to make any contract at all. For example, the case where a known and trusted

expert is to "value" a particular painting for which there is no market standard differs sharply from the situation where a named expert is to determine the grade of cotton, and the difference would support a finding that in the one the parties did not intend to make a binding agreement if that expert were unavailable whereas in the other they did so intend. Other circumstances would of course affect the validity of such a finding.

5. Under subsection (3), wrongful interference by one party with any agreed machinery for price fixing in the contract may be treated by the other party as a repudiation justifying cancellation, or merely as a failure to take cooperative action thus shifting to the aggrieved party the reasonable leeway in fixing the price.

6. Throughout the entire section, the purpose is to give effect to the agreement which has been made. That effect, however, is always conditioned by the requirement of good faith action which is made an inherent part of all contracts within this Act. (Section 30-1-203).

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-2-306. Output, requirements and exclusive dealings.

Official Comment

Prior Uniform Statutory Provision: None.

Purposes:

1. Subsection (1) of this section, in regard to output and requirements, applies to this specific problem the general approach of this Act which requires the reading of commercial background and intent into the language of any agreement and demands good faith in the performance of that agreement. It applies to such contracts of nonproducing establishments such as dealers or distributors as well as to manufacturing concerns.

2. Under this Chapter, a contract for output or requirements is not too indefinite since it is held to mean the actual good faith output or requirements of the particular party. Nor does such a contract lack mutuality of obligation since, under this section, the party who will determine quantity is required to operate his plant or conduct his business in good faith and according to commercial standards of fair dealing in the trade so that his output or requirements will approximate a reasonably foreseeable figure. Reasonable elasticity in the requirements is expressly envisaged by this section and good faith variations from prior requirements are permitted even when the variation may be such as to result in discontinuance. A shutdown by a requirements buyer for lack of orders might be permissible when a shut-down merely to curtail losses would not. The essential test is whether the party is acting in good faith. Similarly, a sudden expansion of the plant by which requirements are to be measured would not be included within the scope of the contract as made but normal expansion undertaken in good faith would be within the scope of this section. One of the factors in an expansion situation would be whether the market price had risen greatly in a case in which the requirements contract contained a fixed price. Reasonable variation of an extreme sort is exemplified in Southwest Natural Gas Co. v. Oklahoma Portland Cement Co., 102 F.2d 630 (C.C.A. 10, 1939). This Chapter takes no position as to whether a requirements contract is a provable claim in bankruptcy.

3. If an estimate of output or requirements is included in the agreement, no quantity unreasonably disproportionate to it may be tendered or demanded. Any minimum or maximum set by the agreement shows a clear limit on the intended elasticity. In similar fashion, the agreed estimate is to be regarded as a center around which the parties intend the variation to occur.

4. When an enterprise is sold, the question may arise whether the buyer is bound by an existing output or requirements contract. That question is outside the scope of this Chapter, and is to be determined on other principles of law. Assuming that the contract continues, the output or requirements in the hands of the new owner continue to be measured by the actual good faith output or requirements under the normal operation of the enterprise prior to sale. The sale itself is not grounds for sudden expansion or decrease.

5. Subsection (2), on exclusive dealing, makes explicit the commercial rule embodied in this Act under which the parties to such contracts are held to have impliedly, even when not expressly, bound themselves to use reasonable diligence as well as good faith in their performance of the contract. Under such contracts the exclusive agent is required, although no express commitment has been made, to use reasonable effort and due diligence in the expansion of the market or the promotion of the product, as the case may be. The principal is expected under such a contract to refrain from supplying any other dealer or agent within the exclusive territory. An exclusive dealing agreement brings into play all of the good faith aspects of the output and requirement

problems of subsection (1). It also raises questions of insecurity and right to adequate assurance under this Chapter.

Case Notes

Requirements Contract: The trial court's finding of a requirements contract was upheld because there is no provision in the contract which specifies an exact quantity and price binding both the seller and buyer and since the contract contains a specific reference to the contingency of participation of local government units. In addition, the plaintiff did not prove that the State, in bad faith, made unreasonable disproportionate variations in the estimates of quantities. W. Sign, Inc. v. St., 180 M 278, 590 P2d 141 (1979).

30-2-307. Delivery in single lot or several lots.

Official Comment

Prior Uniform Statutory Provision: Section 45(1), Uniform Sales Act.

Changes: Rewritten and expanded.

Purposes of Changes:

1. This section applies where the parties have not specifically agreed whether delivery and payment are to be by lots and generally continues the essential intent of original Act, Section 45(1) by assuming that the parties intended delivery to be in a single lot.

2. Where the actual agreement or the circumstances do not indicate otherwise, delivery in lots is not permitted under this section and the buyer is properly entitled to reject for a deficiency in the tender, subject to any privilege in the seller to cure the tender.

3. The "but" clause of this section goes to the case in which it is not commercially feasible to deliver or to receive the goods in a single lot as for example, where a contract calls for the shipment of ten carloads of coal and only three cars are available at a given time. Similarly, in a contract involving brick necessary to build a building the buyer's storage space may be limited so that it would be impossible to receive the entire amount of brick at once, or it may be necessary to assemble the goods as in the case of cattle on the range, or to mine them.

In such cases, a partial delivery is not subject to rejection for the defect in quantity alone, if the circumstances do not indicate a repudiation or default by the seller as to the expected balance or do not give the buyer ground for suspending his performance because of insecurity under the provisions of Section 30-2-609. However, in such cases the undelivered balance of goods under the contract must be forthcoming within a reasonable time and in a reasonable manner according to the policy of Section 30-2-503 on manner of tender of delivery. This is reinforced by the express provisions of Section 30-2-608 that if a lot has been accepted on the reasonable assumption that its nonconformity will be cured, the acceptance may be revoked if the cure does not seasonably occur. The section rejects the rule of Kelly Construction Co. v. Hackensack Brick Co., 91 N.J.L. 585, 103 A. 417, 2 A.L.R. 685 (1918) and approves the result in Lynn M. Ranger, Inc. v. Gildersleeve, 106 Conn. 372, 138 A. 142 (1927) in which a contract was made for six carloads of coal then rolling from the mines and consigned to the seller but the seller agreed to divert the carloads to the buyer as soon as the car numbers became known to him. He arranged a diversion of two cars and then notified the buyer who then repudiated the contract. The seller was held to be entitled to his full remedy for the two cars diverted because simultaneous delivery of all of the cars was not contemplated by either party.

4. Where the circumstances indicate that a party has a right to delivery in lots, the price may be demanded for each lot if it is apportionable.

30-2-308. Absence of specified place for delivery.

Official Comment

[*Corresponding U.C.C. Section:* Section 2-308, U.C.C.]

Prior Uniform Statutory Provision: Paragraphs (a) and (b)—Section 43(1), Uniform Sales Act; Paragraph (c)—none.

Changes: Slight modification in language.

Purposes of Changes and New Matter:

1. Paragraphs (a) and (b) provide for those noncommercial sales and for those occasional commercial sales where no place or means of delivery has been agreed upon by the parties. Where delivery by carrier is "required or authorized by the agreement", the seller's duties as to delivery of the goods are governed not by this section but by Section 30-2-504.

2. Under paragraph (b) when the identified goods contracted for are known to both parties to be in some location other than the seller's place of business or residence, the parties are presumed to have intended that place to be the place of delivery. This paragraph also applies (unless, as

would be normal, the circumstances show that delivery by way of documents is intended) to a bulk of goods in the possession of a bailee. In such a case, however, the seller has the additional obligation to procure the acknowledgment by the bailee of the buyer's right to possession.

3. Where "customary banking channels" call only for due notification by the banker that the documents are available, leaving the buyer himself to see to the physical receipt of the goods, tender at the buyer's address is not required under paragraph (c) [subsection (c)]. But that paragraph merely eliminates the possibility of a default by the seller if "customary banking channels" have been properly used in giving notice to the buyer. Where the bank has purchased a draft accompanied by or associated with documents or has undertaken its collection on behalf of the seller, Part 5 of Article 4 [Title 30, chapter 4, part 5] spells out its duties and relations to its customer. Where the documents move forward under a letter of credit the Article on Letters of Credit [Title 30, chapter 5] spells out the duties and relations between the bank, the seller and the buyer. Delivery in relationship to either tangible or electronic documents of title is defined in Article 1, Section 1-201 [30-1-201].

4. The rules of this section apply only "unless otherwise agreed." The surrounding circumstances, usage of trade, course of dealing and course of performance, as well as the express language of the parties, may constitute an "otherwise agreement".

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

30-2-309. Absence of specific time provisions — notice of termination.

Official Comment

Prior Uniform Statutory Provision: Subsection (1)—see Sections 43(2), 45(2), 47(1) and 48, Uniform Sales Act, for policy continued under this Chapter; Subsection (2)—none; Subsection (3)—none.

Changes: Completely different in scope.

Purposes of Changes and New Matter:

1. Subsection (1) requires that all actions taken under a sales contract must be taken within a reasonable time where no time has been agreed upon. The reasonable time under this provision turns on the criteria as to "reasonable time" and on good faith and commercial standards set forth in Sections 30-1-203, 30-1-204 and 30-2-103. It thus depends upon what constitutes acceptable commercial conduct in view of the nature purpose and circumstances of the action to be taken. Agreement as to a definite time, however, may be found in a term implied from the contractual circumstances, usage of trade or course of dealing or performance as well as in an express term. Such cases fall outside of this subsection since in them the time for action is "agreed" by usage.

2. The time for payment, where not agreed upon, is related to the time for delivery; the particular problems which arise in connection with determining the appropriate time of payment and the time for any inspection before payment which is both allowed by law and demanded by the buyer are covered in Section 30-2-513.

3. The facts in regard to shipment and delivery differ so widely as to make detailed provision for them in the text of this Chapter impracticable. The applicable principles, however, make it clear that surprise is to be avoided, good faith judgment is to be protected, and notice or negotiation to reduce the uncertainty to certainty is to be favored.

4. When the time for delivery is left open, unreasonably early offers of or demands for delivery are intended to be read under this Chapter as expressions of desire or intention, requesting the assent or acquiescence of the other party, not as final positions which may amount without more to breach or to create breach by the other side. See Sections 30-2-207 and 30-2-609.

5. The obligation of good faith under this Act requires reasonable notification before a contract may be treated as breached because a reasonable time for delivery or demand has expired. This operates both in the case of a contract originally indefinite as to time and of one subsequently made indefinite by waiver.

When both parties let an originally reasonable time go by in silence, the course of conduct under the contract may be viewed as enlarging the reasonable time for tender or demand of performance. The contract may be terminated by abandonment.

6. Parties to a contract are not required in giving reasonable notification to fix, at peril of breach, a time which is in fact reasonable in the unforeseeable judgment of a later trier of fact. Effective communication of a proposed time limit calls for a response, so that failure to reply will make out acquiescence. Where objection is made, however, or if the demand is merely for information as to when goods will be delivered or will be ordered out, demand for assurances on

the ground of insecurity may be made under this Chapter pending further negotiations. Only when a party insists on undue delay or on rejection of the other party's reasonable proposal is there a question of flat breach under the present section.

7. Subsection (2) applies a commercially reasonable view to resolve the conflict which has arisen in the cases as to contracts of indefinite duration. The "reasonable time" of duration appropriate to a given arrangement is limited by the circumstances. When the arrangement has been carried on by the parties over the years, the "reasonable time" can continue indefinitely and the contract will not terminate until notice.

8. Subsection (3) recognizes that the application of principles of good faith and sound commercial practice normally call for such notification of the termination of a going contract relationship as will give the other party reasonable time to seek a substitute arrangement. An agreement dispensing with notification or limiting the time for the seeking of a substitute arrangement is, of course, valid under this subsection unless the results of putting it into operation would be the creation of an unconscionable state of affairs.

9. Justifiable cancellation for breach is a remedy for breach and is not the kind of termination covered by the present subsection.

10. The requirement of notification is dispensed with where the contract provides for termination on the happening of an "agreed event." "Event" is a term chosen here to contrast with "option" or the like.

Case Notes

Payment After Unilateral Price Increase as Termination of Contract and Formation of New Contract — Adequate Notice Found: Hansens ordered 30 truckloads of logs from Lumber Enterprises, Inc., at a special price. The parties agreed to ship and receive the logs over a longer period of time than originally agreed. After delivery of 18 truckloads, Lumber Enterprises raised the price of each load by about 50% and told Hansens to "take it or leave it". Hansens agreed to the increase under protest but refused to pay for the last three loads. Citing the official comment to 30-2-209 and testimony by the Lumber Enterprises manager that the company had to raise prices because it discovered it was losing money on each truckload at the agreed price, the Supreme Court held that the indefinite extension allowed the contract to be terminated at any time by either party. The Supreme Court held that when Lumber Enterprises raised its prices and the Hansens purchased logs more than 30 days after that increase, the former contract had been terminated and a new contract agreed to after reasonable notification. The District Court therefore did not abuse its discretion in applying this section. Lumber Enterprises, Inc. v. Hansen, 257 M 11, 846 P2d 1046, 50 St. Rep. 138 (1993).

Commercially Reasonable Shipping Date: Although not specified in the contract, subsequent correspondence between the parties indicates the time for shipment or delivery of the metal siding from Morin to Volk was to be approximately May 1, 1978 (90 days from the January 30 letter from Volk advising Morin that the color of the siding was to be "Buckskin 500"). Morin acknowledged the May 1, 1978, delivery date by letter dated February 2, 1978. The court concludes that even if the scheduled shipping date of May 1, 1978, were not one expressly agreed upon, it is, under all the facts and circumstances, a shipping date which would be implied as commercially reasonable. Morin Bldg. Prod. Co., Inc. v. Volk Constr., Inc., 500 F. Supp. 82, 37 St. Rep. 1803 (D.C. Mont. 1980).

Time for Delivery: When the correspondence which constituted the memoranda of a contract for the sale did not specify that time was of the essence, the reasonable time provision applied. Martel Constr., Inc. v. Gleason Equip., Inc., 166 M 479, 534 P2d 883 (1975).

30-2-310. Open time for payment or running of credit — authority to ship under reservation.

Official Comment

[*Corresponding U.C.C. Section:* Section 2-310, U.C.C.]

[*Code Commissioner Note:* In 2005, Montana adopted Alternative B of the 2003 revision to Article 7 for this section.]

Prior Uniform Statutory Provision: Sections 42 and 47(2), Uniform Sales Act.

Changes: Completely rewritten in this and other sections.

Purposes of Changes: This section is drawn to reflect modern business methods of dealing at a distance rather than face to face. Thus:

1. Paragraph (a) provides that payment is due at the time and place "the buyer is to receive the goods" rather than at the point of delivery except in documentary shipment cases (paragraph (c)). This grants an opportunity for the exercise by the buyer of his preliminary right to inspection

before paying even though under the delivery term the risk of loss may have previously passed to him or the running of the credit period has already started.

2. Paragraph (b) [subsection (2)] while providing for inspection by the buyer before he pays, protects the seller. He is not required to give up possession of the goods until he has received payment, where no credit has been contemplated by the parties. The seller may collect through a bank by a sight draft against an order bill of lading "hold until arrival; inspection allowed." The obligations of the bank under such a provision are set forth in Part 5 of Article 4 [Title 30, chapter 4, part 5]. Under subsection (c) [subsection (3)], in the absence of a credit term, the seller is permitted to ship under reservation and if he does payment is then due where and when the buyer is to receive delivery of the tangible documents of title. In the case of an electronic document of title, payment is due when the buyer is to receive delivery of the electronic document and at the seller's place of business, or if none, the seller's residence. Delivery as to documents of title is stated in Article 1, Section 1-201 [30-1-201].

3. Unless otherwise agreed, the place for the delivery of the documents and payment is the buyer's city but the time for payment is only after arrival of the goods, since under paragraph (b) [subsection (2)], and Sections 2-512 and 2-513 [30-2-512 and 30-2-513] the buyer is under no duty to pay prior to inspection. Tender of a document of title requires that the seller be ready, willing and able to transfer possession of a tangible document of title or control of an electronic document of title to the buyer.

4. Where the mode of shipment is such that goods must be unloaded immediately upon arrival, too rapidly to permit adequate inspection before receipt, the seller must be guided by the provisions of this Chapter on inspection which provide that if the seller wishes to demand payment before inspection, he must put an appropriate term into the contract. Even requiring payment against documents will not of itself have this desired result if the documents are to be held until the arrival of the goods. But under (b) and (c) if the terms are C.I.F., C.O.D., or cash against documents payment may be due before inspection.

5. Paragraph (d) states the common commercial understanding that an agreed credit period runs from the time of shipment or from that dating of the invoice which is commonly recognized as a representation of the time of shipment. The provision concerning any delay in sending forth the invoice is included because such conduct results in depriving the buyer of his full notice and warning as to when he must be prepared to pay.

Compiler's Comments

2005 Amendment: Chapter 575 in (3) at end inserted "regardless of where the goods are to be received"; in (3)(a) at end substituted "delivery of the tangible documents" for "the documents regardless of where the goods are to be received"; inserted (3)(b) relating to electronic documents; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-2-311. Options and cooperation respecting performance.

Official Comment

Prior Uniform Statutory Provision: None.

Purposes:

1. Subsection (1) permits the parties to leave certain detailed particulars of performance to be filled in by either of them without running the risk of having the contract invalidated for indefiniteness. The party to whom the agreement gives power to specify the missing details is required to exercise good faith and to act in accordance with commercial standards so that there is no surprise and the range of permissible variation is limited by what is commercially reasonable. The "agreement" which permits one party so to specify may be found as well in a course of dealing, usage of trade, or implication from circumstances as in explicit language used by the parties.

2. Options as to assortment of goods or shipping arrangements are specifically reserved to the buyer and seller respectively under subsection (2) where no other arrangement has been made. This section rejects the test which mechanically and without regard to usage or the

purpose of the option gave the option to the party "first under a duty to move" and applies instead a standard commercial interpretation to these circumstances. The "unless otherwise agreed" provision of this subsection covers not only express terms but the background and circumstances which enter into the agreement.

3. Subsection (3) applies when the exercise of an option or cooperation by one party is necessary to or materially affects the other party's performance, but it is not seasonably forthcoming; the subsection relieves the other party from the necessity for performance or excuses his delay in performance as the case may be. The contract-keeping party may at his option under this subsection proceed to perform in any commercially reasonable manner rather than wait. In addition to the special remedies provided, this subsection also reserves "all other remedies". The remedy of particular importance in this connection is that provided for insecurity. Request may also be made pursuant to the obligation of good faith for a reasonable indication of the time and manner of performance for which a party is to hold himself ready.

4. The remedy provided in subsection (3) is one which does not operate in the situation which falls within the scope of Section 30-2-614 on substituted performance. Where the failure to cooperate results from circumstances set forth in that Section, the other party is under a duty to proffer or demand (as the case may be) substitute performance as a condition to claiming rights against the noncooperating party.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-2-312. Warranty of title and against infringement — buyer's obligation against infringement.

Official Comment

Prior Uniform Statutory Provision: Section 13, Uniform Sales Act.

Changes: Completely rewritten, the provisions concerning infringement being new.

Purposes of Changes:

1. Subsection (1) makes provision for a buyer's basic needs in respect to a title which he in good faith expects to acquire by his purchase, namely, that he receive a good, clean title transferred to him also in a rightful manner so that he will not be exposed to a lawsuit in order to protect it.

The warranty extends to a buyer whether or not the seller was in possession of the goods at the time the sale or contract to sell was made.

The warranty of quiet possession is abolished. Disturbance of quiet possession, although not mentioned specifically, is one way, among many, in which the breach of the warranty of title may be established.

The "knowledge" referred to in subsection (1)(b) is actual knowledge as distinct from notice.

2. The provisions of this Chapter requiring notification to the seller within a reasonable time after the buyer's discovery of a breach apply to notice of a breach of the warranty of title, where the seller's breach was innocent. However, if the seller's breach was in bad faith he cannot be permitted to claim that he has been misled or prejudiced by the delay in giving notice. In such case the "reasonable" time for notice should receive a very liberal interpretation. Whether the breach by the seller is in good or bad faith Section 30-2-725 provides that the cause of action accrues when the breach occurs. Under the provisions of that section the breach of the warranty of good title occurs when tender of delivery is made since the warranty is not one which extends to "future performance of the goods."

3. When the goods are part of the seller's normal stock and are sold in his normal course of business, it is his duty to see that no claim of infringement of a patent or trademark by a third party will mar the buyer's title. A sale by a person other than a dealer, however, raises no implication in its circumstances of such a warranty. Nor is there such an implication when the buyer orders goods to be assembled, prepared or manufactured on his own specifications. If, in such a case, the resulting product infringes a patent or trademark, the liability will run from buyer to seller. There is, under such circumstances, a tacit representation on the part of the buyer that the seller will be safe in manufacturing according to the specifications, and the buyer is under an obligation in good faith to indemnify him for any loss suffered.

4. This section rejects the cases which recognize the principle that infringements violate the warranty of title but deny the buyer a remedy unless he has been expressly prevented from using the goods. Under this Chapter "eviction" is not a necessary condition to the buyer's remedy since the buyer's remedy arises immediately upon receipt of notice of infringement; it is merely one way of establishing the fact of breach.

5. Subsection (2) recognizes that sales by sheriffs, executors, certain foreclosing lienors and persons similarly situated may be so out of the ordinary commercial course that their peculiar character is immediately apparent to the buyer and therefore no personal obligation is imposed upon the seller who is purporting to sell only an unknown or limited right. This subsection does not touch upon and leaves open all questions of restitution arising in such cases, when a unique article so sold is reclaimed by a third party as the rightful owner.

Foreclosure sales under Chapter 9A are another matter. Section 30-9A-610 provides that a disposition of collateral under that section includes warranties such as those imposed by this section on a voluntary disposition of property of the kind involved. Consequently, unless properly excluded under subsection (2) or under the special provisions for exclusion in Section 30-9A-610, a disposition under Section 30-9A-610 of collateral consisting of goods includes the warranties imposed by subsection (1) and, if applicable, subsection (3).

6. The warranty of subsection (1) is not designated as an "implied" warranty, and hence is not subject to Section 30-2-316(3). Disclaimer of the warranty of title is governed instead by subsection (2), which requires either specific language or the described circumstances.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Warranty of Title Breached When Seller Sold Stolen Goods: Defendant pawnshop operator who sold stolen property to plaintiff refused to give plaintiff a refund after the property was recovered by police. Defendant argued that he disclaimed any warranty of title to goods sold in his business by posting a sign alerting buyers that merchandise is sold "as is" and by writing the same notation on his sales slips. Defendant clearly breached the warranty of clear title under this section when he sold stolen goods because neither a thief nor his successor pass clear title to stolen goods. It was irrelevant that defendant claimed he did not know the goods were stolen. Brokke v. Williams, 235 M 305, 766 P2d 1311, 46 St. Rep. 6 (1989).

30-2-313. Express warranties by affirmation, promise, description, sample.

Official Comment

Prior Uniform Statutory Provision: Sections 12, 14 and 16, Uniform Sales Act.

Changes: Rewritten.

Purposes of Changes: To consolidate and systematize basic principles with the result that:

1. "Express" warranties rest on "dickered" aspects of the individual bargain, and go so clearly to the essence of that bargain that words of disclaimer in a form are repugnant to the basic dickered terms. "Implied" warranties rest so clearly on a common factual situation or set of conditions that no particular language or action is necessary to evidence them and they will arise in such a situation unless unmistakably negated.

This section reverts to the older case law insofar as the warranties of description and sample are designated "express" rather than "implied".

2. Although this section is limited in its scope and direct purpose to warranties made by the seller to the buyer as part of a contract for sale, the warranty sections of this Chapter are not designed in any way to disturb those lines of case law growth which have recognized that warranties need not be confined either to sales contracts or to the direct parties to such a contract. They may arise in other appropriate circumstances such as in the case of bailments for hire, whether such bailment is itself the main contract or is merely a supplying of containers under a contract for the sale of their contents. The provisions of Section 30-2-318 on third party beneficiaries expressly recognize this case law development within one particular area. Beyond that, the matter is left to the case law with the intention that the policies of this Act may offer useful guidance in dealing with further cases as they arise.

3. The present section deals with affirmations of fact by the seller, descriptions of the goods or exhibitions of samples, exactly as any other part of a negotiation which ends in a contract is dealt with. No specific intention to make a warranty is necessary if any of these factors is made part of the basis of the bargain. In actual practice affirmations of fact made by the seller about the goods during a bargain are regarded as part of the description of those goods; hence no particular reliance on such statements need be shown in order to weave them into the fabric of the agreement. Rather, any fact which is to take such affirmations, once made, out of the agreement requires clear affirmative proof. The issue normally is one of fact.

4. In view of the principle that the whole purpose of the law of warranty is to determine what it is that the seller has in essence agreed to sell, the policy is adopted of those cases which

refuse except in unusual circumstances to recognize a material deletion of the seller's obligation. Thus, a contract is normally a contract for a sale of something describable and described. A clause generally disclaiming "all warranties, express or implied" cannot reduce the seller's obligation with respect to such description and therefore cannot be given literal effect under Section 30-2-316.

This is not intended to mean that the parties, if they consciously desire, cannot make their own bargain as they wish. But in determining what they have agreed upon good faith is a factor and consideration should be given to the fact that the probability is small that a real price is intended to be exchanged for a pseudo-obligation.

5. Paragraph (1)(b) makes specific some of the principles set forth above when a description of the goods is given by the seller.

A description need not be by words. Technical specifications, blueprints and the like can afford more exact description than mere language and if made part of the basis of the bargain goods must conform with them. Past deliveries may set the description of quality, either expressly or impliedly by course of dealing. Of course, all descriptions by merchants must be read against the applicable trade usages with the general rules as to merchantability resolving any doubts.

6. The basic situation as to statements affecting the true essence of the bargain is no different when a sample or model is involved in the transaction. This section includes both a "sample" actually drawn from the bulk of goods which is the subject matter of the sale, and a "model" which is offered for inspection when the subject matter is not at hand and which has not been drawn from the bulk of the goods.

Although the underlying principles are unchanged, the facts are often ambiguous when something is shown as illustrative, rather than as a straight sample. In general, the presumption is that any sample or model just as any affirmation of fact is intended to become a basis of the bargain. But there is no escape from the question of fact. When the seller exhibits a sample purporting to be drawn from an existing bulk, good faith of course requires that the sample be fairly drawn. But in mercantile experience the mere exhibition of a "sample" does not of itself show whether it is merely intended to "suggest" or to "be" the character of the subject-matter of the contract. The question is whether the seller has so acted with reference to the sample as to make him responsible that the whole shall have at least the values shown by it. The circumstances aid in answering this question. If the sample has been drawn from an existing bulk, it must be regarded as describing values of the goods contracted for unless it is accompanied by an unmistakable denial of such responsibility. If, on the other hand, a model of merchandise not on hand is offered, the mercantile presumption that it has become a literal description of the subject matter is not so strong, and particularly so if modification on the buyer's initiative impairs any feature of the model.

7. The precise time when words of description or affirmation are made or samples are shown is not material. The sole question is whether the language or samples or models are fairly to be regarded as part of the contract. If language is used after the closing of the deal (as when the buyer when taking delivery asks and receives an additional assurance), the warranty becomes a modification, and need not be supported by consideration if it is otherwise reasonable and in order (Section 30-2-209).

8. Concerning affirmations of value or a seller's opinion or commendation under subsection (2), the basic question remains the same: What statements of the seller have in the circumstances and in objective judgment become part of the basis of the bargain? As indicated above, all of the statements of the seller do so unless good reason is shown to the contrary. The provisions of subsection (2) are included, however, since common experience discloses that some statements or predictions cannot fairly be viewed as entering into the bargain. Even as to false statements of value, however, the possibility is left open that a remedy may be provided by the law relating to fraud or misrepresentation.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

Case Notes

Statement in Sales Brochure Rising to Level of Express Warranty: Defendant motor home manufacturer argued that plaintiffs' claims for breach of warranty arising from a swaying and handling problem with their motor home were not supported by the evidence and should not have gone to the jury. Defendant contended that plaintiffs reviewed the express warranties associated with a motor home and knew that defendant's warranty did not cover the chassis and its component parts, which were covered by a separate warranty with the chassis manufacturer. The District Court rejected defendant's argument, and on appeal the Supreme Court affirmed. A statement in one of defendant's sales brochures promised a "flawless ride", and the jury could have concluded that the statement created an express warranty that was subsequently breached. Vader v. Fleetwood Enterprises, Inc., 2009 MT 6, 348 M 344, 201 P3d 139 (2009).

Abuse of Product: Plaintiff brought suit after the engine of his 2-year-old truck quit running. The truck had 42,000 miles on it at the time. Defendant refused to repair the truck under warranty. Testimony indicated that there was significant damage to the truck. The evidence of the condition of the truck indicated that the truck was abused and that the abuse directly affected the engine's performance. There was substantial evidence to support a verdict for the defendant. Owens v. Gen. Motors Corp., 249 M 124, 813 P2d 985, 48 St. Rep. 608 (1991).

Statements and Conduct as Basis for Express Warranty: Scheckla represented to Melotz that an engine was in good working condition, recently had major repair work done to it, and could be put right to work. After the engine was installed and developed problems, Melotz was told to replace the bearings and if that did not correct the problems, Scheckla would pay for the repairs. Additionally, on at least one other occasion, Scheckla recommended the type of repairs that should be done and had his mechanic work on the engine in an attempt to fix it. Scheckla's statements, together with his conduct after the engine was installed, provided a sufficient basis upon which the jury could find that an express warranty existed. Melotz v. Scheckla, 245 M 327, 801 P2d 593, 47 St. Rep. 2165 (1990).

Warranties — When Created — When Disclaimed: Plaintiffs brought an action against a farm implement company for breach of implied warranties of merchantability and fitness. The court noted that the Montana U.C.C. allows a seller to disclaim these implied warranties by means of "conspicuous" language in a writing. It was found the disclaimers in this case were sufficiently conspicuous to be effective under 30-2-316. The plaintiffs claimed the advertising, promotional materials, and operator's manual created express warranties under 30-2-313. The court held the disclaimers did not destroy the express warranty of safety made in the operator's manual. Schlenz v. John Deere Co., 511 F. Supp. 224, 38 St. Rep. 579 (D.C. Mont. 1981).

Sale of Sprinkler Irrigation Equipment: The evidence supported the court's findings that defendants made express warranties to plaintiffs in the course of a sales transaction involving sprinkler irrigation equipment, orally and by brochure, and that they were breached. Whitaker v. Farmhand, Inc., 173 M 345, 567 P2d 916 (1977).

Workmanship Warranty: The court properly found, based upon the only evidence presented, that the third-party defendant expressly warranted and guaranteed its work and that the work was improperly performed, causing the defective condition. Prudential Fed. S & L v. Bldg. Agencies, Inc., 173 M 263, 567 P2d 445 (1977).

30-2-314. Implied warranty — merchantability — usage of trade.

Official Comment

Prior Uniform Statutory Provision: Section 15(2), Uniform Sales Act.

Changes: Completely rewritten.

Purposes of Changes: This section, drawn in view of the steadily developing case law on the subject, is intended to make it clear that:

1. The seller's obligation applies to present sales as well as to contracts to sell subject to the effects of any examination of specific goods. (Subsection (2) of Section 30-2-316). Also, the warranty of merchantability applies to sales for use as well as to sales for resale.

2. The question when the warranty is imposed turns basically on the meaning of the terms of the agreement as recognized in the trade. Goods delivered under an agreement made by a merchant in a given line of trade must be of a quality comparable to that generally acceptable in that line of trade under the description or other designation of the goods used in the agreement. The responsibility imposed rests on any merchant-seller, and the absence of the words "grower or manufacturer or not" which appeared in Section 15(2) of the Uniform Sales Act does not restrict the applicability of this section.

3. A specific designation of goods by the buyer does not exclude the seller's obligation that they be fit for the general purposes appropriate to such goods. A contract for the sale of second-hand goods, however, involves only such obligation as is appropriate to such goods for that is their contract description. A person making an isolated sale of goods is not a "merchant" within the meaning of the full scope of this section and, thus, no warranty of merchantability would apply. His knowledge of any defects not apparent on inspection would, however, without need for express agreement and in keeping with the underlying reason of the present section

and the provisions on good faith, impose an obligation that known material but hidden defects be fully disclosed.

4. Although a seller may not be a "merchant" as to the goods in question, if he states generally that they are "guaranteed" the provisions of this section may furnish a guide to the content of the resulting express warranty. This has particular significance in the case of second-hand sales, and has further significance in limiting the effect of fine-print disclaimer clauses where their effect would be inconsistent with large-print assertions of "guarantee".

5. The second sentence of subsection (1) covers the warranty with respect to food and drink. Serving food or drink for value is a sale, whether to be consumed on the premises or elsewhere. Cases to the contrary are rejected. The principal warranty is that stated in subsections (1) and (2)(c) of this section.

6. Subsection (2) does not purport to exhaust the meaning of "merchantable" nor to negate any of its attributes not specifically mentioned in the text of the statute, but arising by usage of trade or through case law. The language used is "must be at least such as . . . ," and the intention is to leave open other possible attributes of merchantability.

7. Paragraphs (a) and (b) of subsection (2) are to be read together. Both refer, as indicated above, to the standards of that line of the trade which fits the transaction and the seller's business. "Fair average" is a term directly appropriate to agricultural bulk products and means goods centering around the middle belt of quality, not the least or the worst that can be understood in the particular trade by the designation, but such as can pass "without objection." Of course a fair percentage of the least is permissible but the goods are not "fair average" if they are all of the least or worst quality possible under the description. In cases of doubt as to what quality is intended, the price at which a merchant closes a contract is an excellent index of the nature and scope of his obligation under the present section.

8. Fitness for the ordinary purposes for which goods of the type are used is a fundamental concept of the present section and is covered in paragraph (c). As stated above, merchantability is also a part of the obligation owing to the purchaser for use. Correspondingly, protection, under this aspect of the warranty, of the person buying for resale to the ultimate consumer is equally necessary, and merchantable goods must therefore be "honestly" resalable in the normal course of business because they are what they purport to be.

9. Paragraph (d) on evenness of kind, quality and quantity follows case law. But precautionary language has been added as a reminder of the frequent usages of trade which permit substantial variations both with and without an allowance or an obligation to replace the varying units.

10. Paragraph (e) applies only where the nature of the goods and of the transaction require a certain type of container, package or label. Paragraph (f) applies, on the other hand, wherever there is a label or container on which representations are made, even though the original contract, either by express terms or usage of trade, may not have required either the labelling or the representation. This follows from the general obligation of good faith which requires that a buyer should not be placed in the position of reselling or using goods delivered under false representations appearing on the package or container. No problem of extra consideration arises in this connection since, under this Chapter, an obligation is imposed by the original contract not to deliver mislabeled articles, and the obligation is imposed where mercantile good faith so requires and without reference to the doctrine of consideration.

11. Exclusion or modification of the warranty of merchantability, or of any part of it, is dealt with in the section to which the text of the present section makes explicit precautionary references. That section must be read with particular reference to its subsection (4) on limitation of remedies. The warranty of merchantability, wherever it is normal, is so commonly taken for granted that its exclusion from the contract is a matter threatening surprise and therefore requiring special precaution.

12. Subsection (3) is to make explicit that usage of trade and course of dealing can create warranties and that they are implied rather than express warranties and thus subject to exclusion or modification under Section 30-2-316. A typical instance would be the obligation to provide pedigree papers to evidence conformity of the animal to the contract in the case of a pedigreed dog or blooded bull.

13. In an action based on breach of warranty, it is of course necessary to show not only the existence of the warranty but the fact that the warranty was broken and that the breach of the warranty was the proximate cause of the loss sustained. In such an action an affirmative showing by the seller that the loss resulted from some action or event following his own delivery of the goods can operate as a defense. Equally, evidence indicating that the seller exercised care in the manufacture, processing or selection of the goods is relevant to the issue of whether the warranty

was in fact broken. Action by the buyer following an examination of the goods which ought to have indicated the defect complained of can be shown as matter bearing on whether the breach itself was the cause of the injury.

Case Notes

Failure to Warn Claims Available to Bystanders: A youth pitcher died after being struck in the head by a ball hit by a bat manufactured and sold by the defendant. His parents brought claims for design defect and failure to warn against the bat manufacturer. The bat manufacturer argued that a failure to warn claim is available to only the actual user or purchaser of the bat, and not to bystanders. Citing Streich v. Hilton-Davis, 214 Mont. 44, 692 P.2d 440 (1984), and Hagen v. Dow Chem. Co., 261 Mont. 487, 863 P.2d 413 (1993), the Supreme Court concluded that Montana's product liability jurisprudence permits a person who is neither the actual user nor the purchaser of the product to file a failure to warn claim. In this case, the bat manufacturer was subject to liability for all of the baseball players for inadequately communicating the potential risk of harm posed by the bat. Patch v. Hillerich & Bradsby Co., 2011 MT 175, 361 Mont. 241, 257 P.3d 383.

Feasibility of Providing Warning — Jury Question: Defendant baseball bat manufacturer argued that providing a warning to bystanders about the use of a bat was "unworkable" and that the District Court erred in not granting it summary judgment on the plaintiffs' failure to warn claim. The Supreme Court affirmed the District Court's ruling that the feasibility of providing a warning to bystanders was a question for the jury and was not proper for summary judgment. Patch v. Hillerich & Bradsby Co., 2011 MT 175, 361 Mont. 241, 257 P.3d 383.

Foreseeability Not Required in Breach of Contract Action Under Uniform Commercial Code When Injury Results From Breach of Warranty: A breach of contract action under the Uniform Commercial Code does not require foreseeability if injury to person or property proximately results from any breach of warranty. Rothing v. Kallestad, 2007 MT 109, 337 M 193, 159 P3d 222 (2007).

Negligence and Strict Liability Action for Damages by Pesticide Not Preempted by FIFRA — McAlpine Overruled: Plaintiffs brought an action for damages allegedly suffered when a pesticide was applied at the building where they worked. The District Court granted summary judgment for the pesticide manufacturer on the basis that the claims were preempted by the Federal Insecticide, Fungicide, and Rodenticide Act (FIFRA) and McAlpine v. Rhone-Poulenc Ag Co., 285 M 224, 947 P2d 474 (1997), because all of the theories of liability were based on inclusions in or omissions from the pesticide labels. In particular, 7 U.S.C. 136v(b) provides that a state may not impose or continue in effect any requirement for labeling or packaging in addition to or different from those required under the federal law. On appeal, the Supreme Court overruled McAlpine and instead applied Medtronic, Inc. v. Lohr, 518 US 470 (1996), concluding that Congress, through FIFRA, intended only to preempt states from imposing positive law requirements in the form of regulations and laws and did not intend to extinguish damage remedies under state common law. The word "requirements" in section 136v(b) means enactments of positive law by legislative or administrative bodies, not state law damage actions. The case was reversed and remanded for further proceedings. Sleath v. West Mont Home Health Serv., Inc., 2000 MT 381, 304 M 1, 16 P3d 1042, 57 St. Rep. 1629 (2000).

Damage to Crops by Herbicide — Extent of Preemption by FIFRA — Claims for Breach of Express and Implied Warranty Not Preempted — Negligence and Strict Liability Preempted — Remedy for Prevention of Discovery by Summary Judgment: McAlpine applied Weedone LV6, a herbicide manufactured by Rhone-Poulenc and distributed by Ben Taylor, to crops of barley and spring wheat. After several weeks of cool morning temperatures, McAlpine noticed damage to his crops, which experts from Montana State University (now Montana State University-Bozeman) and the Montana Department of Agriculture said was caused by cool temperatures after application of the herbicide. The McAlpines brought a civil action against Rhone-Poulenc, claiming damages from negligence, breach of express and implied warranty, and strict liability. The District Court granted summary judgment for the defendants on the basis that the plaintiffs' claims were based on deficiencies in the label on Weedone LV6 and that those claims were preempted by the Federal Insecticide, Fungicide, and Rodenticide Act (FIFRA). Citing Wis. Pub. Intervenor v. Mortier, 501 US 597 (1991), and Cipollone v. Liggett Group, Inc., 505 US 504 (1992), the Supreme Court interpreted the FIFRA preemption statement, 7 U.S.C. 136v(b), to preempt only claims based upon negligence in labeling and not to preempt the appellants' claims based upon either express or implied warranty or strict liability. Therefore, the Supreme Court held that the appellants must be given the opportunity to prove that Rhone-Poulenc and Ben Taylor breached their warranty by designing, manufacturing, and marketing a product that was inherently defective and that the same defendants are strictly liable for designing, manufacturing, and marketing an unreasonably dangerous product. In response to Rhone-Poulenc's argument that the McAlpines failed to offer any evidence to defeat summary judgment, the Supreme Court pointed out that because the District Court granted summary judgment, the McAlpines were prevented from conducting complete discovery and that until discovery was completed, it was premature for the Supreme Court to conclude that the McAlpines' evidence was insufficient. McAlpine v. Rhone-Poulenc Ag Co., 285 M 224, 947 P2d 474, 54 St. Rep. 1123 (1997), overruled in Sleath v. West Mont Home Health Serv., Inc., 2000 MT 381, 304 M 1, 16 P3d 1042, 57 St. Rep. 1629 (2000), holding that state common-law negligence and strict liability claims based on or implicating pesticide labels are not preempted by FIFRA. Following the 1997 remand of McAlpine, the McAlpines settled with Ben Taylor, Inc., and proceeded to trial against Rhone-Poulenc on a theory of strict products liability, claiming that Weedone LV6 was a defective product because its propensity to damage or destroy crops in conjunction with cold weather was a danger outside the expectations of the ordinary consumer. Rhone-Poulenc acknowledged that the crop damage was caused by the phenoxy herbicide, but argued that the damage was not unreasonably dangerous and that liability exists only when a product is sufficiently dangerous. The trial court instructed the jury that it must find that the herbicide was in a "defective condition unreasonably dangerous", rather than merely in a defective condition, and the jury returned a verdict for Rhone-Poulenc. The McAlpines appealed. The Supreme Court previously held in McJunkin v. Kaufman, 229 M 432, 748 P2d 910 (1987), that a product is defective if it is unreasonably dangerous, but a plaintiff is not required to show that a product is defective and also that it is unreasonably dangerous, because establishing that a product is unreasonably dangerous is merely a means of proving that it is defective. Thus, the "defective condition unreasonably dangerous" language creates a vague and imprecise dual test and should not have been submitted to the jury because it was not plain, clear, and concise. The jury should have been required to find merely that the product was in a defective condition, so the case was again remanded. Further, the decision in Sleath, id., also applied on remand, so evidence of the product label was admissible in further proceedings. McAlpine v. Rhone-Poulenc Ag Co., 2000 MT 383, 304 M 31, 16 P3d 1054, 57 St. Rep. 1644 (2000).

Absence of Evidence of Defective Vehicle Window Design — Failure to Warn Not Defect — Jury Verdict Affirmed: As Wise drove a Ford Escort through a car wash, one of the side windows imploded when water was sprayed on it, injuring Wise, who sued Ford Motor Company for damages. The District Court properly applied the standards of product tort liability, including Ford's liability for failure to warn of a danger in its product as a separate theory of product liability. Alternate causes of the breakage were not necessarily eliminated, and the jury could have found that Wise did not meet his burden of proof by way of circumstantial evidence. The jury found in favor of Ford. Evidence supported the verdict that the vehicle was not defectively designed or defective for Ford's failure to warn that the side windows could break. Because the jury had substantial evidence upon which to base its decision that the vehicle did not have an unreasonably dangerous defective condition, judgment was affirmed. Wise v. Ford Motor Co., 284 M 336, 943 P2d 1310, 54 St. Rep. 909 (1997).

Buyer Entitled to Damages for Shipment of Damaged Plants: Reed owned a greenhouse and ordered a shipment of poinsettias from McCalif for Christmas. When the plants arrived, many were damaged. Reed refused to pay $3,027.09 for the marketable plants that he kept and resold, contending that he had lost $8,683.95 on the damaged plants for which he had already received purchase orders from other buyers. The Supreme Court held that the record proved that there was no other source for replacement of the damaged plants and that McCalif was aware of that fact and the fact that Reed had entered into contracts for the resale of the plants. The Supreme Court ruled that Reed had the right to accept part of the plants received and reject the rest and that Reed was entitled to incidental and consequential damages because of McCalif's breach. The measure of damages was the difference between what Reed owed for the plants that he kept and what he lost on the orders that he could not fill. McCalif Grower Supplies, Inc. v. Reed, 272 M 254, 900 P2d 880, 52 St. Rep. 659 (1995).

Abuse of Product: Plaintiff brought suit after the engine of his 2-year-old truck quit running. The truck had 42,000 miles on it at the time. Defendant refused to repair the truck under warranty. Testimony indicated that there was significant damage to the truck. The evidence of the condition of the truck indicated that the truck was abused and that the abuse directly affected the engine's performance. There was substantial evidence to support a verdict for the defendant. Owens v. Gen. Motors Corp., 249 M 124, 813 P2d 985, 48 St. Rep. 608 (1991).

Disclaimer on Back of Purchase Agreement Not Per Se Sufficient to Render Disclaimer Ineffective: Plaintiffs contended that a disclaimer of warranty of merchantability was invalid because there was no evidence they ever saw or were made aware of the disclaimer or were made aware of its significance. The Supreme Court noted that the disclaimer was not hidden in the fine print but was in larger, darker, bolder type and was capitalized and underlined. The fact that the disclaimer appeared on the back of the purchase agreement was not per se sufficient to render it ineffective because a person is presumed to have read contractual agreements he enters into. McJunkin v. Kaufman, 229 M 432, 748 P2d 910, 44 St. Rep. 2111 (1987).

Failure to Prove Unreasonably Dangerous Defective Condition — Proper Test of Defective Product: The Supreme Court adopted a modified approach to the test of strict liability as defined by sec. 402A, Restatement (Second) of Torts, in holding that while a product is defective if it is unreasonably dangerous, the lack of a dangerous aspect does not automatically preclude a finding that the product is defective. The proper test of a defective product is whether the product is unreasonably unsuitable for its intended or foreseeable purpose. McJunkin v. Kaufman, 229 M 432, 748 P2d 910, 44 St. Rep. 2111 (1987).

Factors to Be Considered in Alternative Design Products Liability Case: Recognizing that all factors may not be appropriate in every case and that additional factors should be considered where appropriate, the court found that the following factors should be considered in an alternative design product liability case:

"(1) A manufacturer who sells a product in a defective condition unreasonably dangerous because of a design defect is subject to liability for harm thereby caused to the ultimate user.

(2) A product may be in a defective condition unreasonably dangerous if the manufacturer should have used an alternative design.

(3) In determining whether an alternative design should have been used, the jury should balance so many of the following factors as it finds to be pertinent at the time of manufacture:

(a) The reasonable probability that the product as originally designed would cause serious harm to the claimant.

(b) Consideration of the reasonable probability of harm from the use of the original product as compared to the reasonable probability of harm from the use of the product with the alternative design.

(c) The technological feasibility of an alternative design that would have prevented claimant's harm.

(d) The relative costs both to the manufacturer and the consumer of producing, distributing and selling the original product as compared to the product with the alternative design.

(e) The time reasonably required to implement the alternative design." Rix v. Gen. Motors Corp., 222 M 318, 723 P2d 195, 43 St. Rep. 1296 (1986), followed in Krueger v. Gen. Motors Corp., 240 M 266, 783 P2d 1340, 46 St. Rep. 2114 (1989).

Manufacturing Defects Defined: In finding jury instructions to be adequate, the court held that the essential question was whether the product was flawed or defective because it was not constructed correctly by the manufacturer. The court quoted from Caprara v. Chrysler Corp., 436 N.Y.S.2d 251 (1981), saying: "Manufacturing defects, by definition, are "imperfections that inevitably occur in a typically small percentage of products of a given design as a result of the fallibility of the manufacturing process. A defectively manufactured product does not conform in some significant aspect to the intended design, nor does it conform to the great majority of products manufactured in accordance with that design." Stated differently, a defectively manufactured product is flawed because it is misconstructed without regard to whether the intended design of the manufacturer was safe or not. Such defects result from some mishap in the manufacturing process itself, improper workmanship, or because defective materials were used in construction." Rix v. Gen. Motors Corp., 222 M 318, 723 P2d 195, 43 St. Rep. 1296 (1986), followed in Krueger v. Gen. Motors Corp., 240 M 266, 783 P2d 1340, 46 St. Rep. 2114 (1989).

Duty to Warn of Known Danger — Lack of Warning of Known Danger as Defect: In a tort action over injury caused by a hay baler, the Supreme Court held, based on the holding of Brown v. N. Am. Mfg. Co., 176 M 98, 576 P2d 711 (1978), that it was error to instruct the jury that a manufacturer has no duty to warn a person who claims to be entitled to a warning if the person actually knows of the danger. Under the facts of this case, there is a duty to warn of a known danger if the product is unreasonably dangerous and lack of such warning can make an otherwise nondefective product defective. Tacke v. Vermeer Mfg. Co., 220 M 1, 713 P2d 527, 43 St. Rep. 123 (1986). Recognition of a failure to warn claim and the Brown criteria were applied in Riley v. Am. Honda Motor Co., Inc., 259 M 128, 856 P2d 196, 50 St. Rep. 714 (1993). See also Emery v. Federated Foods, Inc., 262 M 83, 863 P2d 426, 50 St. Rep. 1454 (1993).

Products Liability — Breach of Warranties — No Privity Requirement: Goods are not merchantable if, in their ordinary use, the goods cause damage to the property to which they are applied or harm to the person using them. Potato sprout suppressant that caused erratic growing results in potato crop was nonmerchantable because in its ordinary use it caused damage to property to which it was applied. There was also a breach of warranty of fitness because manufacturer's representative knew the use for which plaintiff purchased product. The privity requirement has been abolished in Montana, and a remote manufacturer may be liable for breach of implied warranties. Streich v. Hilton-Davis, 214 M 44, 692 P2d 440, 41 St. Rep. 2310 (1984).

Products Liability — Failure to Warn of Adverse Side Effects — Expert Witness Testimony Not Necessary to Establish Standard of Care: Plaintiffs sued manufacturer of chemical potato sprout suppressant when use of product caused erratic growing results in potato crop. Plaintiffs' expert witness made no declaration as to failure to warn or that product was defective. Expert witness gave results of field tests that revealed decided risk of adverse side effects against which manufacturer did not warn. Supreme Court held that expert witness testimony was not necessary to establish standard of care owed by manufacturer to plaintiffs and that defendant breached that standard because any layman could understand insufficiency of warning. Evidence was sufficient to establish duty to warn of adverse side effects and that manufacturer breached that duty. Streich v. Hilton-Davis, 214 M 44, 692 P2d 440, 41 St. Rep. 2310 (1984).

Products Liability — Negligence — Duty of Care: A manufacturer has a duty to use reasonable care to give warning of dangerous condition of a product to those he expects to use the product or those endangered by its foreseeable use. Streich v. Hilton-Davis, 214 M 44, 692 P2d 440, 41 St. Rep. 2310 (1984), followed in Krueger v. Gen. Motors Corp., 240 M 266, 783 P2d 1340, 46 St. Rep. 2114 (1989).

Products Liability — Strict Liability Applicable in Commercial Case — Failure to Warn — Jury Instructions: Plaintiffs, potato growers, sued manufacturer of chemical potato sprout suppressant that caused potato crop to show delayed and erratic emergence, multiple sprouting, a heavy tuber set resulting in small potatoes, and reduced yield. The only warning on the bag was a statement that after planting there might be a "slight delay in emergence depending on weather conditions and variety". District Court jury found defendant liable for damages based on theories of strict liability in tort, negligence, and breach of warranties. Supreme Court affirmed judgment and damage award. Supreme Court held that theory of strict liability applies in a case of lost profits in a purely commercial setting not involving personal injury. Supreme Court stated that when the defect involves an inadequate warning, the test of Restatement (Second) of Torts, section 402(a), is met, i.e., the product is "in a defective condition unreasonably dangerous" to the user or to his property. Use of accepted form instructions for personal injury strict liability cases that were modified to fit a property damage case were not error. Streich v. Hilton-Davis, 214 M 44, 692 P2d 440, 41 St. Rep. 2310 (1984).

Products Liability — When Only Damage Done to Defective Product Itself: A claim of strict liability in tort can be maintained when the only injury suffered is to the product itself. Thompson v. Nebr. Mobile Homes Corp., 198 M 461, 647 P2d 334, 39 St. Rep. 1094 (1982).

Modular Home — Applicable Warranty Law: Sale of modular home manufactured at defendant's plant and delivered to plaintiffs' building site was governed by the U.C.C. warranty provisions and not the warranty provisions of Title 30, ch. 11, part 2, which are made inapplicable by 30-11-224. The fact that defendant had charge of the home until after it was affixed to plaintiffs' foundation and no longer had mobility did not affect the applicability of the U.C.C. warranty provisions, for the home was manufactured to plaintiffs' specifications, was thus identified to the contract under the U.C.C. at the time of the first step of its production, was movable at that time, and thus was "goods" the sale of which the U.C.C. applied. Little v. Grizzly Mfg., 195 M 419, 636 P2d 839, 38 St. Rep. 1994 (1981).

Implied Warranty of Merchantability Inapplicable to Lease: Defendant leased a truck from plaintiff. The truck was in the shop many times, and after an accident and long delays in obtaining parts, defendant defaulted on the lease. Plaintiff sued for amounts owing under the lease, and defendant counterclaimed for breach of the implied warranty of merchantability. The implied warranty of merchantability is only applicable in the event of a "sale" as defined in the Uniform Commercial Code. On the basis of the definition of sale and language contained in the lease agreement, the Supreme Court found that the implied warranty of merchantability was not applicable. R&W Leasing v. Mosher, 195 M 285, 636 P2d 832, 38 St. Rep. 1857 (1981).

Proof of Credit Purchase — Requisite Proof of Warranty Breach: In an action to collect the purchase price of tires purchased on credit, the defendant (buyer) filed a counterclaim for breach of warranty against the plaintiff. The defendant's counterclaim properly was denied because the defendant had failed to prove a prima facie case. Defendant appealed that there was no proof of some of the purchases. The Supreme Court said that an open account between the seller and buyer can be proved by evidence that the seller's records show that the goods were sold, that invoices had been sent to the buyer who failed to object to them, and that the seller's records are accurate. Here the buyer's rebuttal testimony was indefinite, and credibility was a trial court question. No breach of warranty was proven; only the testimony of the buyer was given and no solid evidence, such as any tires, records of the amount of use of the tires, or maintenance records, was produced. This, with findings of possible alternative causes of the problems with the tires, was a sufficient record to support the finding that breach of warranty was not proved by sufficient evidence. Defendant therefore was liable for the price of the tires. D&K Distrib. v. Ford, 189 M 505, 616 P2d 1097, 37 St. Rep. 1693 (1980).

Sale of Sprinkler Irrigation Equipment: The evidence supported the court's findings that implied warranties of merchantability and fitness for a particular purpose did exist in a transaction for the sale of sprinkler irrigation equipment and that they were breached. Whitaker v. Farmhand, Inc., 173 M 345, 567 P2d 916 (1977).

Proof of Manufacturer Defect: The court did not err in granting defendants' motion for directed verdict when plaintiff failed to prove that the defect that caused an engine fire existed when the vehicle left the hands of the defendants — a necessary element in breach of implied warranty of merchantability, strict liability, and res ipsa loquitur legal theories. St. Paul Mercury Ins. Co. v. Jeep Corp. & Am. Motors Sales, 175 M 69, 572 P2d 204 (1977).

Breach of Warranty — Cattle Breeding: Implied warranties of merchantability and fitness were not met by artificial insemination service which sold semen to cattle rancher who had experienced a 95% calf crop via natural service prior to using artificial insemination, where the rancher experienced a 70% calf crop with artificial insemination in the first year and only a 7% calf crop in the second year using semen from the same bull under almost identical conditions. The only logical inference was that the semen purchased for use in the second year was defective. Waddell v. Am. Breeders Serv. Inc., 161 M 221, 505 P2d 417, 61 ALR 3d 801 (1973).

Law Review Articles

Developments in Montana Products Liability Law, 1977-1987, Bronson, 48 Mont. L. Rev. 297, 313 through 317 (1987).

Comparative Principles and Products Liability in Montana, 41 Mont. L. Rev. 269 (1980).

Products Liability, Tobias & Rossbach, 38 Mont. L. Rev. 221 (1977).

30-2-315. Implied warranty — fitness for particular purpose.

Official Comment

Prior Uniform Statutory Provision: Section 15(1), (4), (5), Uniform Sales Act.

Changes: Rewritten.

Purposes of Changes:

1. Whether or not this warranty arises in any individual case is basically a question of fact to be determined by the circumstances of the contracting. Under this section the buyer need not bring home to the seller actual knowledge of the particular purpose for which the goods are intended or of his reliance on the seller's skill and judgment, if the circumstances are such that the seller has reason to realize the purpose intended or that the reliance exists. The buyer, of course, must actually be relying on the seller.

2. A "particular purpose" differs from the ordinary purpose for which the goods are used in that it envisages a specific use by the buyer which is peculiar to the nature of his business whereas the ordinary purposes for which goods are used are those envisaged in the concept of merchantability and go to uses which are customarily made of the goods in question. For example, shoes are generally used for the purpose of walking upon ordinary ground, but a seller may know that a particular pair was selected to be used for climbing mountains.

A contract may of course include both a warranty of merchantability and one of fitness for a particular purpose.

The provisions of this Chapter on the cumulation and conflict of express and implied warranties must be considered on the question of inconsistency between or among warranties. In such a case any question of fact as to which warranty was intended by the parties to apply must be resolved in favor of the warranty of fitness for particular purpose as against all other warranties except where the buyer has taken upon himself the responsibility of furnishing the technical specifications.

3. In connection with the warranty of fitness for a particular purpose the provisions of this Chapter on the allocation or division of risks are particularly applicable in any transaction in which the purpose for which the goods are to be used combines requirements both as to the quality of the goods themselves and compliance with certain laws or regulations. How the risks are divided is a question of fact to be determined, where not expressly contained in the

agreement, from the circumstances of contracting, usage of trade, course of performance and the like, matters which may constitute the "otherwise agreement" of the parties by which they may divide the risk or burden.

4. The absence from this section of the language used in the Uniform Sales Act in referring to the seller, "whether he be the grower or manufacturer or not," is not intended to impose any requirement that the seller be a grower or manufacturer. Although normally the warranty will arise only where the seller is a merchant with the appropriate "skill or judgment," it can arise as to nonmerchants where this is justified by the particular circumstances.

5. The elimination of the "patent or other trade name" exception constitutes the major extension of the warranty of fitness which has been made by the cases and continued in this Chapter. Under the present section the existence of a patent or other trade name and the designation of the article by that name, or indeed in any other definite manner, is only one of the facts to be considered on the question of whether the buyer actually relied on the seller, but it is not of itself decisive of the issue. If the buyer himself is insisting on a particular brand he is not relying on the seller's skill and judgment and so no warranty results. But the mere fact that the article purchased has a particular patent or trade name is not sufficient to indicate nonreliance if the article has been recommended by the seller as adequate for the buyer's purposes.

6. The specific reference forward in the present section to the following section on exclusion or modification of warranties is to call attention to the possibility of eliminating the warranty in any given case. However it must be noted that under the following section the warranty of fitness for a particular purpose must be excluded or modified by a conspicuous writing.

Case Notes

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Reliance on Expertise — Implied Warranty of Fitness for Particular Purpose: Defendant relied on plaintiff's expertise to select an affordable fire alarm system that would provide reliable protection for the hotel's property and guests. Where the seller is aware that the buyer is relying upon the seller's judgment to select suitable goods, an implied warranty that the goods are fit for that particular purpose is created. The system installed was complicated, difficult to use, and frequently malfunctioned. Defendant advised plaintiff of the failure of the system after a fire in the snack bar, which was prior to the fire in a guest room that eventually resulted in this action. Plaintiff's own records showed repeated notifications of problems with the system. This was reasonable notice under 30-2-607(3). The implied warranty of fitness for a particular purpose was breached, and defendant was entitled to recover loss in value of the goods plus consequential and incidental damages. Fire Supply & Serv., Inc. v. Chico Hot Springs, 196 M 435, 639 P2d 1160, 39 St. Rep. 231 (1982).

Disclaimer Not Conspicuous: The disclaimer of warranties in an agreement is ineffective to exclude an implied warranty of fitness for a particular purpose since the disclaimer is in the same typeface as the rest of the contract and is not indented, underlined, or inked in a contrasting color to comply with the provision of the code requiring conspicuousness. Transcont. Refrigeration Co. v. Figgins, 179 M 12, 585 P2d 1301 (1978).

Sale of Sprinkler Irrigation Equipment: The evidence supported the court's findings that implied warranties of merchantability and fitness for a particular purpose did exist in a transaction for the sale of sprinkler irrigation equipment and that they were breached. Whitaker v. Farmhand, Inc., 173 M 345, 567 P2d 916 (1977).

Amendment of Complaint: Granting plaintiff's motion to amend complaint to include theory of implied warranty of fitness for a particular purpose was error when motion was presented shortly before trial and plaintiff had relied upon theory of negligence through the entire course of pretrial proceedings. Warranty theory was foreign to the proper pleading of the case and required defendant to be prepared for an entirely different defense theory. McGuire v. Nelson, 162 M 37, 508 P2d 558 (1973).

Breach of Warranty — Cattle Breeding: Implied warranties of merchantability and fitness were not met by artificial insemination service which sold semen to cattle rancher who had experienced a 95% calf crop via natural service prior to using artificial insemination, where the rancher experienced a 70% calf crop with artificial insemination in the first year and only a 7% calf crop in the second year using semen from the same bull under almost identical conditions. The only logical inference was that the semen purchased for use in the second year was defective. Waddell v. Am. Breeders Serv. Inc., 161 M 221, 505 P2d 417, 61 ALR 3d 801 (1973).

30-2-316. Exclusion or modification of warranties.

Official Comment

Prior Uniform Statutory Provision: None. See Sections 15 and 71, Uniform Sales Act.

Purposes:

1. This section is designed principally to deal with those frequent clauses in sales contracts which seek to exclude "all warranties, express or implied." It seeks to protect a buyer from unexpected and unbargained language of disclaimer by denying effect to such language when inconsistent with language of express warranty and permitting the exclusion of implied warranties only by conspicuous language or other circumstances which protect the buyer from surprise.

2. The seller is protected under this Chapter against false allegations of oral warranties by its provisions on parol and extrinsic evidence and against unauthorized representations by the customary "lack of authority" clauses. This Chapter treats the limitation or avoidance of consequential damages as a matter of limiting remedies for breach, separate from the matter of creation of liability under a warranty. If no warranty exists, there is of course no problem of limiting remedies for breach of warranty. Under subsection (4) the question of limitation of remedy is governed by the sections referred to rather than by this section.

3. Disclaimer of the implied warranty of merchantability is permitted under subsection (2), but with the safeguard that such disclaimers must mention merchantability and in case of a writing must be conspicuous.

4. Unlike the implied warranty of merchantability, implied warranties of fitness for a particular purpose may be excluded by general language, but only if it is in writing and conspicuous.

5. Subsection (2) presupposes that the implied warranty in question exists unless excluded or modified. Whether or not language of disclaimer satisfies the requirements of this section, such language may be relevant under other sections to the question whether the warranty was ever in fact created. Thus, unless the provisions of this Chapter on parol and extrinsic evidence prevent, oral language of disclaimer may raise issues of fact as to whether reliance by the buyer occurred and whether the seller had "reason to know" under the section on implied warranty of fitness for a particular purpose.

6. The exceptions to the general rule set forth in paragraphs (a), (b) and (c) of subsection (3) are common factual situations in which the circumstances surrounding the transaction are in themselves sufficient to call the buyer's attention to the fact that no implied warranties are made or that a certain implied warranty is being excluded.

7. Paragraph (a) of subsection (3) deals with general terms such as "as is," "as they stand," "with all faults," and the like. Such terms in ordinary commercial usage are understood to mean that the buyer takes the entire risk as to the quality of the goods involved. The terms covered by paragraph (a) are in fact merely a particularization of paragraph (c) which provides for exclusion or modification of implied warranties by usage of trade.

8. Under paragraph (b) of subsection (3) warranties may be excluded or modified by the circumstances where the buyer examines the goods or a sample or model of them before entering into the contract. "Examination" as used in this paragraph is not synonymous with inspection before acceptance or at any other time after the contract has been made. It goes rather to the nature of the responsibility assumed by the seller at the time of the making of the contract. Of course if the buyer discovers the defect and uses the goods anyway, or if he unreasonably fails to examine the goods before he uses them, resulting injuries may be found to result from his own action rather than proximately from a breach of warranty. See Sections 30-2-314 and 30-2-715 and comments thereto.

In order to bring the transaction within the scope of "refused to examine" in paragraph (b), it is not sufficient that the goods are available for inspection. There must in addition be a demand by the seller that the buyer examine the goods fully. The seller by the demand puts the buyer on notice that he is assuming the risk of defects which the examination ought to reveal. The language "refused to examine" in this paragraph is intended to make clear the necessity for such demand.

Application of the doctrine of "caveat emptor" in all cases where the buyer examines the goods regardless of statements made by the seller is, however, rejected by this Chapter. Thus, if the offer of examination is accompanied by words as to their merchantability or specific attributes and the buyer indicates clearly that he is relying on those words rather than on his examination, they give rise to an "express" warranty. In such cases the question is one of fact as to whether a warranty of merchantability has been expressly incorporated in the agreement. Disclaimer of such an express warranty is governed by subsection (1) of the present section.

The particular buyer's skill and the normal method of examining goods in the circumstances determine what defects are excluded by the examination. A failure to notice defects which are obvious cannot excuse the buyer. However, an examination under circumstances which do not permit chemical or other testing of the goods would not exclude defects which could be ascertained only by such testing. Nor can latent defects be excluded by a simple examination. A professional buyer examining a product in his field will be held to have assumed the risk as to all defects which a professional in the field ought to observe, while a nonprofessional buyer will be held to have assumed the risk only for such defects as a layman might be expected to observe.

9. The situation in which the buyer gives precise and complete specifications to the seller is not explicitly covered in this section, but this is a frequent circumstance by which the implied warranties may be excluded. The warranty of fitness for a particular purpose would not normally arise since in such a situation there is usually no reliance on the seller by the buyer. The warranty of merchantability in such a transaction, however, must be considered in connection with the next section on the cumulation and conflict of warranties. Under paragraph (c) of that section in case of such an inconsistency the implied warranty of merchantability is displaced by the express warranty that the goods will comply with the specifications. Thus, where the buyer gives detailed specifications as to the goods, neither of the implied warranties as to quality will normally apply to the transaction unless consistent with the specifications.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

1983 Amendment: Inserted (3)(e) excluding implied warranties for seed sales.

Montana Subsection: Subsections 3(d) and 3(e) are not part of the U.C.C. as promulgated by the American Law Institute. Subsection 3(d) was added by the Montana Legislature in sec. 1, Ch. 95, L. 1979. Subsection 3(e) was added by the Montana Legislature in sec. 1, Ch. 33, L. 1983.

Case Notes

Implied Warranty Established by Notice Regarding Sale of Service Contract and Resulting Rights: The dealer of a used car attempted to sell the car "as is" but also sold the customer a service contract. A notice stated that upon the sale of the service contract, state law implied warranties "may give you additional rights". Because of this notice and regardless of the "as is" disclaimers, the dealer failed to disclaim statutory implied warranties under this section, and an implied warranty was established. Payne v. Berry's Auto, Inc., 2013 MT 102, 369 Mont. 529, 301 P.3d 804.

Warranty of Title Not Subject to Disclaimers as to Fitness and Merchantability: Defendant pawnshop operator who sold stolen property to plaintiff refused to give plaintiff a refund after the property was recovered by police. Defendant argued that he disclaimed any warranty of title to goods sold in his business by posting a sign alerting buyers that merchandise is sold "as is" and by writing the same notation on his sales slips. Warranty of title is not subject to the disclaimers found in this section pertaining to fitness and merchantability. Defendant's conduct does not meet the disclaimer of warranty of title found in 30-2-312 because there was no agreement between defendant and plaintiff regarding the title of the goods. Brokke v. Williams, 235 M 305, 766 P2d 1311, 46 St. Rep. 6 (1989).

Disclaimer on Back of Purchase Agreement Not Per Se Sufficient to Render Disclaimer Ineffective: Plaintiffs contended that a disclaimer of warranty of merchantability was invalid because there was no evidence they ever saw or were made aware of the disclaimer or were made aware of its significance. The Supreme Court noted that the disclaimer was not hidden in the fine print but was in larger, darker, bolder type and was capitalized and underlined. The fact that the disclaimer appeared on the back of the purchase agreement was not per se sufficient to render it ineffective because a person is presumed to have read contractual agreements he enters into. McJunkin v. Kaufman, 229 M 432, 748 P2d 910, 44 St. Rep. 2111 (1987).

Warranties — When Created — When Disclaimed: Plaintiffs brought an action against a farm implement company for breach of implied warranties of merchantability and fitness. The court noted that the Montana U.C.C. allows a seller to disclaim these implied warranties by means of "conspicuous" language in a writing. It was found the disclaimers in this case were sufficiently conspicuous to be effective under 30-2-316. The plaintiffs claimed the advertising, promotional materials, and operator's manual created express warranties under 30-2-313. The court held the disclaimers did not destroy the express warranty of safety made in the operator's manual. Schlenz v. John Deere Co., 511 F. Supp. 224, 38 St. Rep. 579 (D.C. Mont. 1981).

Effect of "As Is" Clause in Used Car Sales Agreement: When defendant failed to inspect a car for defects before sale to plaintiff and the defect that was the proximate cause of plaintiff's accident and subsequent injuries would have been discovered in a reasonable safety inspection, defendant should not be allowed to hide behind the cloak of a simple "as is" disclaimer. Public policy requires a used car dealer to inspect the cars he sells and to make sure they are in safe, working condition. Kopischke v. First Cont. Corp., 187 M 471, 610 P2d 668 (1980).

Disclaimer Not Conspicuous: The disclaimer of warranties in an agreement is ineffective to exclude an implied warranty of fitness for a particular purpose since the disclaimer is in the same typeface as the rest of the contract and is not indented, underlined, or inked in a contrasting color to comply with the provision of the code requiring conspicuousness. Transcont. Refrigeration Co. v. Figgins, 179 M 12, 585 P2d 1301 (1978).

Disclaimer — Ineffective: A disclaimer or limitation of warranty contained in a manufacturer's manual received by the purchasers subsequent to the sale does not limit recovery for implied or express warranties made prior to or at the time of the sale. Whitaker v. Farmhand, Inc., 173 M 345, 567 P2d 916 (1977), followed in Vandalia Ranch, Inc. v. Farmers Union Oil & Supply Co., 221 M 253, 718 P2d 647, 43 St. Rep. 790 (1986).

Used Farm Equipment — Implied Warranties: Implied warranties of merchantability and fitness for purpose were inapplicable to sale of used farm combine where buyer owned a large farm-ranch operation and had been in the farm business for a substantial length of time and knew or should have known that used machinery was customarily not warranted beyond a sharing of the cost of repairs and he acquiesced in sharing of repair expenses for more than a year. Spurgeon v. Jamieson Motors, 164 M 296, 521 P2d 924 (1974).

30-2-317. Cumulation and conflict of warranties express or implied.

Official Comment

Prior Uniform Statutory Provision: On cumulation of warranties see Sections 14, 15, and 16, Uniform Sales Act.

Changes: Completely rewritten into one section.

Purposes of Changes:

1. The present section rests on the basic policy of this Chapter that no warranty is created except by some conduct (either affirmative action or failure to disclose) on the part of the seller. Therefore, all warranties are made cumulative unless this construction of the contract is impossible or unreasonable.

This Chapter thus follows the general policy of the Uniform Sales Act except that in case of the sale of an article by its patent or trade name the elimination of the warranty of fitness depends solely on whether the buyer has relied on the seller's skill and judgment; the use of the patent or trade name is but one factor in making this determination.

2. The rules of this section are designed to aid in determining the intention of the parties as to which of inconsistent warranties which have arisen from the circumstances of their transaction shall prevail. These rules of intention are to be applied only where factors making for an equitable estoppel of the seller do not exist and where he has in perfect good faith made warranties which later turn out to be inconsistent. To the extent that the seller has led the buyer to believe that all of the warranties can be performed, he is estopped from setting up any essential inconsistency as a defense.

3. The rules in subsections (a), (b) and (c) are designed to ascertain the intention of the parties by reference to the factor which probably claimed the attention of the parties in the first instance. These rules are not absolute but may be changed by evidence showing that the conditions which existed at the time of contracting make the construction called for by the section inconsistent or unreasonable.

30-2-318. Third-party beneficiaries of warranties express or implied.

Official Comment

Prior Uniform Statutory Provision: None.

Purposes:

1. The last sentence of this section does not mean that a seller is precluded from excluding or disclaiming a warranty which might otherwise arise in connection with the sale provided such exclusion or modification is permitted by Section 30-2-316. Nor does that sentence preclude the seller from limiting the remedies of his own buyer and of any beneficiaries, in any manner provided in Sections 30-2-718 or 30-2-719. To the extent that the contract of sale contains provisions under which warranties are excluded or modified, or remedies for breach are limited, such provisions are equally operative against beneficiaries of warranties under this section. What this last sentence forbids is exclusion of liability by the seller to the persons to whom the warranties which he has made to his buyer would extend under this section.

2. The purpose of this section is to give certain beneficiaries the benefit of the same warranty which the buyer received in the contract of sale, thereby freeing any such beneficiaries from any technical rules as to "privity." It seeks to accomplish this purpose without any derogation of any right or remedy resting on negligence. It rests primarily upon the merchant-seller's warranty under this Chapter that the goods sold are merchantable and fit for the ordinary purposes for which such goods are used rather than the warranty of fitness for a particular purpose. Implicit in the section is that any beneficiary of a warranty may bring a direct action for breach of warranty against the seller whose warranty extends to him.

3. The Montana alternative expressly includes as beneficiaries within its provisions the family, household and guests of the purchaser. Beyond this, the section in this form is neutral and is not intended to enlarge or restrict the developing case law on whether the seller's warranties, given to his buyer who resells, extend to other persons in the distributive chain.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Alternative Sections: Montana has adopted alternative A for this section, from the three alternatives proposed to the states.

Case Notes

Breach of Contractual Warranties — Proper Parties — Statute of Frauds: Plaintiffs in an action for breach of express and implied warranties were farmers. Defendants manufactured farm implements. One of the plaintiffs had an arm severed in an accident involving the defendants' machinery. On appeal, the defendants argued that the injured plaintiff was not a party to the purchase contract. The plaintiff alleged the salesman knew that he and the party who actually signed the purchase order were to be co-owners of the hay baler in question. The signature was for the one co-owner for himself and as agent for the plaintiff as well. Because principal and agent law supplements the Montana U.C.C. which covers the purchase of the baler, the court considered applying 28-10-203, which prevents oral authorization to contract when the contract itself must be written, as here. It noted exceptions to the Statute of Frauds, however. The question of whether payment of the purchase price took this contract out of the Statute of Frauds was a genuine issue of material fact preventing a summary judgment for the defendants under the Federal Rules of Civil Procedure. Holding the question one of law, the court said it had to hold an evidentiary hearing on the issues. Schlenz v. John Deere Co., 511 F. Supp. 224, 38 St. Rep. 579 (D.C. Mont. 1981).

Breach of Casket Warranty — Mental Suffering: A contract for the sale of a casket is one of those rare contracts which could give rise to a cause of action for liability based on mental suffering alone and the seller's warranty of casket seal can be recovered upon by members of the family of the buyer. Hirst v. Elgin Metal Casket Co., 438 F. Supp. 906 (D.C. Mont. 1977).

30-2-319. F.O.B. and F.A.S. terms.

Official Comment

Prior Uniform Statutory Provision: None.

Purposes:

1. This section is intended to negate the uncommercial line of decision which treats an "F.O.B." term as "merely a price term." The distinctions taken in subsection (1) handle most of the issues which have on occasion led to the unfortunate judicial language just referred to. Other matters which have led to sound results being based on unhappy language in regard to F.O.B. clauses are dealt with in this Act by Section 30-2-311(2) (seller's option rearrangements relating to shipment) and Sections 30-2-614 and 30-2-615 (substituted performance and seller's excuse).

2. Subsection (1)(c) not only specifies the duties of a seller who engages to deliver "F.O.B. vessel," or the like, but ought to make clear that no agreement is soundly drawn when it looks to reshipment from San Francisco or New York, but speaks merely of "F.O.B." the place.

3. The buyer's obligations stated in subsection (1) (c) and subsection (3) are, as shown in the text, obligations of cooperation. The last sentence of subsection (3) expressly, though perhaps unnecessarily, authorizes the seller, pending instructions, to go ahead with such preparatory moves as shipment from the interior to the named point of delivery. The sentence presupposes the usual case in which instructions "fail"; a prior repudiation by the buyer, giving notice that breach was intended, would remove the reason for the sentence, and would normally bring into play, instead, the second sentence of Section 30-2-704, which duly calls for lessening damages.

4. The treatment of "F.O.B. vessel" in conjunction with F.A.S. fits, in regard to the need for payment against documents, with standard practice and caselaw; but "F.O.B. vessel" is a term which by its very language makes express the need for an "on board" document. In this respect, that term is stricter than the ordinary overseas "shipment" contract (C.I.F., etc., Section 30-2-320).

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

Case Notes

Sufficient Evidence Required to Show Issue of Material Fact — Contracts: The plaintiff entered into a contract with the defendant to provide the defendant with crushed aggregate material from his gravel pit. The defendant no longer needed the aggregate material and refused to pay the final invoices. The Supreme Court held that the District Court properly granted summary judgment to the plaintiff because the defendant failed to present sufficient evidence to establish that an issue of material fact existed regarding the amount of material extracted by the defendant. In addition, the Supreme Court awarded reasonable attorney fees, trial costs, and appeal costs to the plaintiff under 28-2-2105 and remanded the case to determine the fees and costs. Moore v. Goran, LLC, 2017 MT 208, 388 Mont. 340, 400 P.3d 729.

30-2-320. C.I.F. and C.&F. terms.

Official Comment

[*Corresponding U.C.C. Section:* Section 2-320, U.C.C.]

Prior Uniform Statutory Provision: None.

Purposes: To make it clear that:

1. The C.I.F. contract is not a destination but a shipment contract with risk of subsequent loss or damage to the goods passing to the buyer upon shipment if the seller has properly performed all his obligations with respect to the goods. Delivery to the carrier is delivery to the buyer for purposes of risk and "title". Delivery of possession of the goods is accomplished by delivery of the bill of lading, and upon tender of the required documents the buyer must pay the agreed price without awaiting the arrival of the goods and if they have been lost or damaged after proper shipment he must seek his remedy against the carrier or insurer. The buyer has no right of inspection prior to payment or acceptance of the documents.

2. The seller's obligations remain the same even though the C.I.F. term is "used only in connection with the stated price and destination".

3. The insurance stipulated by the C.I.F. term is for the buyer's benefit, to protect him against the risk of loss or damage to the goods in transit. A clause in a C.I.F. contract "insurance — for the account of sellers" should be viewed in its ordinary mercantile meaning that the sellers must pay for the insurance and not that it is intended to run to the seller's benefit.

4. A bill of lading covering the entire transportation from the port of shipment is explicitly required but the provision on this point must be read in the light of its reason to assure the buyer of as full protection as the conditions of shipment reasonably permit, remembering always that this type of contract is designed to move the goods in the channels commercially available. To enable the buyer to deal with the goods while they are afloat the bill of lading must be one that covers only the quantity of goods called for by the contract. The buyer is not required to accept his part of the goods without a bill of lading because the latter covers a larger quantity, nor is he required to accept a bill of lading for the whole quantity under a stipulation to hold the excess for the owner. Although the buyer is not compelled to accept either goods or documents under such circumstances he may of course claim his rights in any goods which have been identified to his contract.

5. The seller is given the option of paying or providing for the payment of freight. He has no option to ship "freight collect" unless the agreement so provides. The rule of the common law that the buyer need not pay the freight if the goods do not arrive is preserved.

Unless the shipment has been sent "freight collect" the buyer is entitled to receive documentary evidence that he is not obligated to pay the freight; the seller is therefore required to obtain a receipt "showing that the freight has been paid or provided for." The usual notation on the bill of lading that the freight has been prepaid is a sufficient receipt, as at common law. The phrase "provided for" is intended to cover the frequent situation in which the carrier extends credit to a shipper for the freight on successive shipments and receives periodical payments of the accrued freight charges from him.

6. The requirement that unless otherwise agreed the seller must procure insurance "of a kind and on terms then current at the port for shipment in the usual amount, in the currency of the contract, sufficiently shown to cover the same goods covered by the bill of lading", applies to both marine and war risk insurance. As applied to marine insurance, it means such insurance as is usual or customary at the port for shipment with reference to the particular kind of goods involved, the character and equipment of the vessel, the route of the voyage, the port of destination and any other considerations that affect the risk. It is the substantial equivalent of the ordinary insurance in the particular trade and on the particular voyage and is subject to agreed specifications of type or extent of coverage. The language does not mean that the insurance must be adequate to cover all risks to which the goods may be subject in transit. There are some types of loss or damage that are not covered by the usual marine insurance and are excepted in bills of lading or in applicable statutes from the causes of loss or damage for which the carrier or the vessel is liable. Such risks must be borne by the buyer under this Chapter.

Insurance secured in compliance with a C.I.F. term must cover the entire transportation of the goods to the named destination.

7. An additional obligation is imposed upon the seller in requiring him to procure customary war risk insurance at the buyer's expense. This changes the common law on the point. The seller is not required to assume the risk of including in the C.I.F. price the cost of such insurance, since it often fluctuates rapidly, but is required to treat it simply as a necessary for the buyer's account. What war risk insurance is "current" or usual turns on the standard forms of policy or rider in common use.

8. The C.I.F. contract calls for insurance covering the value of the goods at the time and place of shipment and does not include any increase in market value during transit or any anticipated profit to the buyer on a sale by him.

The contract contemplates that before the goods arrive at their destination they may be sold again and again on C.I.F. terms and that the original policy of insurance and bill of lading will run with the interest in the goods by being transferred to each successive buyer. A buyer who becomes the seller in such an intermediate contract for sale does not thereby, if his sub-buyer knows the circumstances, undertake to insure the goods again at an increased price fixed in the new contract or to cover the increase in price by additional insurance, and his buyer may not reject the documents on the ground that the original policy does not cover such higher price. If such a sub-buyer desires additional insurance he must procure it for himself.

Where the seller exercises an option to ship "freight collect" and to credit the buyer with the freight against the C.I.F. price, the insurance need not cover the freight since the freight is not at the buyer's risk. On the other hand, where the seller prepays the freight upon shipping under a bill of lading requiring prepayment and providing that the freight shall be deemed earned and shall be retained by the carrier "ship and/or cargo lost or not lost," or using words of similar import, he must procure insurance that will cover the freight, because notwithstanding that the goods are lost in transit the buyer is bound to pay the freight as part of the C.I.F. price and will be unable to recover it back from the carrier.

9. Insurance "for the account of whom it may concern" is usual and sufficient. However, for a valid tender the policy of insurance must be one which can be disposed of together with the bill of lading and so must be "sufficiently shown to cover the same goods covered by the bill of lading". It must cover separately the quantity of goods called for by the buyer's contract and not merely insure his goods as part of a larger quantity in which others are interested, a case provided for in American mercantile practice by the use of negotiable certificates of insurance which are expressly authorized by this section. By usage these certificates are treated as the equivalent of separate policies and are good tender under C.I.F. contracts. The term "certificate of insurance", however, does not of itself include certificates or "cover notes" issued by the insurance broker and stating that the goods are covered by a policy. Their sufficiency as substitutes for policies will depend upon proof of an established usage or course of dealing. The present section rejects the English rule that not only brokers' certificates and "cover notes" but also certain forms of American insurance certificates are not the equivalent of policies and are not good tender under a C.I.F. contract.

The seller's failure to tender a proper insurance document is waived if the buyer refuses to make payment on other and untenable grounds at a time when proper insurance could have been obtained and tendered by the seller if timely objection had been made. Even a failure to insure on shipment may be cured by seasonable tender of a policy retroactive in effect; e.g., one insuring the goods "lost or not lost." The provisions of this Chapter on cure of improper tender and on waiver of buyer's objections by silence are applicable to insurance tenders under a C.I.F. term. Where there is no waiver by the buyer as described above, however, the fact that the goods arrive safely does not cure the seller's breach of his obligations to insure them and tender to the buyer a proper insurance document.

10. The seller's invoice of the goods shipped under a C.I.F. contract is regarded as a usual and necessary document upon which reliance may properly be placed. It is the document which evidences points of description, quality and the like which do not readily appear in other documents. This Chapter rejects those statements to the effect that the invoice is a usual but not a necessary document under a C.I.F. term.

11. The buyer needs all of the documents required under a C.I.F. contract, in due form and, if a tangible document of title, with necessary endorsements, so that before the goods arrive he may deal with them by negotiating the documents or may obtain prompt possession of the goods after their arrival. If the goods are lost or damaged in transit the documents are necessary to enable him promptly to assert his remedy against the carrier or insurer. The seller is therefore obligated to do what is mercantilely reasonable in the circumstances and should make every reasonable exertion to send forward the documents as soon as possible after the shipment. The requirement that the documents be forwarded with "commercial promptness" expresses a more urgent need for action than that suggested by the phrase "reasonable time".

12. Under a C.I.F. contract the buyer, as under the common law, must pay the price upon tender of the required documents without first inspecting the goods, but his payment in these circumstances does not constitute an acceptance of the goods nor does it impair his right of subsequent inspection or his options and remedies in the case of improper delivery. All remedies and rights for the seller's breach are reserved to him. The buyer must pay before inspection and assert his remedy against the seller afterward unless the nonconformity of the goods amounts to a real failure of consideration, since the purpose of choosing this form of contract is to give

the seller protection against the buyer's unjustifiable rejection of the goods at a distant port of destination which would necessitate taking possession of the goods and suing the buyer there.

13. A valid C.I.F. contract may be made which requires part of the transportation to be made on land and part on the sea, as where the goods are to be brought by rail from an inland point to a seaport and thence transported by vessel to the named destination under a "through" or combination bill of lading issued by the railroad company. In such a case shipment by rail from the inland point within the contract period is a timely shipment notwithstanding that the loading of the goods on the vessel is delayed by causes beyond the seller's control.

14. Although subsection (2) stating the legal effects of the C.I.F. term is an "unless otherwise agreed" provision, the express language used in an agreement is frequently a precautionary, fuller statement of the normal C.I.F. terms and hence not intended as a departure or variation from them. Moreover, the dominant outlines of the C.I.F. term are so well understood commercially that any variation should, whenever reasonably possible, be read as falling within those dominant outlines rather than as destroying the whole meaning of a term which essentially indicates a contract for proper shipment rather than one for delivery at destination. Particularly careful consideration is necessary before a printed form or clause is construed to mean agreement otherwise and where a C.I.F. contract is prepared on a printed form designed for some other type of contract, the C.I.F. terms must prevail over printed clauses repugnant to them.

15. Under subsection (4) the fact that the seller knows at the time of the tender of the documents that the goods have been lost in transit does not affect his rights if he has performed his contractual obligations. Similarly, the seller cannot perform under a C.I.F. term by purchasing and tendering landed goods.

16. Under the C. & F. term, as under the C.I.F. term, title and risk of loss are intended to pass to the buyer on shipment. A stipulation in a C. & F. contract that the seller shall effect insurance on the goods and charge the buyer with the premium (in effect that he shall act as the buyer's agent for that purpose) is entirely in keeping with the pattern. On the other hand, it often happens that the buyer is in a more advantageous position than the seller to effect insurance on the goods or that he has in force an "open" or "floating" policy covering all shipments made by him or to him, in either of which events the C. & F. term is adequate without mention of insurance.

17. It is to be remembered that in a French contract the term "C.A.F." does not mean "Cost and Freight" but has exactly the same meaning as the term "C.I.F." since it is merely the French equivalent of that term. The "A" does not stand for "and" but for "assurance" which means insurance.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

30-2-321. C.I.F. or C.&F. — "net landed weights" — "payment on arrival" — warranty of condition on arrival.

Official Comment

Prior Uniform Statutory Provision: None.

Purposes:

This section deals with two variations of the C.I.F. contract which have evolved in mercantile practice but are entirely consistent with the basic C.I.F. pattern. Subsections (1) and (2), which provide for a shift to the seller of the risk of quality and weight deterioration during shipment, are designed to conform the law to the best mercantile practice and usage without changing the legal consequences of the C.I.F. or C. & F. term as to the passing of marine risks to the buyer at the point of shipment. Subsection (3) provides that where under the contract documents are to be presented for payment after arrival of the goods, this amounts merely to a postponement of the payment under the C.I.F. contract and is not to be confused with the "no arrival, no sale" contract. If the goods are lost, delivery of the documents and payment against them are due when the goods should have arrived. The clause for payment on or after arrival is not to be construed as such a condition precedent to payment that if the goods are lost in transit the buyer need never pay and the seller must bear the loss.

30-2-322. Delivery "ex-ship".

Official Comment

Prior Uniform Statutory Provision: None.

Purposes:

1. The delivery term, "ex-ship", as between seller and buyer, is the reverse of the f.a.s. term covered.

2. Delivery need not be made from any particular vessel under a clause calling for delivery "ex-ship", even though a vessel on which shipment is to be made originally is named in the contract, unless the agreement by appropriate language, restricts the clause to delivery from a named vessel.

3. The appropriate place and manner of unloading at the port of destination depend upon the nature of the goods and the facilities and usages of the port.

4. A contract fixing a price "ex-ship" with payment "cash against documents" calls only for such documents as are appropriate to the contract. Tender of a delivery order and of a receipt for the freight after the arrival of the carrying vessel is adequate. The seller is not required to tender a bill of lading as a document of title nor is he required to insure the goods for the buyer's benefit, as the goods are not at the buyer's risk during the voyage.

30-2-323. Form of bill of lading required in overseas shipment — "overseas".

Official Comment

[*Corresponding U.C.C. Section:* Section 2-323, U.C.C.]

Prior Uniform Statutory Provision: None.

Purposes:

1. Subsection (1) follows the "American" rule that a regular bill of lading indicating delivery of the goods at the dock for shipment is sufficient, except under a term "F.O.B. vessel." See Section 30-2-319 and comment thereto.

2. Subsection (2) deals with the problem of bills of lading covering deep water shipments, issued not as a single bill of lading but in a set of parts, each part referring to the other parts and the entire set constituting in commercial practice and at law a single bill of lading. Commercial practice in international commerce is to accept and pay against presentation of the first part of a set if the part is sent from overseas even though the contract of the buyer requires presentation of a full set of bills of lading provided adequate indemnity for the missing parts is forthcoming. In accord with the amendment to Section 7-304 [30-7-304], bills of lading in a set are limited to tangible bills.

This subsection codifies that practice as between buyer and seller. Chapter 5 (Section 30-5-113, now repealed) authorizes banks presenting drafts under letters of credit to give indemnities against the missing parts, and this subsection means that the buyer must accept and act on such indemnities if he in good faith deems them adequate. But neither this subsection nor Chapter 5 decides whether a bank which has issued a letter of credit is similarly bound. The issuing bank's obligation under a letter of credit is independent and depends on its own terms. See Chapter 5.

Compiler's Comments

2005 Amendment: Chapter 575 in (2) near beginning inserted "tangible". Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-2-324. "No arrival, no sale" term.

Official Comment

Prior Uniform Statutory Provision: None.

Purposes:

1. The "no arrival, no sale" term in a "destination" overseas contract leaves risk of loss on the seller but gives him an exemption from liability for nondelivery. Both the nature of the case and the duty of good faith require that the seller must not interfere with the arrival of the goods in any way. If the circumstances impose upon him the responsibility for making or arranging the shipment, he must have a shipment made despite the exemption clause. Further, the shipment made must be a conforming one, for the exemption under a "no arrival, no sale" term applies only to the hazards of transportation and the goods must be proper in all other respects.

The reason of this section is that where the seller is reselling the goods bought by him as shipped by another and this fact is known to the buyer, so that the seller is not under any obligation to make the shipment himself, the seller is entitled under the "no arrival, no sale" clause to exemption from payment of damages for non-delivery if the goods do not arrive or if the goods which actually arrive are non-conforming. This does not extend to sellers who arrange shipment by their own agents, in which case the clause is limited to casualty due to marine hazards. But sellers who make known that they are contracting only with respect to what will be delivered to them by parties over whom they assume no control are entitled to the full quantum of the exemption.

2. The provisions of this Chapter on identification must be read together with the present section in order to bring the exemption into application. Until there is some designation of the goods in a particular shipment or on a particular ship as being those to which the contract refers there can be no application of an exemption for their non-arrival.

3. The seller's duty to tender the agreed or declared goods if they do arrive is not impaired because of their delay in arrival or by their arrival after transshipment.

4. The phrase "to arrive" is often employed in the same sense as "no arrival, no sale" and may then be given the same effect. But a "to arrive" term, added to a C.I.F. or C. & F. contract, does not have the full meaning given by this section to "no arrival, no sale". Such a "to arrive" term is usually intended to operate only to the extent that the risks are not covered by the agreed insurance and the loss or casualty is due to such uncovered hazards. In some instances the "to arrive" term may be regarded as a time of payment term, or, in the case of the reselling seller discussed in point 1 above, as negating responsibility for conformity of the goods, if they arrive, to any description which was based on his good faith belief of the quality. Whether this is the intention of the parties is a question of fact based on all the circumstances surrounding the resale and in case of ambiguity the rules of Sections 30-2-316 and 30-2-317 apply to preclude dishonor.

5. Paragraph (b) applies where goods arrive impaired by damage or partial loss during transportation and makes the policy of this Chapter on casualty to identified goods applicable to such a situation. For the term cannot be regarded as intending to give the seller an unforeseen profit through casualty; it is intended only to protect him from loss due to causes beyond his control.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

30-2-325. "Letter of credit" term — "confirmed credit".

Official Comment

Prior Uniform Statutory Provision: None.

Purposes: To express the established commercial and banking understanding as to the meaning and effects of terms calling for "letters of credit" or "confirmed credit":

1. Subsection (2) follows the general policy of this Chapter and Chapter 3 (Section 30-3-802 [now repealed]) on conditional payment, under which payment by check or other short-term instrument is not ordinarily final as between the parties if the recipient duly presents the instrument and honor is refused. Thus the furnishing of a letter of credit does not substitute the financing agency's obligation for the buyer's, but the seller must first give the buyer reasonable notice of his intention to demand direct payment from him.

2. Subsection (3) requires that the credit be irrevocable and be a prime credit as determined by the standing of the issuer. It is not necessary, unless otherwise agreed, that the credit be a negotiation credit; the seller can finance himself by an assignment of the proceeds under Section 30-5-116(2) [substance now in 30-5-132].

3. The definition of "confirmed credit" is drawn on the supposition that the credit is issued by a bank which is not doing direct business in the seller's financial market; there is no intention to require the obligation of two banks both local to the seller.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-2-326. Sale on approval and sale or return — rights of creditors.

Official Comment

Prior Uniform Statutory Provision: Section 19(3), Uniform Sales Act.

Changes: Completely rewritten in this and the succeeding section.

Purposes of Changes: To make it clear that:

1. Both a "sale on approval" and a "sale or return" should be distinguished from other types of transactions with which they frequently have been confused. A "sale on approval," sometimes also called a sale "on trial" or "on satisfaction," deals with a contract under which the seller undertakes a risk in order to satisfy its prospective buyer with the appearance or performance of the goods that are sold. The goods are delivered to the proposed purchaser but they remain the property of the seller until the buyer accepts them. The price has already been agreed. The buyer's willingness to receive and test the goods is the consideration for the seller's engagement to deliver and sell. A "sale or return," on the other hand, typically is a sale to a merchant whose unwillingness to buy is overcome by the seller's engagement to take back the goods (or any commercial unit of goods) in lieu of payment if they fail to be resold. A sale or return is a present sale of goods which may be undone at the buyer's option. Accordingly, subsection (2) provides that goods delivered on approval are not subject to the prospective buyer's creditors until acceptance, and goods delivered in a sale or return are subject to the buyer's creditors while in the buyer's possession.

These two transactions are so strongly delineated in practice and in general understanding that every presumption runs against a delivery to a consumer being a "sale or return" and against a delivery to a merchant for resale being a "sale on approval."

2. The right to return goods for failure to conform to the contract does not make the transaction a "sale on approval" or "sale or return" and has nothing to do with this section or Section 30-2-327. This section is not concerned with remedies for breach of contract. It deals instead with a power given by the contract to turn back the goods even though they are wholly as warranted. This section nevertheless presupposes that a contract for sale is contemplated by the parties although that contract may be of the peculiar character that this section addresses (i.e., a sale on approval or a sale or return).

If a buyer's obligation as a buyer is conditioned not on his personal approval but on the article's passing a described objective test, the risk of loss by casualty pending the test is properly the seller's and proper return is at his expense. On the point of "satisfaction" as meaning "reasonable satisfaction" when an industrial machine is involved, this Article takes no position.

3. Subsection (3) resolves a conflict in the pre-UCC case law by recognizing that an "or return" provision is so definitely at odds with any ordinary contract for sale of goods that if a written agreement is involved the "or return" term must be contained in a written memorandum. The "or return" aspect of a sales contract must be treated as a separate contract under the Statute of Frauds section and as contradicting the sale insofar as questions of parol or extrinsic evidence are concerned.

4. Certain true consignment transactions were dealt with in former Sections 30-2-326(3) and 30-9-114 [now repealed]. These provisions have been deleted and have been replaced by new provisions in Chapter 9A. See, e.g., Sections 30-9A-109(1)(d); 30-9A-103(2); 30-9A-319.

Compiler's Comments

1999 Amendment: Chapter 305 at beginning of (2) deleted "Except as provided in subsection (3)"; deleted former (3) that read: "(3) Where goods are delivered to a person for sale and such person maintains a place of business at which he deals in goods of the kind involved, under a name other than the name of the person making delivery, then with respect to claims of creditors of the person conducting the business the goods are deemed to be on sale or return. The provisions of this subsection are applicable even though an agreement purports to reserve title to the person making delivery until payment or resale or uses such words as "on consignment" or "on memorandum". However, this subsection is not applicable if the person making delivery:

(a) complies with an applicable law providing for a consignor's interest or the like to be evidenced by a sign; or

(b) establishes that the person conducting the business is generally known by his creditors to be substantially engaged in selling the goods of others; or

(c) complies with the filing provisions of the Chapter on Secured Transactions (Chapter 9)"; and made minor changes in style. Amendment effective July 1, 2001.

Case Notes

Consignment — Not Sale or Return: Bobbie opened a business selling gift items, gourmet foods, and kitchen items. Bobbie began having financial problems and started taking in antiques and other collectibles on a consignment basis. Bobbie eventually went bankrupt. The bankruptcy trustee appealed the decision of the bankruptcy court which held that the property held on consignment was not part of the bankruptcy estate. On appeal, the federal District Court affirmed the decision, stating that the antiques were on consignment rather than a "sale or return" and that 30-2-326 does not apply because consignee did not maintain "a place of business at which she dealt in goods of the kind involved". (See 1999 amendment.) Newhall v. Haines, 10 Bankr. 1019, 38 St. Rep. 786 (D.C. Mont. 1981).

30-2-327. Special incidents of sale on approval and sale or return.

Official Comment

Prior Uniform Statutory Provision: Section 19(3), Uniform Sales Act.

Changes: Completely rewritten in preceding and this section.

Purposes of Changes: To make it clear that:

1. In the case of a sale on approval:

If all of the goods involved conform to the contract, the buyer's acceptance of part of the goods constitutes acceptance of the whole. Acceptance of part falls outside the normal intent of the parties in the "on approval" situation and the policy of this Chapter allowing partial acceptance of a defective delivery has no application here. A case where a buyer takes home two dresses to select one commonly involves two distinct contracts; if not, it is covered by the words "unless otherwise agreed".

2. In the case of a sale or return, the return of any unsold unit merely because it is unsold is the normal intent of the "sale or return" provision, and therefore the right to return for this reason alone is independent of any other action under the contract which would turn on wholly different considerations. On the other hand, where the return of goods is for breach, including return of items resold by the buyer and returned by the ultimate purchasers because of defects, the return procedure is governed not by the present section but by the provisions on the effects and revocation of acceptance.

3. In the case of a sale on approval the risk rests on the seller until acceptance of the goods by the buyer, while in a sale or return the risk remains throughout on the buyer.

4. Notice of election to return given by the buyer in a sale on approval is sufficient to relieve him of any further liability. Actual return by the buyer to the seller is required in the case of a sale or return contract. What constitutes due "giving" of notice, as required in "on approval" sales, is governed by the provisions on good faith and notice. "Seasonable" is used here as defined in Section 30-1-204. Nevertheless, the provisions of both this Chapter and of the contract on this point must be read with commercial reason and with full attention to good faith.

Part 4
Title, Creditors, and Good Faith Purchasers

30-2-401. Passing of title — reservation for security — limited application of this section.

Official Comment

[*Corresponding U.C.C. Section:* Section 2-401, U.C.C.]

[*Code Commissioner Note:* In 2005, Montana adopted Alternative B of the 2003 revision to Article 7 for this section.]

Prior Uniform Statutory Provision: See generally, Sections 17, 18, 19 and 20, Uniform Sales Act.

Purposes: To make it clear that:

1. This Chapter deals with the issues between seller and buyer in terms of step by step performance or non-performance under the contract for sale and not in terms of whether or not "title" to the goods has passed. That the rules of this section in no way alter the rights of either the buyer, seller or third parties declared elsewhere in the Chapter is made clear by the preamble of this section. This section, however, in no way intends to indicate which line of interpretation should be followed in cases where the applicability of "public" regulation depends upon a "sale" or upon location of "title" without further definition. The basic policy of this Chapter that known purpose and reason should govern interpretation cannot extend beyond the scope of its own provisions. It is therefore necessary to state what a "sale" is and when title passes under this Chapter in case the courts deem any public regulation to incorporate the defined term of the "private" law.

2. "Future" goods cannot be the subject of a present sale. Before title can pass the goods must be identified in the manner set forth in Section 30-2-501. The parties, however, have full liberty to arrange by specific terms for the passing of title to goods which are existing.

3. The "special property" of the buyer in goods identified to the contract is excluded from the definition of "security interest"; its incidents are defined in provisions of this Chapter such as

those on the rights of the seller's creditors, on good faith purchase, on the buyer's right to goods on the seller's insolvency, and on the buyer's right to specific performance or replevin.

4. The factual situations in subsections (2) and (3) upon which passage of title turn actually base the test upon the time when the seller has finally committed himself in regard to specific goods. Thus in a "shipment" contract he commits himself by the act of making the shipment. If shipment is not contemplated subsection (3) turns on the seller's final commitment, i.e. the delivery of documents or the making of the contract. As to delivery of an electronic document of title, see definition of delivery in Article 1, Section 1-201 [30-1-201]. This Article [Title 30, chapter 2] does not state a rule as to the place of title passage as to goods covered by an electronic document of title.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

2005 Amendment: Chapter 575 in (2) near middle after "reference to the" deleted "physical"; in (3)(a) near beginning inserted "tangible" and at end inserted "and if the seller is to deliver an electronic document of title, title passes when the seller delivers the document"; in (3)(b) near middle after "documents" inserted "of title"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

1989 Amendment: In (4), near beginning of introductory clause, inserted "or cattle being released from auction yards for interstate shipment".

Montana Changes: See 1989 amendment note.

Case Notes

Sufficient Evidence Required to Show Issue of Material Fact — Contracts: The plaintiff entered into a contract with the defendant to provide the defendant with crushed aggregate material from his gravel pit. The defendant no longer needed the aggregate material and refused to pay the final invoices. The Supreme Court held that the District Court properly granted summary judgment to the plaintiff because the defendant failed to present sufficient evidence to establish that an issue of material fact existed regarding the amount of material extracted by the defendant. In addition, the Supreme Court awarded reasonable attorney fees, trial costs, and appeal costs to the plaintiff under 28-2-2105 and remanded the case to determine the fees and costs. Moore v. Goran, LLC, 2017 MT 208, 388 Mont. 340, 400 P.3d 729.

Principal's Impairment or Suspension of Rights of Guarantor — Exoneration of Guarantor Proper: Ace Leasing, Inc. (Ace), funded a lease to O'Neill for $45,000 for business equipment. Boustead was guarantor of the lease agreement. If O'Neill failed to perform, the lease provided that Ace could proceed directly against Boustead. O'Neill failed to make timely payments. Ace canceled the lease. O'Neill and Ace then discussed the matter, and O'Neill explained that the late payments were the result of the late arrival of the ordered equipment. Ace agreed to accept several late payments, but Boustead was not part of the negotiations. O'Neill again missed several payments, and Ace requested that Boustead pay off the lease. Boustead refused to pay on grounds that the cancellation letter and acceptance of late payments without Boustead's knowledge, as well as the method of purchasing the equipment, constituted a material change in the agreement and in Boustead's obligations as guarantor. The District Court agreed and exonerated Boustead as guarantor under 28-11-211. The court also held that Boustead's risk was increased because Ace did not own the equipment, so the transaction between Ace and O'Neill constituted a loan rather than a lease. Ace appealed the findings regarding ownership and alteration of the agreement. The Supreme Court affirmed. Under this section, the title of goods passes to the buyer at the time that and place at which the seller completes performance with reference to physical delivery of the goods, unless the agreement provides otherwise. Here, neither Ace nor O'Neill conformed to the purchase provision of the agreement. Because Ace failed to obtain title, Ace could not assume the role of lessor and, while retaining title and ownership, transfer to O'Neill merely the right of possession and use of the equipment, so the transaction effectively became a loan agreement between the parties with O'Neill holding title to the equipment according to the default provisions of the Uniform Commercial Code. Further, Ace's actions in accepting late payments after canceling the agreement and in failing to comply with the terms of the lease requiring Ace to purchase the equipment and retain ownership to secure its interest were a material alteration in the agreement as affecting Boustead. Ace impaired or suspended its rights and remedies against O'Neill and, without Boustead's consent, impaired or suspended Boustead's rights as well, which was sufficient to exonerate Boustead as guarantor under 28-11-211. Ace Leasing, Inc. v. Boustead, 2002 MT 213, 311 M 285, 55 P3d 371 (2002).

Determination of Vehicle Ownership — Installment Sales Contract Not Indicative of Ownership for Insurance Purposes: Jordet, an adult, jointly purchased a vehicle for the exclusive use of his minor sister-in-law, who made the downpayment, repaid registration and license fees, made the only installment payment, purchased separate insurance, possessed the only keys, and maintained sole use and control of the vehicle. The District Court decided that the term "owned vehicle" in Jordet's automobile policy included the jointly owned vehicle and that Jordet's signature on the installment sales contract conclusively placed the vehicle under his policy. The Supreme Court reversed, noting that the purchase of property and the insurance of property are distinct transactions and that Jordet's signature on the sales contract did not establish ownership for insurance purposes. Implicit in ownership is the ability to control how, when, where, and by whom the property will be used. Since Jordet never exercised any of the indicia of ownership that would be compatible with his insuring the vehicle, it was not an "owned vehicle" under the terms of his policy. Truck Ins. Exch. v. Nelson, 228 M 233, 743 P2d 572, 44 St. Rep. 1482 (1987).

Transfer of Car Ownership for Purposes of Garage Liability Insurance Policy: In action by insurance company to determine rights and obligations under garage liability insurance policy issued to dealer in relation to vehicle sold by dealership that later was involved in accident without purchaser acquiring registration or certificate of title, the court held that change in ownership occurred under a purchase contract although the certificate of title had not transferred. The presumption in 61-3-105 (now repealed) can be overcome by the facts in a particular case. Section 61-3-201 has no effect on ownership transfer for insurance purposes. Prospector Chevrolet, Inc., delivered the vehicle to Clive Lapp. Under the U.C.C., the sale was complete and Lapp became the owner. Lapp had the right to use or dispose of the automobile as he wished. Prospector had relinquished all its legal rights to the vehicle even though it still had the statutory duties relating to transfer of certificate of ownership. Legal title passed to Lapp on date of delivery. Safeco Ins. Co. v. Lapp, 215 M 196, 695 P2d 1310, 42 St. Rep. 289 (1985).

30-2-402. Rights of seller's creditors against sold goods.

Official Comment

Prior Uniform Statutory Provision: Subsection (2)—Section 26, Uniform Sales Act; Subsections (1) and (3)—none.

Changes: Rephrased.

Purposes of Changes and New Matter: To avoid confusion on ordinary issues between current sellers and buyers and issues in the field of preference and hindrance by making it clear that:

1. Local law on questions of hindrance of creditors by the seller's retention of possession of the goods are outside the scope of this Chapter, but retention of possession in the current course of trade is legitimate. Transactions which fall within the law's policy against improper preferences are reserved from the protection of this Chapter.
2. The retention of possession of the goods by a merchant seller for a commercially reasonable time after a sale or identification in current course is exempted from attack as fraudulent. Similarly, the provisions of subsection (3) have no application to identification or delivery made in the current course of trade, as measured against general commercial understanding of what a "current" transaction is.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

30-2-403. Power to transfer — good faith purchase of goods — "entrusting".

Official Comment

[*Corresponding U.C.C. Section:* Section 2-403, U.C.C.]

Prior Uniform Statutory Provision: Sections 20(4), 23, 24, 25, Uniform Sales Act; Section 9, especially 9(2), Uniform Trust Receipts Act; Section 9, Uniform Conditional Sales Act.

Changes: Consolidated and rewritten.

Purposes of Changes: To gather together a series of prior uniform statutory provisions and the case-law thereunder and to state a unified and simplified policy on good faith purchase of goods.

1. The basic policy of our law allowing transfer of such title as the transferor has is generally continued and expanded under subsection (1). In this respect the provisions of the section are applicable to a person taking by any form of "purchase" as defined by this Act. Moreover the policy of this Act expressly providing for the application of supplementary general principles of law to sales transactions wherever appropriate joins with the present section to continue unimpaired all rights acquired under the law of agency or of apparent agency or ownership or other estoppel, whether based on statutory provisions or on case law principles. The section also leaves unimpaired the powers given to selling factors under the earlier Factors Acts. In addition subsection (1) provides specifically for the protection of the good faith purchaser for value in a number of specific situations which have been troublesome under prior law.

On the other hand, the contract of purchase is of course limited by its own terms as in a case of pledge for a limited amount or of sale of a fractional interest in goods.

2. The many particular situations in which a buyer in ordinary course of business from a dealer has been protected against reservation of property or other hidden interest are gathered by subsections (2)-(4) into a single principle protecting persons who buy in ordinary course out of inventory. Consignors have no reason to complain, nor have lenders who hold a security interest in the inventory, since the very purpose of goods in inventory is to be turned into cash by sale.

The principle is extended in subsection (3) to fit with the abolition of the old law of "cash sale" by subsection (1)(c). It is also freed from any technicalities depending on the extended law of larceny; such extension of the concept of theft to include trick, particular types of fraud, and the like is for the purpose of helping conviction of the offender; it has no proper application to the long-standing policy of civil protection of buyers from persons guilty of such trick or fraud. Finally, the policy is extended, in the interest of simplicity and sense, to any entrusting by a bailor; this is in consonance with the explicit provisions of Section 30-7-205 on the powers of a warehouse who is also in the business of buying and selling fungible goods of the kind he stores. As to entrusting by a secured party, subsection (2) is limited by the more specific provisions of Section 30-9A-320(1), which deny protection to a person buying farm products from a person engaged in farming operations.

3. The definition of "buyer in ordinary course of business" (Section 30-1-201) is effective here and preserves the essence of the healthy limitations engrafted by the case-law on the older statutes. The older loose concept of good faith and wide definition of value combined to create apparent good faith purchasers in many situations in which the result outraged common sense; the court's solution was to protect the original title especially by use of "cash sale" or of over-technical construction of the enabling clauses of the statutes. But such rulings then turned into limitations on the proper protection of buyers in the ordinary market. Section 30-1-201(9) cuts down the category of buyer in ordinary course in such fashion as to take care of the results of the cases, but with no price either in confusion or in injustice to proper dealings in the normal market.

4. Except as provided in subsection (1), the rights of purchasers other than buyers in ordinary course are left to the Chapters on Secured Transactions, Documents of Title, and Bulk Sales.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

1991 Amendment: In (4), after reference to secured transactions, deleted "bulk transfers (chapter 6)".

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Montana Changes: Montana has changed references from "larceny" to "theft" in this section in order to conform to Montana's criminal statutes.

Part 5

Performance

30-2-501. Insurable interest in goods — manner of identification of goods.

Official Comment

Prior Uniform Statutory Provision: See Sections 17 and 19, Uniform Sales Act.

Purposes:

1. The present section deals with the manner of identifying goods to the contract so that an insurable interest in the buyer and the rights set forth in the next section will accrue. Generally

speaking, identification may be made in any manner "explicitly agreed to" by the parties. The rules of paragraphs (a), (b) and (c) apply only in the absence of such "explicit agreement".

2. In the ordinary case identification of particular existing goods as goods to which the contract refers is unambiguous and may occur in one of many ways. It is possible, however, for the identification to be tentative or contingent. In view of the limited effect given to identification by this Chapter, the general policy is to resolve all doubts in favor of identification.

3. The provision of this section as to "explicit agreement" clarifies the present confusion in the law of sales which has arisen from the fact that under prior uniform legislation all rules of presumption with reference to the passing of title or to appropriation (which in turn depended upon identification) were regarded as subject to the contrary intention of the parties or of the party appropriating. Such uncertainty is reduced to a minimum under this section by requiring "explicit agreement" of the parties before the rules of paragraphs (a), (b) and (c) are displaced — as they would be by a term giving the buyer power to select the goods. An "explicit" agreement, however, need not necessarily be found in the terms used in the particular transaction. Thus, where a usage of the trade has previously been made explicit by reduction to a standard set of "rules and regulations" currently incorporated by reference into the contracts of the parties, a relevant provision of those "rules and regulations" is "explicit" within the meaning of this section.

4. In view of the limited function of identification there is no requirement in this section that the goods be in deliverable state or that all of the seller's duties with respect to the processing of the goods be completed in order that identification occur. For example, despite identification the risk of loss remains on the seller under the risk of loss provisions until completion of his duties as to the goods and all of his remedies remain dependent upon his not defaulting under the contract.

5. Undivided shares in an identified fungible bulk, such as grain in an elevator or oil in a storage tank, can be sold. The mere making of the contract with reference to an undivided share in an identified fungible bulk is enough under subsection (a) to effect an identification if there is no explicit agreement otherwise. The seller's duty, however, to segregate and deliver according to the contract is not affected by such an identification but is controlled by other provisions of this Chapter.

6. Identification of crops under paragraph (c) is made upon planting only if they are to be harvested within the year or within the next normal harvest season. The phrase "next normal harvest season" fairly includes nursery stock raised for normally quick "harvest," but plainly excludes a "timber" crop to which the concept of a harvest "season" is inapplicable.

Paragraph (c) is also applicable to a crop of wool or the young of animals to be born within twelve months after contracting. The product of a lumbering, mining or fishing operation, though seasonal, is not within the concept of "growing". Identification under a contract for all or part of the output of such an operation can be effected early in the operation.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-2-502. Buyer's right to goods on seller's insolvency.

Official Comment

Prior Uniform Statutory Provision: Compare Sections 17, 18 and 19, Uniform Sales Act.

Purposes:

1. This section gives an additional right to the buyer as a result of identification of the goods to the contract in the manner provided in Section 2-501. The buyer is given a right to recover the goods, conditioned upon making and keeping good a tender of any unpaid portion of the price, in two limited circumstances. First, the buyer may recover goods bought for personal, family, or household purposes if the seller repudiates the contract or fails to deliver the goods. Second, in any case, the buyer may recover the goods if the seller becomes insolvent within 10 days after the seller receives the first installment on their price. The buyer's right to recover the goods under this section is an exception to the usual rule, under which the disappointed buyer must resort to an action to recover damages.

2. The question of whether the buyer also acquires a security interest in identified goods and has rights to the goods when insolvency takes place after the ten-day period provided in this section depends upon compliance with the provisions of the Chapter on Secured Transactions (Chapter 9A).

3. Under subsection (2), the buyer's right to recover consumer goods under subsection (1)(a) vests upon acquisition of a special property, which occurs upon identification of the goods to the contract. See Section 30-2-501. Inasmuch as a secured party normally acquires no greater

rights in its collateral that its debtor had or had power to convey, see Section 30-2-403(1) (first sentence), a buyer who acquires a right to recover under this section will take free of a security interest created by the seller if it attaches to the goods after the goods have been identified to the contract. The buyer will take free, even if the buyer does not buy in ordinary course and even if the security interest is perfected. Of course, to the extent that the buyer pays the price after the security interest attaches, the payments will constitute proceeds of the security interest.

4. Subsection (3) is included to preclude the possibility of unjust enrichment, which would exist if the buyer were permitted to recover goods even though they were greatly superior in quality or quantity to that called for by the contract for sale.

Compiler's Comments

1999 Amendment: Chapter 305 near beginning of (1) inserted reference to subsection (3); inserted (1)(a) concerning household goods; at beginning of (1)(b) inserted "in other cases"; inserted (2) concerning right to recover goods; and made minor changes in style. Amendment effective July 1, 2001.

30-2-503. Manner of seller's tender of delivery.

Official Comment

[*Corresponding U.C.C. Section:* Section 2-503, U.C.C.]

[*Code Commissioner Note:* In 2005, Montana adopted Alternative B of the 2003 revision to Article 7 for this section.]

Prior Uniform Statutory Provision: See Sections 11, 19, 20, 43(3) and (4), 46 and 51, Uniform Sales Act.

Changes: The general policy of the above sections is continued and supplemented but subsection (3) changes the rule of prior section 19(5) as to what constitutes a "destination" contract and subsection (4) incorporates a minor correction as to tender of delivery of goods in the possession of a bailee.

Purposes of Changes:

1. The major general rules governing the manner of proper or due tender of delivery are gathered in this section. The term "tender" is used in this Chapter in two different senses. In one sense it refers to "due tender" which contemplates an offer coupled with a present ability to fulfill all the conditions resting on the tendering party and must be followed by actual performance if the other party shows himself ready to proceed. Unless the context unmistakably indicates otherwise this is the meaning of "tender" in this Chapter and the occasional addition of the word "due" is only for clarity and emphasis. At other times it is used to refer to an offer of goods or documents under a contract as if in fulfillment of its conditions even though there is a defect when measured against the contract obligation. Used in either sense, however, "tender" connotes such performance by the tendering party as puts the other party in default if he fails to proceed in some manner. These concepts of tender would apply to tender of either tangible or electronic documents of title.

2. The seller's general duty to tender and deliver is laid down in Section 30-2-301 and more particularly in Section 30-2-507. The seller's right to a receipt if he demands one and receipts are customary is governed by Section 30-1-205. Subsection (1) of the present section proceeds to set forth two primary requirements of tender: first, that the seller "put and hold conforming goods at the buyer's disposition" and, second, that he "give the buyer any notice reasonably necessary to enable him to take delivery."

In cases in which payment is due and demanded upon delivery the "buyer's disposition" is qualified by the seller's right to retain control of the goods until payment by the provision of this Chapter on delivery on condition. However, where the seller is demanding payment on delivery he must first allow the buyer to inspect the goods in order to avoid impairing his tender unless the contract for sale is on C.I.F., C.O.D., cash against documents or similar terms negating the privilege of inspection before payment.

In the case of contracts involving documents the seller can "put and hold conforming goods at the buyer's disposition" under subsection (1) by tendering documents which give the buyer complete control of the goods under the provisions of Chapter 7 on due negotiation.

3. Under paragraph (a) of subsection (1) usage of the trade and the circumstances of the particular case determine what is a reasonable hour for tender and what constitutes a reasonable period of holding the goods available.

4. The buyer must furnish reasonable facilities for the receipt of the goods tendered by the seller under subsection (1), paragraph (b). This obligation of the buyer is no part of the seller's tender.

5. For the purposes of subsections (2) and (3) there is omitted from this Chapter the rule under prior uniform legislation that a term requiring the seller to pay the freight or cost of transportation to the buyer is equivalent to an agreement by the seller to deliver to the buyer or at an agreed destination. This omission is with the specific intention of negating the rule, for under this Chapter the "shipment" contract is regarded as the normal one and the "destination" contract as the variant type. The seller is not obligated to deliver at a named destination and bear the concurrent risk of loss until arrival, unless he has specifically agreed so to deliver or the commercial understanding of the terms used by the parties contemplates such delivery.

6. Paragraph (a) of subsection (4) continues the rule of the prior uniform legislation as to acknowledgment by the bailee. Paragraph (b) of subsection (4) adopts the rule that between the buyer and the seller the risk of loss remains on the seller during a period reasonable for securing acknowledgment of the transfer from the bailee, while as against all other parties the buyer's rights are fixed as of the time the bailee receives notice of the transfer.

7. Under subsection (5) documents are never "required" except where there is an express contract term or it is plainly implicit in the peculiar circumstances of the case or in a usage of trade. Documents may, of course, be "authorized" although not required, but such cases are not within the scope of this subsection. When documents are required, there are three main requirements of this subsection: (1) "All": each required document is essential to a proper tender; (2) "Such": the documents must be the ones actually required by the contract in terms of source and substance; (3) "Correct form": All documents must be in correct form. These requirements apply to both tangible and electronic documents of title. When tender is made through customary banking channels, a draft may accompany or be associated with a document of title. The language has been broadened to allow for drafts to be associated with an electronic document of title. Compare Section 2-104(2) [30-2-104(2)] definition of financing agency.

When a prescribed document cannot be procured, a question of fact arises under the provision of this Chapter on substituted performance as to whether the agreed manner of delivery is actually commercially impracticable and whether the substitute is commercially reasonable.

Compiler's Comments

2005 Amendment: Chapter 575 in (4)(b) near beginning substituted "record directing" for "written direction to" and inserted "except as otherwise provided in chapter 9A"; in (5)(a) at end deleted "except as provided in this chapter with respect to bills of lading in a set (subsection (2) of 30-2-323)"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-2-504. Shipment by seller.

Official Comment

Prior Uniform Statutory Provision: Section 46, Uniform Sales Act.

Changes: Rewritten.

Purposes of Changes: To continue the general policy of the prior uniform statutory provision while incorporating certain modifications with respect to the requirement that the contract with the carrier be made expressly on behalf of the buyer and as to the necessity of giving notice of the shipment to the buyer, so that:

1. The section is limited to "shipment" contracts as contrasted with "destination" contracts or contracts for delivery at the place where the goods are located. The general principles embodied in this section cover the special cases of F.O.B. point of shipment contracts and C.I.F. and C. & F. contracts. Under the preceding section on manner of tender of delivery, due tender by the seller requires that he comply with the requirements of this section in appropriate cases.

2. The contract to be made with the carrier under paragraph (a) must conform to all express terms of the agreement, subject to any substitution necessary because of failure of agreed facilities as provided in the later provision on substituted performance. However, under the policies of this Chapter on good faith and commercial standards and on buyer's rights on improper delivery, the requirements of explicit provisions must be read in terms of their commercial and not their literal

meaning. This policy is made express with respect to bills of lading in a set in the provision of this Chapter on form of bills of lading required in overseas shipment.

3. In the absence of agreement, the provision of this Chapter on options and cooperation respecting performance gives the seller the choice of any reasonable carrier, routing and other arrangements. Whether or not the shipment is at the buyer's expense the seller must see to any arrangements, reasonable in the circumstances, such as refrigeration, watering of live stock, protection against cold, the sending along of any necessary help, selection of specialized cars and the like for paragraph (a) is intended to cover all necessary arrangements whether made by contract with the carrier or otherwise. There is, however, a proper relaxation of such requirements if the buyer is himself in a position to make the appropriate arrangements and the seller gives him reasonable notice of the need to do so. It is an improper contract under paragraph (a) for the seller to agree with the carrier to a limited valuation below the true value and thus cut off the buyer's opportunity to recover from the carrier in the event of loss, when the risk of shipment is placed on the buyer by his contract with the seller.

4. Both the language of paragraph (b) and the nature of the situation it concerns indicate that the requirement that the seller must obtain and deliver promptly to the buyer in due form any document necessary to enable him to obtain possession of the goods is intended to cumulate with the other duties of the seller such as those covered in paragraph (a).

In this connection, in the case of pool car shipments a delivery order furnished by the seller on the pool car consignee, or on the carrier for delivery out of a larger quantity, satisfies the requirements of paragraph (b) unless the contract requires some other form of document.

5. This Chapter, unlike the prior uniform statutory provision, makes it the seller's duty to notify the buyer of shipment in all cases. The consequences of his failure to do so, however, are limited in that the buyer may reject on this ground only where material delay or loss ensues.

A standard and acceptable manner of notification in open credit shipments is the sending of an invoice and in the case of documentary contracts is the prompt forwarding of the documents as under paragraph (b) of this section. It is also usual to send on a straight bill of lading but this is not necessary to the required notification. However, should such a document prove necessary or convenient to the buyer, as in the case of loss and claim against the carrier, good faith would require the seller to send it on request.

Frequently the agreement expressly requires prompt notification as by wire or cable. Such a term may be of the essence and the final clause of paragraph (c) does not prevent the parties from making this a particular ground for rejection. To have this vital and irreparable effect upon the seller's duties, such a term should be part of the "dickered" terms written in any "form," or should otherwise be called seasonably and sharply to the seller's attention.

6. Generally, under the final sentence of the section, rejection by the buyer is justified only when the seller's dereliction as to any of the requirements of this section in fact is followed by material delay or damage. It rests on the seller, so far as concerns matters not within the peculiar knowledge of the buyer, to establish that his error has not been followed by events which justify rejection.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-2-505. Seller's shipment under reservation.

Official Comment

[*Corresponding U.C.C. Section:* Section 2-505, U.C.C.]

Prior Uniform Statutory Provision: Section 20(2), (3), (4), Uniform Sales Act.

Changes: Completely rephrased, the "powers" of the parties in cases of reservation being emphasized primarily rather than the "rightfulness" of reservation.

Purposes of Changes: To continue in general the policy of the prior uniform statutory provision with certain modifications of emphasis and language, so that:

1. The security interest reserved to the seller under subsection (1) is restricted to securing payment or performance by the buyer and the seller is strictly limited in his disposition and control of the goods as against the buyer and third parties. Under this Chapter, the provision as to the passing of interest expressly applies "despite any reservation of security title" and also provides that the "rights, obligations and remedies" of the parties are not altered by the incidence of title generally. The security interest, therefore, must be regarded as a means given to the seller to enforce his rights against the buyer which is unaffected by and in turn does not affect the location of title generally. The rules set forth in subsection (1) are not to be altered by

any apparent "contrary intent" of the parties as to passing of title, since the rights and remedies of the parties to the contract of sale, as defined in this Chapter, rest on the contract and its performance or breach and not on stereotyped presumptions as to the location of title.

This Chapter does not attempt to regulate local procedure in regard to the effective maintenance of the seller's security interest when the action is in replevin by the buyer against the carrier.

2. Every shipment of identified goods under a negotiable bill of lading reserves a security interest in the seller under subsection (1) paragraph (a).

It is frequently convenient for the seller to make the bill of lading to the order of a nominee such as his agent at destination, the financing agency to which he expects to negotiate the document or the bank issuing a credit to him. In many instances, also, the buyer is made the order party. This Chapter does not deal directly with the question as to whether a bill of lading made out by the seller to the order of a nominee gives the carrier notice of any rights which the nominee may have so as to limit its freedom or obligation to honor the bill of lading in the hands of the seller as the original shipper if the expected negotiation fails. This is dealt with in the Chapter on Documents of Title (Chapter 7).

3. A non-negotiable bill of lading taken to a party other than the buyer under subsection (1) paragraph (b) reserves possession of the goods as security in the seller but if he seeks to withhold the goods improperly the buyer can tender payment and recover them.

4. In the case of a shipment by non-negotiable bill of lading taken to a buyer, the seller, under subsection (1) retains no security interest or possession as against the buyer and by the shipment he *de facto* loses control as against the carrier except where he rightfully and effectively stops delivery in transit. In cases in which the contract gives the seller the right to payment against delivery, the seller, by making an immediate demand for payment, can show that his delivery is conditional, but this does not prevent the buyer's power to transfer full title to a sub-buyer in ordinary course or other purchaser under Section 30-2-403.

5. Under subsection (2) an improper reservation by the seller which would constitute a breach in no way impairs such of the buyer's rights as result from identification of the goods. The security title reserved by the seller under subsection (1) does not protect his retaining possession or control of the document or the goods for the purpose of exacting more than is due him under the contract.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

30-2-506. Rights of financing agency.

Official Comment

[*Corresponding U.C.C. Section:* Section 2-506, U.C.C.]

[*Code Commissioner Note:* In 2005, Montana adopted Alternative B of the 2003 revision to Article 7 for this section.]

Prior Uniform Statutory Provision: None.

Purposes:

1. "Financing agency" is broadly defined in this Chapter to cover every normal instance in which a party aids or intervenes in the financing of a sales transaction. The term as used in subsection (1) is not in any sense intended as a limitation and covers any other appropriate situation which may arise outside the scope of the definition.

2. "Paying" as used in subsection (1) is typified by the letter of credit, or "authority to pay" situation in which a banker, by arrangement with the buyer or other consignee, pays on his behalf a draft for the price of the goods. It is immaterial whether the draft is formally drawn on the party paying or his principal, whether it is a sight draft paid in cash or a time draft "paid" in the first instance by acceptance, or whether the payment is viewed as absolute or conditional. All of these cases constitute "payment" under this subsection. Similarly, "purchasing for value" is used to indicate the whole area of financing by the seller's banker, and the principle of subsection (1) is applicable without any niceties of distinction between "purchase," "discount," "advance against collection" or the like. But it is important to notice that the only right to have the draft honored that is acquired is that *against the buyer*; if any right against any one else is claimed it will have to be under some separate obligation of that other person. A letter of credit does not necessarily protect *purchasers* of drafts. See Chapter 5. And for the relations of the parties to documentary drafts see Part 5 of Chapter 4.

3. Subsection (1) is made applicable to payments or advances against a draft which "relates to" a shipment of goods and this has been chosen as a term of maximum breadth. In particular

the term is intended to cover the case of a draft against an invoice or against a delivery order. Further, it is unnecessary that there be an explicit assignment of the invoice attached to the draft to bring the transaction within the reason of this subsection.

4. After shipment, "the rights of the shipper in the goods" are merely security rights and are subject to the buyer's right to force delivery upon tender of the price. The rights acquired by the financing agency are similarly limited and, moreover, if the agency fails to procure any outstanding negotiable document of title, it may find its exercise of these rights hampered or even defeated by the seller's disposition of the document to a third party. This section does not attempt to create any new rights in the financing agency against the carrier which would force the latter to honor a stop order from the agency, a stranger to the shipment, or any new rights against a holder to whom a document of title has been duly negotiated under Chapter 7.

5. The deletion of the language "on its face" from subsection (2) is designed to accommodate electronic documents of title without changing the requirement of regularity of the document.

Compiler's Comments

2005 Amendment: Chapter 575 in (2) at end deleted "on its face". Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-2-507. Effect of seller's tender — delivery on condition.

Official Comment

Prior Uniform Statutory Provision: See Sections 11, 41, 42 and 69, Uniform Sales Act.

Purposes:

1. Subsection (1) continues the policies of the prior uniform statutory provisions with respect to tender and delivery by the seller. Under this Chapter the same rules in these matters are applied to present sales and to contracts for sale. But the provisions of this subsection must be read within the framework of the other sections of this Chapter which bear upon the question of delivery and payment.

2. The "unless otherwise agreed" provision of subsection (1) is directed primarily to cases in which payment in advance has been promised or a letter of credit term has been included. Payment "according to the contract" contemplates immediate payment, payment at the end of an agreed credit term, payment by a time acceptance or the like. Under this Act, "contract" means the total obligation in law which results from the parties' agreement including the effect of this Chapter. In this context, therefore, there must be considered the effect in law of such provisions as those on means and manner of payment and on failure of agreed means and manner of payment.

3. Subsection (2) deals with the effect of a conditional delivery by the seller and in such a situation makes the buyer's "right as against the seller" conditional upon payment. These words are used as words of limitation to conform with the policy set forth in the bona fide purchase sections of this Chapter. Should the seller after making such a conditional delivery fail to follow up his rights, the condition is waived. The provision of this Chapter for a ten day limit within which the seller may reclaim goods delivered on credit to an insolvent buyer is also applicable here.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

30-2-508. Cure by seller of improper tender or delivery — replacement.

Official Comment

Prior Uniform Statutory Provision: None.

Purposes:

1. Subsection (1) permits a seller who has made a non-conforming tender in any case to make a conforming delivery within the contract time upon seasonable notification to the buyer. It applies even where the seller has taken back the non-conforming goods and refunded the purchase price. He may still make a good tender within the contract period. The closer, however,

it is to the contract date, the greater is the necessity for extreme promptness on the seller's part in notifying of his intention to cure, if such notification is to be "seasonable" under this subsection.

The rule of this subsection, moreover, is qualified by its underlying reasons. Thus if, after contracting for June delivery, a buyer later makes known to the seller his need for shipment early in the month and the seller ships accordingly, the "contract time" has been cut down by the supervening modification and the time for cure of tender must be referred to this modified time term.

2. Subsection (2) seeks to avoid injustice to the seller by reason of a surprise rejection by the buyer. However, the seller is not protected unless he had "reasonable grounds to believe" that the tender would be acceptable. Such reasonable grounds can lie in prior course of dealing, course of performance or usage of trade as well as in the particular circumstances surrounding the making of the contract. The seller is charged with commercial knowledge of any factors in a particular sales situation which require him to comply strictly with his obligations under the contract as, for example, strict conformity of documents in an overseas shipment or the sale of precision parts of chemicals for use in manufacture. Further, if the buyer gives notice either implicitly, as by a prior course of dealing involving rigorous inspections, or expressly, as by the deliberate inclusion of a "no replacement" clause in the contract, the seller is to be held to rigid compliance. If the clause appears in a "form" contract evidence that it is out of line with trade usage or the prior course of dealing and was not called to the seller's attention may be sufficient to show that the seller had reasonable grounds to believe that the tender would be acceptable.

3. The words "a further reasonable time to substitute a conforming tender" are intended as words of limitation to protect the buyer. What is a "reasonable time" depends upon the attending circumstances. Compare Section 30-2-511 on the comparable case of a seller's surprise demand for legal tender.

4. Existing trade usages permitting variations without rejection but with price allowance enter into the agreement itself as contractual limitations of remedy and are not covered by this section.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

Case Notes

Right to Rescind: Defendant/buyer did not lose his right to rescind by failing to give plaintiff/seller adequate opportunity to "cure". Inconvenience, economic loss, and lack of cooperation by the plaintiff justified defendant's purchase of replacement goods and rescission of his agreement with plaintiff. Transcont. Refrigeration Co. v. Figgins, 179 M 12, 585 P2d 1301 (1978).

30-2-509. Risk of loss in the absence of breach.

Official Comment

[*Corresponding U.C.C. Section:* Section 2-509, U.C.C.]

[*Code Commissioner Note:* In 2005, Montana adopted Alternative B of the 2003 revision to Article 7 for this section.]

Prior Uniform Statutory Provision: Section 22, Uniform Sales Act.

Changes: Rewritten, subsection (3) of this section modifying prior law.

Purposes of Changes: To make it clear that:

1. The underlying theory of these sections on risk of loss is the adoption of the contractual approach rather than an arbitrary shifting of the risk with the "property" in the goods. The scope of the present section, therefore, is limited strictly to those cases where there has been no breach by the seller. Where for any reason his delivery or tender fails to conform to the contract, the present section does not apply and the situation is governed by the provisions on effect of breach on risk of loss.

2. The provisions of subsection (1) apply where the contract "requires or authorizes" shipment of the goods. This language is intended to be construed parallel to comparable language in the section on shipment by seller. In order that the goods be "duly delivered to the carrier" under paragraph (a) a contract must be entered into with the carrier which will satisfy the requirements of the section on shipment by the seller and the delivery must be made under circumstances which will enable the seller to take any further steps necessary to a due tender. The underlying reason of this subsection does not require that the shipment be made after contracting, but where, for example, the seller buys the goods afloat and later diverts the shipment to the buyer, he must identify the goods to the contract before the risk of loss can pass. To transfer the risk it is enough that a proper shipment and a proper identification come to apply to the same goods although,

aside from special agreement, the risk will not pass retroactively to the time of shipment in such a case.

3. Whether the contract involves delivery at the seller's place of business or at the situs of the goods, a merchant seller cannot transfer risk of loss and it remains upon him until actual receipt by the buyer, even though full payment has been made and the buyer has been notified that the goods are at his disposal. Protection is afforded him, in the event of breach by the buyer, under the next section.

The underlying theory of this rule is that a merchant who is to make physical delivery at his own place continues meanwhile to control the goods and can be expected to insure his interest in them. The buyer, on the other hand, has no control of the goods and it is extremely unlikely that he will carry insurance on goods not yet in his possession.

4. Where the agreement provides for delivery of the goods as between the buyer and seller without removal from the physical possession of a bailee, the provisions on manner of tender of delivery apply on the point of transfer of risk. Due delivery of a negotiable document of title covering the goods or acknowledgment by the bailee that he holds for the buyer completes the "delivery" and passes the risk. See definition of delivery in Article 1, Section 1-201 [30-1-201] and the definition of control in Article 7, Section 7-106 [30-7-107].

5. The provisions of this section are made subject by subsection (4) to the "contrary agreement" of the parties. This language is intended as the equivalent of the phrase "unless otherwise agreed" used more frequently throughout this Act. "Contrary" is in no way used as a word of limitation and the buyer and seller are left free to readjust their rights and risks as declared by this section in any manner agreeable to them. Contrary agreement can also be found in the circumstances of the case, a trade usage or practice, or a course of dealing or performance.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

2005 Amendment: Chapter 575 in (2)(a) at beginning substituted "on the buyer's receipt of possession or control" for "on his receipt"; in (2)(c) after "receipt of" inserted "possession or control of" and substituted "direction to deliver in a record" for "written direction to deliver"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

Case Notes

Delivery Versus Acceptance: The Supreme Court rejected defendant's contention that Montana Seeds, Inc., failed to establish its claim for goods "sold and delivered" by not proving actual delivery. The determining factor was whether defendant "accepted" the goods. Here there were two shipments. Only the second shipment's acceptance was challenged by defendant based on his contention that it was misdelivered. However, defendant bore the risk of loss because he did not specify a particular destination. His cause of action for misdelivery was against the carrier. Mont. Seeds, Inc. v. Holliday, 178 M 119, 582 P2d 1223 (1978).

30-2-510. Effect of breach on risk of loss.

Official Comment

Prior Uniform Statutory Provision: None.

Purposes: To make clear that:

1. Under subsection (1) the seller by his individual action cannot shift the risk of loss to the buyer unless his action conforms with all the conditions resting on him under the contract.

2. The "cure" of defective tenders contemplated by subsection (1) applies only to those situations in which the seller makes changes in goods already tendered, such as repair, partial substitution, sorting out from an improper mixture and the like since "cure" by repossession and new tender has no effect on the risk of loss of the goods originally tendered. The seller's privilege of cure does not shift the risk, however, until the cure is completed.

Where defective documents are involved a cure of the defect by the seller or a waiver of the defects by the buyer will operate to shift the risk under this section. However, if the goods have been destroyed prior to the cure or the buyer is unaware of their destruction at the time he waives the defect in the documents, the risk of the loss must still be borne by the seller, for the risk shifts only at the time of cure, waiver of documentary defects or acceptance of the goods.

3. In cases where there has been a breach of the contract, if the one in control of the goods is the aggrieved party, whatever loss or damage may prove to be uncovered by his insurance falls upon the contract breaker under subsections (2) and (3) rather than upon him. The word "effective" as applied to insurance coverage in those subsections is used to meet the case of supervening insolvency of the insurer. The "deficiency" referred to in the text means such deficiency in the insurance coverage as exists without subrogation. This section merely distributes the risk of loss as stated and is not intended to be disturbed by any subrogation of an insurer.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

30-2-511. Tender of payment by buyer — payment by check.

Official Comment

Prior Uniform Statutory Provision: Section 42, Uniform Sales Act.

Changes: Rewritten by this section and Section 30-2-507.

Purposes of Changes:

1. The requirement of payment against delivery in subsection (1) is applicable to non-commercial sales generally and to ordinary sales at retail although it has no application to the great body of commercial contracts which carry credit terms. Subsection (1) applies also to documentary contracts in general and to contracts which look to shipment by the seller but contain no term on time and manner of payment, in which situations the payment may, in proper case, be demanded against delivery of appropriate documents.

In the case of specific transactions such as C.O.D. sales or agreements providing for payment against documents, the provisions of this subsection must be considered in conjunction with the special sections of the Chapter dealing with such terms. The provision that tender of payment is a condition to the seller's duty to tender and complete "any delivery" integrates this section with the language and policy of the section on delivery in several lots which call for separate payment. Finally, attention should be directed to the provision on right to adequate assurance of performance which recognizes, even before the time for tender, an obligation on the buyer not to impair the seller's expectation of receiving payment in due course.

2. Unless there is agreement otherwise the concurrence of the conditions as to tender of payment and tender of delivery requires their performance at a single place or time. This Chapter determines that place and time by determining in various other sections the place and time for tender of delivery under various circumstances and in particular types of transactions. The sections dealing with time and place of delivery together with the section on right to inspection of goods answer the subsidiary question as to when payment may be demanded before inspection by the buyer.

3. The essence of the principle involved in subsection (2) is avoidance of commercial surprise at the time of performance. The section on substituted performance covers the peculiar case in which legal tender is not available to the commercial community.

4. Subsection (3) is concerned with the rights and obligations as between the parties to a sales transaction when payment is made by check. This Chapter recognizes that the taking of a seemingly solvent party's check is commercially normal and proper and, if due diligence is exercised in collection, is not to be penalized in any way. The conditional character of the payment under this section refers only to the effect of the transaction "as between the parties" thereto and does not purport to cut into the law of "absolute" and "conditional" payment as applied to such other problems as the discharge of sureties or the responsibilities of a drawee bank which is at the same time an agent for collection.

The phrase "by check" includes not only the buyer's own but any check which does not effect a discharge under Chapter 3 (Section 30-3-310). Similarly the reason of this subsection should apply and the same result should be reached where the buyer "pays" by sight draft on a commercial firm which is financing him.

5. Under subsection (3) payment by check is defeated if it is not honored upon due presentment. This corresponds to the provisions of Chapter on Commercial Paper. (Section 30-3-310). But if the seller procures certification of the check instead of cashing it, the buyer is discharged. (Section 30-3-411 [now repealed]).

6. Where the instrument offered by the buyer is not a payment but a credit instrument such as a note or a check postdated by even one day, the seller's acceptance of the instrument insofar as third parties are concerned, amounts to a delivery on credit and his remedies are set forth in the section on buyer's insolvency. As between the buyer and the seller, however, the matter turns on the present subsection and the section on conditional delivery and subsequent dishonor of the instrument gives the seller rights on it as well as for breach of the contract for sale.

Compiler's Comments

1991 Amendment: In (3) substituted reference to "30-3-310" for "30-3-802"; and made minor change in style.

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

30-2-512. Payment by buyer before inspection.

Official Comment

Prior Uniform Statutory Provision: None, but see Sections 47 and 49, Uniform Sales Act.

Purposes:

1. Subsection (1) of the present section recognizes that the essence of a contract providing for payment before inspection is the intention of the parties to shift to the buyer the risks which would usually rest upon the seller. The basic nature of the transaction is thus preserved and the buyer is in most cases required to pay first and litigate as to any defects later.

2. "Inspection" under this section is an inspection in a manner reasonable for detecting defects in goods whose surface appearance is satisfactory.

3. Clause (a) of this subsection states an exception to the general rule based on common sense and normal commercial practice. The apparent non-conformity referred to is one which is evident in the mere process of taking delivery.

4. Clause (b) is concerned with contracts for payment against documents and incorporates the general clarification and modification of the case law contained in the section on excuse of a financing agency. Section 30-5-114 [now repealed].

5. Subsection (2) makes explicit the general policy of the Uniform Sales Act that the payment required before inspection in no way impairs the buyer's remedies or rights in the event of a default by the seller. The remedies preserved to the buyer are all of his remedies, which include as a matter of reason the remedy for total non-delivery after payment in advance.

The provision on performance or acceptance under reservation of rights does not apply to the situations contemplated here in which payment is made in due course under the contract and the buyer need not pay "under protest" or the like in order to preserve his rights as to defects discovered upon inspection.

6. This section applies to cases in which the contract requires payment before inspection either by the express agreement of the parties or by reason of the effect in law of that contract. The present section must therefore be considered in conjunction with the provision on right to inspection of goods which sets forth the instances in which the buyer is not entitled to inspection before payment.

Compiler's Comments

1997 Amendment: Chapter 536 in (1)(b), at end, substituted "30-5-129(2)" for "30-5-114"; and made minor changes in style.

30-2-513. Buyer's right to inspection of goods.

Official Comment

[*Corresponding U.C.C. Section:* Section 2-513, U.C.C.]

Prior Uniform Statutory Provision: Section 47(2), (3), Uniform Sales Act.

Changes: Rewritten, Subsections (2) and (3) being new.

Purposes of Changes and New Matter: To correspond in substance with the prior uniform statutory provision and to incorporate in addition some of the results of the better case law so that:

1. The buyer is entitled to inspect goods as provided in subsection (1) unless it has been otherwise agreed by the parties. The phrase "unless otherwise agreed" is intended principally to cover such situations as those outlined in subsections (3) and (4) and those in which the agreement of the parties negates inspection before tender of delivery. However, no agreement by the parties can displace the entire right of inspection except where the contract is simply for the sale of "this thing." Even in a sale of boxed goods "as is" inspection is a right of the buyer, since if the boxes prove to contain some other merchandise altogether the price can be recovered back; nor do the limitations of the provision on effect of acceptance apply in such a case.

2. The buyer's right of inspection is available to him upon tender, delivery or appropriation of the goods with notice to him. Since inspection is available to him on tender, where payment is due against delivery he may, unless otherwise agreed, make his inspection before payment of the price. It is also available to him after receipt of the goods and so may be postponed after receipt for a reasonable time. Failure to inspect before payment does not impair the right to inspect after receipt of the goods unless the case falls within subsection (4) on agreed and exclusive inspection provisions. The right to inspect goods which have been appropriated with notice to the buyer holds whether or not the sale was by sample.

3. The buyer may exercise his right of inspection at any reasonable time or place and in any reasonable manner. It is not necessary that he select the most appropriate time, place or manner to inspect or that his selection be the customary one in the trade or locality. Any reasonable time, place or manner is available to him and the reasonableness will be determined by trade usages, past practices between the parties and the other circumstances of the case.

The last sentence of subsection (1) makes it clear that the place of arrival of shipped goods is a reasonable place for their inspection.

4. Expenses of an inspection made to satisfy the buyer of the seller's performance must be assumed by the buyer in the first instance. Since the rule provides merely for an allocation of expense there is no policy to prevent the parties from providing otherwise in the agreement. Where the buyer would normally bear the expenses of the inspection but the goods are rightly rejected because of what the inspection reveals, demonstrable and reasonable costs of the inspection are part of his incidental damage caused by the seller's breach.

5. In the case of payment against documents, subsection (3) requires payment before inspection, since shipping documents against which payment is to be made will commonly be tendered while the goods are still in transit. This Chapter recognizes no exception in any peculiar case in which the goods happen to arrive before the documents are tendered. However, where by the agreement payment is to await the arrival of the goods, inspection before payment becomes proper since the goods are then "available for inspection."

Where by the agreement the documents are to be tendered after arrival of the goods, the buyer is entitled to inspect before payment since the goods are then "available for inspection". Proof of usage is not necessary to establish this right, but if inspection before payment is disputed the contrary must be established by usage or by an explicit contract term to that effect.

For the same reason, that the goods are available for inspection, a term calling for payment against storage documents or a delivery order does not normally bar the buyer's right to inspection before payment under subsection (3)(b). This result is reinforced by the buyer's right under subsection (1) to inspect goods which have been appropriated with notice to him.

6. Under subsection (4) an agreed place or method of inspection is generally held to be intended as exclusive. However, where compliance with such an agreed inspection term becomes impossible, the question is basically one of intention. If the parties clearly intend that the method of inspection named is to be a necessary condition without which the entire deal is to fail, the contract is at an end if that method becomes impossible. On the other hand, if the parties merely seek to indicate a convenient and reliable method but do not intend to give up the deal in the event of its failure, any reasonable method of inspection may be substituted under this Chapter.

Since the purpose of an agreed place of inspection is only to make sure at that point whether or not the goods will be thrown back, the "exclusive" feature of the named place is satisfied under this Chapter if the buyer's failure to inspect there is held to be an acceptance with the knowledge of such defects as inspection would have revealed within the section on waiver of buyer's objections by failure to particularize. Revocation of the acceptance is limited to the situations stated in the section pertaining to that subject. The reasonable time within which to give notice of defects within the section on notice of breach begins to run from the point of the "acceptance."

7. Clauses on time of inspection are commonly clauses which limit the time in which the buyer must inspect and give notice of defects. Such clauses are therefore governed by the section of this Chapter which requires that such a time limitation must be reasonable.

8. Inspection under this Chapter is not to be regarded as a "condition precedent to the passing of title" so that risk until inspection remains on the seller. Under subsection (4) such an approach cannot be sustained. Issues between the buyer and seller are settled in this Chapter almost wholly by special provisions and not by the technical determination of the locus of the title. Thus "inspection as a condition to the passing of title" becomes a concept almost without meaning. However, in peculiar circumstances inspection may still have some of the consequences hitherto sought and obtained under that concept.

9. "Inspection" under this section has to do with the buyer's check-up on whether the seller's performance is in accordance with a contract previously made and is not to be confused with the "examination" of the goods or of a sample or model of them at the time of contracting which may affect the warranties involved in the contract.

30-2-514. When documents deliverable on acceptance — when on payment.

Official Comment

Prior Uniform Statutory Provision: Section 41, Uniform Bills of Lading Act.

Changes: Rewritten.

Purposes of Changes: To make the provision one of general application so that:

1. It covers any document against which a draft may be drawn, whatever may be the form of the document, and applies to interpret the action of a seller or consignor insofar as it may affect the rights and duties of any buyer, consignee or financing agency concerned with the paper. Supplementary or corresponding provisions are found in Sections 30-4-503 and 30-5-112 [now repealed].

2. An "arrival" draft is a sight draft within the purpose of this section.

30-2-515. Preserving evidence of goods in dispute.

Official Comment

Prior Uniform Statutory Provision: None.

Purposes:

1. To meet certain serious problems which arise when there is a dispute as to the quality of the goods and thereby perhaps to aid the parties in reaching a settlement, and to further the use of devices which will promote certainty as to the condition of the goods, or at least aid in preserving evidence of their condition.

2. Under paragraph (a), to afford either party an opportunity for preserving evidence, whether or not agreement has been reached, and thereby to reduce uncertainty in any litigation and, in turn perhaps, to promote agreement.

Paragraph (a) does not conflict with the provisions on the seller's right to resell rejected goods or the buyer's similar right. Apparent conflict between these provisions which will be suggested in certain circumstances is to be resolved by requiring prompt action by the parties. Nor does paragraph (a) impair the effect of a term for payment before inspection. Short of such defects as amount to fraud or substantial failure of consideration, non-conformity is neither an excuse nor a defense to an action for non-acceptance of documents. Normally, therefore, until the buyer has made payment, inspected and rejected the goods, there is no occasion or use for the rights under paragraph (a).

3. Under paragraph (b), to provide for third party inspection upon the agreement of the parties, thereby opening the door to amicable adjustments based upon the findings of such third parties.

The use of the phrase "conformity or condition" makes it clear that the parties' agreement may range from a complete settlement of all aspects of the dispute by a third party to the use of a third party merely to determine and record the condition of the goods so that they can be resold or used to reduce the stake in controversy. "Conformity", at one end of the scale of possible issues, includes the whole question of interpretation of the agreement and its legal effect, the state of the goods in regard to quality and condition, whether any defects are due to factors which operate at the risk of the buyer, and the degree of non-conformity where that may be material. "Condition", at the other end of the scale, includes nothing but the degree of damage or deterioration which the goods show. Paragraph (b) is intended to reach any point in the gamut which the parties may agree upon.

The principle of the section on reservation of rights reinforces this paragraph in simplifying such adjustments as the parties wish to make in partial settlement while reserving their rights as to any further points. Paragraph (b) also suggests the use of arbitration, where desired, of any points left open, but nothing in this section is intended to repeal or amend any statute governing arbitration. Where any question arises as to the extent of the parties' agreement under the paragraph, the presumption should be that it was meant to extend only to the relation between the contract description and the goods as delivered, since that is what a craftsman in the trade would normally be expected to report upon. Finally, a written and authenticated report of inspection or tests by a third party, whether or not sampling has been practicable, is entitled to be admitted as evidence under this Act, for it is a third party document.

Part 6
Breach, Repudiation, and Excuse

30-2-601. Buyer's rights on improper delivery.

Official Comment

Prior Uniform Statutory Provision: No one general equivalent provision but numerous provisions, dealing with situations of non-conformity where buyer may accept or reject, including Sections 11, 44 and 69(1), Uniform Sales Act.

Changes: Partial acceptance in good faith is recognized and the buyer's remedies on the contract for breach of warranty and the like, where the buyer has returned the goods after transfer of title, are no longer barred.

Purposes of Changes: To make it clear that:

1. A buyer accepting a non-conforming tender is not penalized by the loss of any remedy otherwise open to him. This policy extends to cover and regulate the acceptance of a part of any lot improperly tendered in any case where the price can reasonably be apportioned. Partial acceptance is permitted whether the part of the goods accepted conforms or not. The only limitation on partial acceptance is that good faith and commercial reasonableness must be used to avoid undue impairment of the value of the remaining portion of the goods. This is the reason for the insistence on the "commercial unit" in paragraph (c). In this respect, the test is not only what unit has been the basis of contract, but whether the partial acceptance produces so materially adverse an effect on the remainder as to constitute bad faith.

2. Acceptance made with the knowledge of the other party is final. An original refusal to accept may be withdrawn by a later acceptance if the seller has indicated that he is holding the tender open. However, if the buyer attempts to accept, either in whole or in part, after his original rejection has caused the seller to arrange for other disposition of the goods, the buyer must answer for any ensuing damage since the next section provides that any exercise of ownership after rejection is wrongful as against the seller. Further, he is liable even though the seller may choose to treat his action as acceptance rather than conversion, since the damage flows from the misleading notice. Such arrangements for resale or other disposition of the goods by the seller must be viewed as within the normal contemplation of a buyer who has given notice of rejection. However, the buyer's attempts in good faith to dispose of defective goods where the seller has failed to give instructions within a reasonable time are not to be regarded as an acceptance.

Case Notes

Buyer Entitled to Damages for Shipment of Damaged Plants: Reed owned a greenhouse and ordered a shipment of poinsettias from McCalif for Christmas. When the plants arrived, many were damaged. Reed refused to pay $3,027.09 for the marketable plants that he kept and resold, contending that he had lost $8,683.95 on the damaged plants for which he had already received purchase orders from other buyers. The Supreme Court held that the record proved that there was no other source for replacement of the damaged plants and that McCalif was aware of that fact and the fact that Reed had entered into contracts for the resale of the plants. The Supreme Court ruled that Reed had the right to accept part of the plants received and reject the rest and that Reed was entitled to incidental and consequential damages because of McCalif's breach. The measure of damages was the difference between what Reed owed for the plants that he kept and what he lost on the orders that he could not fill. McCalif Grower Supplies, Inc. v. Reed, 272 M 254, 900 P2d 880, 52 St. Rep. 659 (1995).

Timely Rejection of Defective Goods: Vendees who leased a printing press from the vendor stopped making payments, claiming they believed the press to be defective. When the vendor sued to make the vendees liable for a lump-sum payment, summary judgment was entered for the vendor. On appeal, the judgment was set aside and the agreement between the parties was determined to be a sales contract subject to the statutory U.C.C. provisions regulating sales. The cause was remanded for trial on the question of whether the vendees timely and properly rejected the press, under 30-2-601 and 30-2-602, when they stopped monthly payments after two payments. Lessees contend they notified the lessor immediately and more than once that the press was defective; the lessor has neither admitted nor denied these contentions, which are questions of fact for the trial court to determine upon remand. (See 1991 enactment of chapter 2A.) Beneficial Commercial Corp. v. Cottrell, 212 M 493, 688 P2d 1254, 41 St. Rep. 1888 (1984).

Sufficient Rejection of Nonconforming Goods: Plaintiff sold defendants an irrigation system and pump. Plaintiff substituted a different type of pump for the one ordered by defendants. Plaintiff and his supplier installed the system, and defendants paid for everything but the pump and its installation. Plaintiff and his supplier supervised the digging of the sump for the installation of the pump but did not test it. The pump became clogged before any water ever came out of it. The supplier cleaned the pump and had an agent reinstall it. Defendants tried unsuccessfully to get the system to work and called plaintiff to complain several times. Defendants finally told plaintiff to come and get the pump and refused to pay for it. They later purchased a different pump which operated the system properly. Plaintiff sued for the price of the pump and installation costs. The District Court entered judgment for the defendants. Plaintiff contends that the District Court's findings of fact and conclusions of law were insufficient in failing to adequately address the provisions of the U.C.C. governing rejection of nonconforming goods. The Supreme Court found that although the findings and conclusions could have been better, there was substantial evidence to support the conclusions that: (1) the goods were nonconforming; (2) there was a failure to cure the defects of the pump; and (3) the use of the pump was in fact a prolonged effort to determine why the pump failed to work and to cure the defect, and as such was not an act inconsistent with the seller's ownership. There was no acceptance by the defendants, no use inconsistent with the ownership of the plaintiff, and no delay in offering the return of the nonconforming pump significant enough to justify a conclusion that defendants had accepted the pump. Steinmetz v. Robertus, 196 M 311, 637 P2d 31, 38 St. Rep. 2067 (1981).

30-2-602. Manner and effect of rightful rejection.

Official Comment

Prior Uniform Statutory Provision: Section 50, Uniform Sales Act.

Changes: Rewritten.

Purposes of Changes: To make it clear that:

1. A tender or delivery of goods made pursuant to a contract of sale, even though wholly non-conforming, requires affirmative action by the buyer to avoid acceptance. Under subsection (1), therefore, the buyer is given a reasonable time to notify the seller of his rejection, but without such seasonable notification his rejection is ineffective. The sections of this Chapter dealing with inspection of goods must be read in connection with the buyer's reasonable time for action under this subsection. Contract provisions limiting the time for rejection fall within the rule of the section on "Time" and are effective if the time set gives the buyer a reasonable time for discovery of defects. What constitutes a due "notifying" of rejection by the buyer to the seller is defined in Section 30-1-201.

2. Subsection (2) lays down the normal duties of the buyer upon rejection, which flow from the relationship of the parties. Beyond his duty to hold the goods with reasonable care for the buyer's [seller's] disposition, this section continues the policy of prior uniform legislation in generally relieving the buyer from any duties with respect to them, except when the circumstances impose the limited obligation of salvage upon him under the next section.

3. The present section applies only to rightful rejection by the buyer. If the seller has made a tender which in all respects conforms to the contract, the buyer has a positive duty to accept and his failure to do so constitutes a "wrongful rejection" which gives the seller immediate remedies for breach. Subsection (3) is included here to emphasize the sharp distinction between the rejection of an improper tender and the non-acceptance which is a breach by the buyer.

4. The provisions of this section are to be appropriately limited or modified when a negotiation is in process.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

Case Notes

Failure to Notify Seller of Nonconformity of Goods — Damages Unwarranted: Defendants claimed that a jury instruction should have been given regarding damages owing under the Uniform Commercial Code for a sale of nonconforming goods. However, defendants did not reject the goods upon delivery or notify the seller within a reasonable time regarding the nonconformity. Because no damages were owing, an instruction on the measure of damages was not appropriate. NW. Truck & Trailer Sales, Inc. v. Dvorak, 269 M 150, 887 P2d 260, 51 St. Rep. 1530 (1994).

Timely Rejection of Defective Goods: Vendees who leased a printing press from the vendor stopped making payments, claiming they believed the press to be defective. When the vendor sued to make the vendees liable for a lump-sum payment, summary judgment was entered for the vendor. On appeal, the judgment was set aside and the agreement between the parties was determined to be a sales contract subject to the statutory U.C.C. provisions regulating sales. The cause was remanded for trial on the question of whether the vendees timely and properly rejected the press, under 30-2-601 and 30-2-602, when they stopped monthly payments after two payments. Lessees contend they notified the lessor immediately and more than once that the press was defective; the lessor has neither admitted nor denied these contentions, which are questions of fact for the trial court to determine upon remand. (See 1991 enactment of chapter 2A.) Beneficial Commercial Corp. v. Cottrell, 212 M 493, 688 P2d 1254, 41 St. Rep. 1888 (1984).

Sufficient Rejection of Nonconforming Goods: Plaintiff sold defendants an irrigation system and pump. Plaintiff substituted a different type of pump for the one ordered by defendants. Plaintiff and his supplier installed the system, and defendants paid for everything but the pump and its installation. Plaintiff and his supplier supervised the digging of the sump for the installation of the pump but did not test it. The pump became clogged before any water ever came out of it. The supplier cleaned the pump and had an agent reinstall it. Defendants tried unsuccessfully to get the system to work and called plaintiff to complain several times. Defendants finally told plaintiff to come and get the pump and refused to pay for it. They later purchased a different pump which operated the system properly. Plaintiff sued for the price of the pump and installation costs. The District Court entered judgment for the defendants. Plaintiff contends that the District Court's findings of fact and conclusions of law were insufficient in failing to adequately address the provisions of the U.C.C. governing rejection of nonconforming goods. The Supreme Court found that although the findings and conclusions could have been better, there was substantial evidence to support the conclusions that: (1) the goods were nonconforming; (2) there was a failure to cure the defects of the pump; and (3) the use of the pump was in fact a prolonged effort to determine why the pump failed to work and to cure the defect, and as such was not an act inconsistent with the seller's ownership. There was no acceptance by the defendants, no use inconsistent with the ownership of the plaintiff, and no delay in offering the return of the nonconforming pump significant enough to justify a conclusion that defendants had accepted the pump. Steinmetz v. Robertus, 196 M 311, 637 P2d 31, 38 St. Rep. 2067 (1981).

30-2-603. Merchant buyer's duties as to rightfully rejected goods.

Official Comment

Prior Uniform Statutory Provision: None.

Purposes:

1. This section recognizes the duty imposed upon the merchant buyer by good faith and commercial practice to follow any reasonable instructions of the seller as to reshipping, storing, delivery to a third party, reselling or the like. Subsection (1) goes further and extends the duty to include the making of reasonable efforts to effect a salvage sale where the value of the goods is threatened and the seller's instructions do not arrive in time to prevent serious loss.

2. The limitations on the buyer's duty to resell under subsection (1) are to be liberally construed. The buyer's duty to resell under this section arises from commercial necessity and thus is present only when the seller has "no agent or place of business at the market of rejection". A financing agency which is acting in behalf of the seller in handling the documents rejected by the buyer is sufficiently the seller's agent to lift the burden of salvage resale from the buyer. (See provisions of Sections 30-4-503 and 30-5-112 [now repealed] on bank's duties with respect to rejected documents.) The buyer's duty to resell is extended only to goods in his "possession or control", but these are intended as words of wide, rather than narrow, import. In effect, the measure of the buyer's "control" is whether he can practicably effect control without undue commercial burden.

3. The explicit provisions for reimbursement and compensation to the buyer in subsection (2) are applicable and necessary only where he is not acting under instructions from the seller. As provided in subsection (1) the seller's instructions to be "reasonable" must on demand of the buyer include indemnity for expenses.

4. Since this section makes the resale of perishable goods an affirmative duty in contrast to a mere right to sell as under the case law, subsection (3) makes it clear that the buyer is liable only for the exercise of good faith in determining whether the value of the goods is sufficiently threatened to justify a quick resale or whether he has waited a sufficient length of time for instructions, or what a reasonable means and place of resale is.

5. A buyer who fails to make a salvage sale when his duty to do so under this section has arisen is subject to damages pursuant to the section on liberal administration of remedies.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

30-2-604. Buyer's options as to salvage of rightfully rejected goods.

Official Comment

Prior Uniform Statutory Provision: None.

Purposes:

The basic purpose of this section is twofold: on the one hand it aims at reducing the stake in dispute and on the other at avoiding the pinning of a technical "acceptance" on a buyer who has taken steps towards realization on or preservation of the goods in good faith. This section is essentially a salvage section and the buyer's right to act under it is conditioned upon (1) non-conformity of the goods, (2) due notification of rejection to the seller under the section on manner of rejection, and (3) the absence of any instructions from the seller which the merchant-buyer has a duty to follow under the preceding section.

This section is designed to accord all reasonable leeway to a rightfully rejecting buyer acting in good faith. The listing of what the buyer may do in the absence of instructions from the seller is intended to be not exhaustive but merely illustrative. This is not a "merchant's" section and the options are pure options given to merchant and non-merchant buyers alike. The merchant-buyer, however, may in some instances be under a duty rather than an option to resell under the provisions of the preceding section.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-2-605. Waiver of buyer's objections by failure to particularize.

Official Comment

[*Corresponding U.C.C. Section:* Section 2-605, U.C.C.]

Prior Uniform Statutory Provision: None.

Purposes:

1. The present section rests upon a policy of permitting the buyer to give a quick and informal notice of defects in a tender without penalizing him for omissions in his statement, while at the same time protecting a seller who is reasonably misled by the buyer's failure to state curable defects.

2. Where the defect in a tender is one which could have been cured by the seller, a buyer who merely rejects the delivery without stating his objections to it is probably acting in commercial bad faith and seeking to get out of a deal which has become unprofitable. Subsection (1) (a), following the general policy of this Chapter which looks to preserving the deal wherever possible, therefore insists that the seller's right to correct his tender in such circumstances be protected.

3. When the time for cure is past, subsection (1)(b) makes it plain that a seller is entitled upon request to a final statement of objections upon which he can rely. What is needed is that he make clear to the buyer exactly what is being sought. A formal demand under paragraph (b) will be sufficient in the case of a merchant-buyer.

4. Subsection (2) applies to the particular case of documents the same principle which the section on effects of acceptance applies to the case of goods. The matter is dealt with in this section in term of "waiver" of objections rather than of right to revoke acceptance, partly to avoid any confusion with the problems of acceptance of goods and partly because defects in documents which are not taken as grounds for rejection are generally minor ones. The only defects concerned in the present subsection are defects in the documents which are apparent. This rule applies to both tangible and electronic documents of title. Where payment is required against the documents they must be inspected before payment, and the payment then constitutes acceptance of the documents. Under the section dealing with this problem, such acceptance of the documents does not constitute an acceptance of the goods or impair any options or remedies of the buyer for their improper delivery. Where the documents are delivered without requiring such contemporary action as payment from the buyer, the reason of the next section on what constitutes acceptance of goods, applies. Their acceptance by non-objection is therefore postponed until after a reasonable time for their inspection. In either situation, however, the buyer "waives" only the defects apparent in the documents.

Compiler's Comments

2005 Amendment: Chapter 575 in (2) near end substituted "in the documents" for "on the face of the documents"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-2-606. What constitutes acceptance of goods.

Official Comment

Prior Uniform Statutory Provision: Section 48, Uniform Sales Act.

Changes: Rewritten, the qualification in paragraph (c) and subsection (2) being new; otherwise the general policy of the prior legislation is continued.

Purposes of Changes and New Matter: To make it clear that:

1. Under this Chapter "acceptance" as applied to goods means that the buyer, pursuant to the contract, takes particular goods which have been appropriated to the contract as his own, whether or not he is obligated to do so, and whether he does so by words, action, or silence when it is time to speak. If the goods conform to the contract, acceptance amounts only to the performance by the buyer of one part of his legal obligation.

2. Under this Chapter acceptance of goods is always acceptance of identified goods which have been appropriated to the contract or are appropriated by the contract. There is no provision for "acceptance of title" apart from acceptance in general, since acceptance of title is not material under this Chapter to the detailed rights and duties of the parties. (See Section 30-2-401). The refinements of the older law between acceptance of goods and of title become unnecessary in view of the provisions of the sections on effect and revocation of acceptance, on effects of identification and on risk of loss, and those sections which free the seller's and buyer's remedies from the complications and confusions caused by the question of whether title has or has not passed to the buyer before breach.

3. Under paragraph (a), payment made after tender is always one circumstance tending to signify acceptance of the goods but in itself it can never be more than one circumstance and is not conclusive. Also, a conditional communication of acceptance always remains subject to its expressed conditions.

4. Under paragraph (c), any action taken by the buyer, which is inconsistent with his claim that he has rejected the goods, constitutes an acceptance. However, the provisions of paragraph (c) are subject to the sections dealing with rejection by the buyer which permit the buyer to take certain actions with respect to the goods pursuant to his options and duties imposed by those sections, without effecting an acceptance of the goods. The second clause of paragraph (c) modifies some of the prior case law and makes it clear that "acceptance" in law based on the wrongful act of the acceptor is acceptance only as against the wrongdoer and then only at the option of the party wronged.

In the same manner in which a buyer can bind himself, despite his insistence that he is rejecting or has rejected the goods, by an act inconsistent with the seller's ownership under paragraph (c), he can obligate himself by a communication of acceptance despite a prior rejection under paragraph (a). However, the sections on buyer's rights on improper delivery and on the effect of rightful rejection, make it clear that after he once rejects a tender, paragraph (a) does not operate in favor of the buyer unless the seller has re-tendered the goods or has taken affirmative action indicating that he is holding the tender open. See also Comment 2 to Section 30-2-601.

5. Subsection (2) supplements the policy of the section on buyer's rights on improper delivery, recognizing the validity of a partial acceptance but insisting that the buyer exercise this right only as to whole commercial units.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

Case Notes

Finding of Fact Inconsistent With Conclusions of Law: The lower court found that defendant allowed plaintiff to take a silage chopper on a "tryout" basis to determine whether the rpm requirements of the chopper were compatible with plaintiff's tractor power takeoff capacity. The Supreme Court held it was inconsistent for the lower court to proceed from that finding and conclude, as a matter of law, that defendant was liable based on breach of implied warranty of fitness, negligent misrepresentation, and constructive fraud. As to liability for breach of warranty, the claim would lie only after acceptance of goods. In this case, a finding of taking goods on a "tryout" basis was contradictory to the acceptance requirement. Because acceptance was critical to the outcome of that cause of action and the other causes of action, the conflicting findings and conclusions constituted error. Nelson v. Davis Modern Mach., 220 M 347, 715 P2d 1052, 43 St. Rep. 423 (1986).

Acceptance of Nonconforming Goods — Recovery of Damages Not Precluded — Notice: Respondent Meland received building materials on July 7, 1981. About 10 days later, he began assembling the building and discovered that the materials did not conform to the contract terms, at which time he immediately notified appellant Intermountain of the problem. He then proceeded with construction, using the component parts to produce a building height he desired. Under 30-2-606(1)(c), acceptance of goods occurs when the buyer does any act inconsistent with the seller's ownership. Meland's use of the delivered goods to construct a building was inconsistent with Intermountain's ownership and constituted acceptance. Intermountain argued that once there is acceptance no damages may be had. The Supreme Court ruled that under 30-2-607(2) acceptance precludes rejection of the goods or revocation if made with the knowledge of the nonconformity unless there is a reasonable assumption that the nonconformity may be reasonably cured, but does not preclude recovery for damages due. When a buyer has accepted goods and given notification, he may recover damages for any nonconformity under 30-2-714(1). Section 30-2-607(3) requires that the buyer must notify the seller within a reasonable time after he discovers any breach. In this case, notice was sufficient and the award of damages was affirmed. Meland v. Intermtn. Sys., Inc., 219 M 242, 712 P2d 1295, 42 St. Rep. 1987 (1985).

Sufficient Rejection of Nonconforming Goods: Plaintiff sold defendants an irrigation system and pump. Plaintiff substituted a different type of pump for the one ordered by defendants. Plaintiff and his supplier installed the system, and defendants paid for everything but the pump and its installation. Plaintiff and his supplier supervised the digging of the sump for the installation of the pump but did not test it. The pump became clogged before any water ever came out of it. The supplier cleaned the pump and had an agent reinstall it. Defendants tried unsuccessfully to get the system to work and called plaintiff to complain several times. Defendants finally told plaintiff to come and get the pump and refused to pay for it. They later purchased a different pump which operated the system properly. Plaintiff sued for the price of the pump and installation costs. The District Court entered judgment for the defendants. Plaintiff contends that the District Court's findings of fact and conclusions of law were insufficient in failing to adequately address the provisions of the U.C.C. governing rejection of nonconforming goods. The Supreme Court found that although the findings and conclusions could have been better, there was substantial evidence to support the conclusions that: (1) the goods were nonconforming; (2) there was a failure to cure the defects of the pump; and (3) the use of the pump was in fact a prolonged effort to determine why the pump failed to work and to cure the defect, and as such was not an act inconsistent with the seller's ownership. There was no acceptance by the defendants, no use inconsistent with the ownership of the plaintiff, and no delay in offering the return of the nonconforming pump significant enough to justify a conclusion that defendants had accepted the pump. Steinmetz v. Robertus, 196 M 311, 637 P2d 31, 38 St. Rep. 2067 (1981).

Modular Home — Applicable Warranty Law: Sale of modular home manufactured at defendant's plant and delivered to plaintiffs' building site was governed by the U.C.C. warranty provisions and not the warranty provisions of Title 30, ch. 11, part 2, which are made inapplicable by 30-11-224. The fact that defendant had charge of the home until after it was affixed to plaintiffs' foundation and no longer had mobility did not affect the applicability of the U.C.C. warranty provisions, for the home was manufactured to plaintiffs' specifications, was thus identified to the contract under the U.C.C. at the time of the first step of its production, was movable at that time, and thus was "goods" the sale of which the U.C.C. applied. Little v. Grizzly Mfg., 195 M 419, 636 P2d 839, 38 St. Rep. 1994 (1981).

Delivery Versus Acceptance: The Supreme Court rejected defendant's contention that Montana Seeds, Inc., failed to establish its claim for goods "sold and delivered" by not proving actual delivery. The determining factor was whether defendant "accepted" the goods. Here there were two shipments. Only the second shipment's acceptance was challenged by defendant based on his contention that it was misdelivered. However, defendant bore the risk of loss because he did not specify a particular destination. His cause of action for misdelivery was against the carrier. Mont. Seeds, Inc. v. Holliday, 178 M 119, 582 P2d 1223 (1978). See also Konitz v. Claver, 1998 MT 27, 287 M 301, 954 P2d 1138, 55 St. Rep. 95 (1998).

30-2-607. Effect of acceptance — notice of breach — burden of establishing breach after acceptance — notice of claim or litigation to person answerable over.

Official Comment

Prior Uniform Statutory Provision: Subsection (1)—Section 41, Uniform Sales Act; Subsections (2) and (3)—Sections 49 and 69, Uniform Sales Act.

Changes: Rewritten.

Purposes of Changes: To continue the prior basic policies with respect to acceptance of goods while making a number of minor though material changes in the interest of simplicity and commercial convenience so that:

1. Under subsection (1), once the buyer accepts a tender the seller acquires a right to its price on the contract terms. In cases of partial acceptance, the price of any part accepted is, if possible, to be reasonably apportioned, using the type of apportionment familiar to the courts in quantum valebat cases, to be determined in terms of "the contract rate," which is the rate determined from the bargain in fact (the agreement) after the rules and policies of this Chapter have been brought to bear.

2. Under subsection (2) acceptance of goods precludes their subsequent rejection. Any return of the goods thereafter must be by way of revocation of acceptance under the next section. Revocation is unavailable for a non-conformity known to the buyer at the time of acceptance, except where the buyer has accepted on the reasonable assumption that the non-conformity would be seasonably cured.

3. All other remedies of the buyer remain unimpaired under subsection (2). This is intended to include the buyer's full rights with respect to future installments despite his acceptance of any earlier non-conforming installment.

4. The time of notification is to be determined by applying commercial standards to a merchant buyer. "A reasonable time" for notification from a retail consumer is to be judged by different standards so that in his case it will be extended, for the rule of requiring notification is designed to defeat commercial bad faith, not to deprive a good faith consumer of his remedy.

The content of the notification need merely be sufficient to let the seller know that the transaction is still troublesome and must be watched. There is no reason to require that the notification which saves the buyer's rights under this section must include a clear statement of all the objections that will be relied on by the buyer, as under the section covering statements of defects upon rejection (Section 30-2-605). Nor is there reason for requiring the notification to be a claim for damages or of any threatened litigation or other resort to a remedy. The notification which saves the buyer's rights under this Chapter need only be such as informs the seller that the transaction is claimed to involve a breach, and thus opens the way for normal settlement through negotiation.

5. Under this Chapter various beneficiaries are given rights for injuries sustained by them because of the seller's breach of warranty. Such a beneficiary does not fall within the reason of the present section in regard to discovery of defects and the giving of notice within a reasonable time after acceptance, since he has nothing to do with acceptance. However, the reason of this section does extend to requiring the beneficiary to notify the seller that an injury has occurred. What is said above, with regard to the extended time for reasonable notification from the lay consumer after the injury is also applicable here; but even a beneficiary can be properly held to the use of good faith in notifying, once he has had time to become aware of the legal situation.

6. Subsection (4) unambiguously places the burden of proof to establish breach on the buyer after acceptance. However, this rule becomes one purely of procedure when the tender accepted was non-conforming and the buyer has given the seller notice of breach under subsection (3). For subsection (2) makes it clear that acceptance leaves unimpaired the buyer's right to be made whole, and that right can be exercised by the buyer not only by way of cross-claim for damages, but also by way of recoupment in diminution or extinction of the price.

7. Subsections (3)(b) and (5)(b) give a warrantor against infringement an opportunity to defend or compromise third-party claims or be relieved of his liability. Subsection (5)(a) codifies for all warranties the practice of voucher to defend. Compare Section 30-3-803 [now repealed]. Subsection (6) makes these provisions applicable to the buyer's liability for infringement under Section 30-2-312.

8. All of the provisions of the present section are subject to any explicit reservation of rights.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

Case Notes

Failure to Notify Seller of Nonconformity of Goods — Damages Unwarranted: Defendants claimed that a jury instruction should have been given regarding damages owing under the Uniform Commercial Code for a sale of nonconforming goods. However, defendants did not reject the goods upon delivery or notify the seller within a reasonable time regarding the nonconformity. Because no damages were owing, an instruction on the measure of damages was not appropriate. NW. Truck & Trailer Sales, Inc. v. Dvorak, 269 M 150, 887 P2d 260, 51 St. Rep. 1530 (1994).

Acceptance of Nonconforming Goods — Recovery of Damages Not Precluded — Notice: Respondent Meland received building materials on July 7, 1981. About 10 days later, he began assembling the building and discovered that the materials did not conform to the contract terms, at which time he immediately notified appellant Intermountain of the problem. He then proceeded with construction, using the component parts to produce a building height he desired. Under 30-2-606(1)(c), acceptance of goods occurs when the buyer does any act inconsistent with the seller's ownership. Meland's use of the delivered goods to construct a building was inconsistent with Intermountain's ownership and constituted acceptance. Intermountain argued that once there is acceptance no damages may be had. The Supreme Court ruled that under 30-2-607(2) acceptance precludes rejection of the goods or revocation if made with the knowledge of the nonconformity unless there is a reasonable assumption that the nonconformity may be reasonably cured, but does not preclude recovery for damages due. When a buyer has accepted goods and given notification, he may recover damages for any nonconformity under 30-2-714(1). Section 30-2-607(3) requires that the buyer must notify the seller within a reasonable time after he discovers any breach. In this case, notice was sufficient and the award of damages was affirmed. Meland v. Intermtn. Sys., Inc., 219 M 242, 712 P2d 1295, 42 St. Rep. 1987 (1985).

Reliance on Expertise — Implied Warranty of Fitness for Particular Purpose: Defendant relied on plaintiff's expertise to select an affordable fire alarm system that would provide reliable protection for the hotel's property and guests. Where the seller is aware that the buyer is relying upon the seller's judgment to select suitable goods, an implied warranty that the goods are fit for that particular purpose is created. The system installed was complicated, difficult to use, and frequently malfunctioned. Defendant advised plaintiff of the failure of the system after a fire in the snack bar, which was prior to the fire in a guest room that eventually resulted in this action. Plaintiff's own records showed repeated notifications of problems with the system. This was reasonable notice under 30-2-607(3). The implied warranty of fitness for a particular purpose was breached, and defendant was entitled to recover loss in value of the goods plus consequential and incidental damages. Fire Supply & Serv., Inc. v. Chico Hot Springs, 196 M 435, 639 P2d 1160, 39 St. Rep. 231 (1982).

Modular Home — Applicable Warranty Law: Sale of modular home manufactured at defendant's plant and delivered to plaintiffs' building site was governed by the U.C.C. warranty provisions and not the warranty provisions of Title 30, ch. 11, part 2, which are made inapplicable by 30-11-224. The fact that defendant had charge of the home until after it was affixed to plaintiffs' foundation and no longer had mobility did not affect the applicability of the U.C.C. warranty provisions, for the home was manufactured to plaintiffs' specifications, was thus identified to the contract under the U.C.C. at the time of the first step of its production, was movable at that time, and thus was "goods" the sale of which the U.C.C. applied. Little v. Grizzly Mfg., 195 M 419, 636 P2d 839, 38 St. Rep. 1994 (1981).

Timeliness of Notice of Breach: In action to recover for breach of warranty of semen sold to cattle rancher by artificial insemination service, buyer gave timely notice of breach of warranty by informing seller of calf crop failure 10 months after artificial insemination process. Waddell v. Am. Breeders Serv., Inc., 161 M 221, 505 P2d 417, 61 ALR 3d 801 (1973).

30-2-608. Revocation of acceptance in whole or in part.

Official Comment

Prior Uniform Statutory Provision: Section 69(1)(d), (3), (4) and (5), Uniform Sales Act.

Changes: Rewritten.

Purposes of Changes: To make it clear that:

1. Although the prior basic policy is continued, the buyer is no longer required to elect between revocation of acceptance and recovery of damages for breach. Both are now available to him. The non-alternative character of the two remedies is stressed by the terms used in the present section. The section no longer speaks of "rescission," a term capable of ambiguous application either to transfer of title to the goods or to the contract of sale and susceptible also of confusion with cancellation for cause of an executed or executory portion of the contract. The

remedy under this section is instead referred to simply as "revocation of acceptance" of goods tendered under a contract for sale and involves no suggestion of "election" of any sort.

2. Revocation of acceptance is possible only where the non-conformity substantially impairs the value of the goods to the buyer. For this purpose the test is not what the seller had reason to know at the time of contracting; the question is whether the non-conformity is such as will in fact cause a substantial impairment of value to the buyer though the seller had no advance knowledge as to the buyer's particular circumstances.

3. "Assurances" by the seller under paragraph (b) of subsection (1) can rest as well in the circumstances or in the contract as in explicit language used at the time of delivery. The reason for recognizing such assurances is that they induce the buyer to delay discovery. These are the only assurances involved in paragraph (b). Explicit assurances may be made either in good faith or bad faith. In either case any remedy accorded by this Chapter is available to the buyer under the section on remedies for fraud.

4. Subsection (2) requires notification of revocation of acceptance within a reasonable time after discovery of the grounds for such revocation. Since this remedy will be generally resorted to only after attempts at adjustment have failed, the reasonable time period should extend in most cases beyond the time in which notification of breach must be given, beyond the time for discovery of non-conformity after acceptance and beyond the time for rejection after tender. The parties may by their agreement limit the time for notification under this section, but the same sanctions and considerations apply to such agreements as are discussed in the comment on manner and effect of rightful rejection.

5. The content of the notice under subsection (2) is to be determined in this case as in others by considerations of good faith, prevention of surprise, and reasonable adjustment. More will generally be necessary than the mere notification of breach required under the preceding section. On the other hand the requirements of the section on waiver of buyer's objections do not apply here. The fact that quick notification of trouble is desirable affords good ground for being slow to bind a buyer by his first statement. Following the general policy of this Chapter, the requirements of the content of notification are less stringent in the case of a non-merchant buyer.

6. Under subsection (2) the prior policy is continued of seeking substantial justice in regard to the condition of goods restored to the seller. Thus the buyer may not revoke his acceptance if the goods have materially deteriorated except by reason of their own defects. Worthless goods, however, need not be offered back and minor defects in the articles reoffered are to be disregarded.

7. The policy of the section allowing partial acceptance is carried over into the present section and the buyer may revoke his acceptance, in appropriate cases, as to the entire lot or any commercial unit thereof.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

30-2-609. Right to adequate assurance of performance.

Official Comment

Prior Uniform Statutory Provision: See Sections 53, 54(1)(b), 55 and 63(2), Uniform Sales Act.

Purposes:

1. The section rests on the recognition of the fact that the essential purpose of a contract between commercial men is actual performance and they do not bargain merely for a promise, or for a promise plus the right to win a lawsuit and that a continuing sense of reliance and security that the promised performance will be forthcoming when due, is an important feature of the bargain. If either the willingness or the ability of a party to perform declines materially between the time of contracting and the time for performance, the other party is threatened with the loss of a substantial part of what he has bargained for. A seller needs protection not merely against having to deliver on credit to a shaky buyer, but also against having to procure and manufacture the goods, perhaps turning down other customers. Once he has been given reason to believe that the buyer's performance has become uncertain, it is an undue hardship to force him to continue his own performance. Similarly, a buyer who believes that the seller's deliveries have become uncertain cannot safely wait for the due date of performance when he has been buying to assure himself of materials for his current manufacturing or to replenish his stock of merchandise.

2. Three measures have been adopted to meet the needs of commercial men in such situations. First, the aggrieved party is permitted to suspend his own performance and any preparation therefor, with excuse for any resulting necessary delay, until the situation has been clarified. "Suspend performance" under this section means to hold up performance pending the

outcome of the demand, and includes also the holding up of any preparatory action. This is the same principle which governs the ancient law of stoppage and seller's lien, and also of excuse of a buyer from prepayment if the seller's actions manifest that he cannot or will not perform. (Original Act, Section 63(2).)

Secondly, the aggrieved party is given the right to require adequate assurance that the other party's performance will be duly forthcoming. This principle is reflected in the familiar clauses permitting the seller to curtail deliveries if the buyer's credit becomes impaired, which when held within the limits of reasonableness and good faith actually express no more than the fair business meaning of any commercial contract.

Third, and finally, this section provides the means by which the aggrieved party may treat the contract as broken if his reasonable grounds for insecurity are not cleared up within a reasonable time. This is the principle underlying the law of anticipatory breach, whether by way of defective part performance or by repudiation. The present section merges these three principles of law and commercial practice into a single theory of general application to all sales agreements looking to future performance.

3. Subsection (2) of the present section requires that "reasonable" grounds and "adequate" assurance as used in subsection (1) be defined by commercial rather than legal standards. The express reference to commercial standards carries no connotation that the obligation of good faith is not equally applicable here.

Under commercial standards and in accord with commercial practice, a ground for insecurity need not arise from or be directly related to the contract in question. The law as to "dependence" or "independence" of promises within a single contract does not control the application of the present section.

Thus a buyer who falls behind in "his account" with the seller, even though the items involved have to do with separate and legally distinct contracts, impairs the seller's expectation of due performance. Again, under the same test, a buyer who requires precision parts which he intends to use immediately upon delivery, may have reasonable grounds for insecurity if he discovers that his seller is making defective deliveries of such parts to other buyers with similar needs. Thus, too, in a situation such as arose in Jay Dreher Corporation v. Delco Appliance Corporation, 93 F.2d 275 (C.C.A.2, 1937), where a manufacturer gave a dealer an exclusive franchise for the sale of his product but on two or three occasions breached the exclusive dealing clause, although there was no default in orders, deliveries or payments under the separate sales contract between the parties, the aggrieved dealer would be entitled to suspend his performance of the contract for sale under the present section and to demand assurance that the exclusive dealing contract would be lived up to. There is no need for an explicit clause tying the exclusive franchise into the contract for the sale of goods since the situation itself ties the agreements together.

The nature of the sales contract enters also into the question of reasonableness. For example, a report from an apparently trustworthy source that the seller had shipped defective goods or was planning to ship them would normally give the buyer reasonable grounds for insecurity. But when the buyer has assumed the risk of payment before inspection of the goods, as in a sales contract on C.I.F. or similar cash against documents terms, that risk is not to be evaded by a demand for assurance. Therefore no ground for insecurity would exist under this section unless the report went to a ground which would excuse payment by the buyer.

4. What constitutes "adequate" assurance of due performance is subject to the same test of factual conditions. For example, where the buyer can make use of a defective delivery, a mere promise by a seller of good repute that he is giving the matter his attention and that the defect will not be repeated, is normally sufficient. Under the same circumstances, however, a similar statement by a known corner-cutter might well be considered insufficient without the posting of a guaranty or, if so demanded by the buyer, a speedy replacement of the delivery involved. By the same token where a delivery has defects, even though easily curable, which interfere with easy use by the buyer, no verbal assurance can be deemed adequate which is not accompanied by replacement, repair, money-allowance, or other commercially reasonable cure.

A fact situation such as arose in Corn Products Refining Co. v. Fasola, 94 N.J.L. 181, 109 A. 505 (1920) offers illustration both of reasonable grounds for insecurity and "adequate" assurance. In that case a contract for the sale of oils on 30 days' credit, 2% off for payment within 10 days, provided that credit was to be extended to the buyer only if his financial responsibility was satisfactory to the seller. The buyer had been in the habit of taking advantage of the discount but at the same time that he failed to make his customary 10 day payment, the seller heard rumors, in fact false, that the buyer's financial condition was shaky. Thereupon, the seller demanded cash before shipment or security satisfactory to him. The buyer sent a good credit report from his banker, expressed willingness to make payments when due on the 30 day terms and insisted on further deliveries under the contract. Under this Chapter the rumors, although false, were enough to make the buyer's financial condition "unsatisfactory" to the seller under the contract clause. Moreover, the buyer's practice of taking the cash discounts is enough, apart from the contract clause, to lay a commercial foundation for suspicion when the practice is suddenly stopped. These matters, however, go only to the justification of the seller's demand for security, or his "reasonable grounds for insecurity".

The adequacy of the assurance given is not measured as in the type of "satisfaction" situation affected with intangibles, such as in personal service cases, cases involving a third party's judgment as final, or cases in which the whole contract is dependent on one party's satisfaction, as in a sale on approval. Here, the seller must exercise good faith and observe commercial standards. This Chapter thus approves the statement of the court in James B. Berry's Sons Co. of Illinois v. Monark Gasoline & Oil Co., Inc., 32 F.2d 74 (C.C.A.8, 1929), that the seller's satisfaction under such a clause must be based upon reason and must not be arbitrary or capricious; and rejects the purely personal "good faith" test of the Corn Products Refining Co. case, which held that in the seller's sole judgment, if for *any* reason he was dissatisfied, he was entitled to revoke the credit. In the absence of the buyer's failure to take the 2% discount as was his custom, the banker's report given in that case would have been "adequate" assurance under this Act, regardless of the language of the "satisfaction" clause. However, the seller is reasonably entitled to feel insecure at a sudden expansion of the buyer's use of a credit term, and should be entitled either to security or to a satisfactory explanation.

The entire foregoing discussion as to adequacy of assurance by way of explanation is subject to qualification when repeated occasions for the application of this section arise. This Act recognizes that repeated delinquencies must be viewed as cumulative. On the other hand, commercial sense also requires that if repeated claims for assurance are made under this section, the basis for these claims must be increasingly obvious.

5. A failure to provide adequate assurance of performance and thereby to re-establish the security of expectation, results in a breach only "by repudiation" under subsection (4). Therefore, the possibility is continued of retraction of the repudiation under the section dealing with that problem, unless the aggrieved party has acted on the breach in some manner.

The thirty day limit on the time to provide assurance is laid down to free the question of reasonable time from uncertainty in later litigation.

6. Clauses seeking to give the protected party exceedingly wide powers to cancel or readjust the contract when ground for insecurity arises must be read against the fact that good faith is a part of the obligation of the contract and not subject to modification by agreement and includes, in the case of a merchant, the reasonable observance of commercial standards of fair dealing in the trade. Such clauses can thus be effective to enlarge the protection given by the present section to a certain extent, to fix the reasonable time within which requested assurance must be given, or to define adequacy of the assurance in any commercially reasonable fashion. But any clause seeking to set up arbitrary standards for action is ineffective under this Chapter. Acceleration clauses are treated similarly in the Chapters on Commercial Paper and Secured Transactions.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

30-2-610. Anticipatory repudiation.

Official Comment

Prior Uniform Statutory Provision: See Sections 63(2) and 65, Uniform Sales Act.

Purposes: To make it clear that:

1. With the problem of insecurity taken care of by the preceding section and with provision being made in this Chapter as to the effect of a defective delivery under an installment contract, anticipatory repudiation centers upon an overt communication of intention or an action which renders performance impossible or demonstrates a clear determination not to continue with performance.

Under the present section when such a repudiation substantially impairs the value of the contract, the aggrieved party may at any time resort to his remedies for breach, or he may suspend his own performance while he negotiates with, or awaits performance by, the other party. But if he awaits performance beyond a commercially reasonable time he cannot recover resulting damages which he should have avoided.

2. It is not necessary for repudiation that performance be made literally and utterly impossible. Repudiation can result from action which reasonably indicates a rejection of the continuing obligation. And, a repudiation automatically results under the preceding section on insecurity when a party fails to provide adequate assurance of due future performance within thirty days after a justifiable demand therefor has been made. Under the language of this section, a demand by one or both parties for more than the contract calls for in the way of counter-performance is not in itself a repudiation nor does it invalidate a plain expression of desire for future performance. However, when under a fair reading it amounts to a statement of intention not to perform except on conditions which go beyond the contract, it becomes a repudiation.

3. The test chosen to justify an aggrieved party's action under this section is the same as that in the section on breach in installment contracts — namely the substantial value of the contract. The most useful test of substantial value is to determine whether material inconvenience or injustice will result if the aggrieved party is forced to wait and receive an ultimate tender minus the part or aspect repudiated.

4. After repudiation, the aggrieved party may immediately resort to any remedy he chooses provided he moves in good faith (see Section 30-1-203). Inaction and silence by the aggrieved party may leave the matter open but it cannot be regarded as misleading the repudiating party. Therefore the aggrieved party is left free to proceed at any time with his options under this section, unless he has taken some positive action which in good faith requires notification to the other party before the remedy is pursued.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Oral Contract for Sale of Grain — Near Three-Month Delay Before Cancellation of Contract Commercially Reasonable Time — Contract Enforced: When a grain elevator manager became aware of a seller's failure to deliver grain under an oral contract, the elevator's regional office sent the seller a letter urging performance and setting a deadline for cancellation of the contract if performance was not made. The Supreme Court upheld the jury's finding that the deadline was a commercially reasonable time before considering the contract breached and that General Mills was entitled to price out the contract at the market price for the grain on the deadline date, not the earlier date on which General Mills became aware that the seller would not perform and when grain prices were lower. Smith v. Gen. Mills, Inc., 1998 MT 280, 291 M 426, 968 P2d 723, 55 St. Rep. 1151 (1998).

30-2-611. Retraction of anticipatory repudiation.

Official Comment

Prior Uniform Statutory Provision: None.

Purposes: To make it clear that:

1. The repudiating party's right to reinstate the contract is entirely dependent upon the action taken by the aggrieved party. If the latter has cancelled the contract or materially changed his position at any time after the repudiation, there can be no retraction under this section.

2. Under subsection (2) an effective retraction must be accompanied by any assurances demanded under the section dealing with right to adequate assurance. A repudiation is of course sufficient to give reasonable ground for insecurity and to warrant a request for assurance as an essential condition of the retraction. However, after a timely and unambiguous expression of retraction, a reasonable time for the assurance to be worked out should be allowed by the aggrieved party before cancellation.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-2-612. "Installment contract" — breach.

Official Comment

Prior Uniform Statutory Provision: Section 45(2), Uniform Sales Act.

Changes: Rewritten.

Purposes of Changes: To continue prior law but to make explicit the more mercantile interpretation of many of the rules involved, so that:

1. The definition of an installment contract is phrased more broadly in this Chapter so as to cover installment deliveries tacitly authorized by the circumstances or by the option of either party.

2. In regard to the apportionment of the price for separate payment this Chapter applies the more liberal test of what can be apportioned rather than the test of what is clearly apportioned by the agreement. This Chapter also recognizes approximate calculation or apportionment of price subject to subsequent adjustment. A provision for separate payment for each lot delivered ordinarily means that the price is at least roughly calculable by units of quantity, but such a provision is not essential to an "installment contract." If separate acceptance of separate deliveries is contemplated, no generalized contrast between wholly "entire" and wholly "divisible" contracts has any standing under this Chapter.

3. This Chapter rejects any approach which gives clauses such as "each delivery is a separate contract" their legalistically literal effect. Such contracts nonetheless call for installment deliveries. Even where a clause speaks of "a separate contract for all purposes", a commercial reading of the language under the section on good faith and commercial standards requires that the singleness of the document and the negotiation, together with the sense of the situation, prevail over any uncommercial and legalistic interpretation.

4. One of the requirements for rejection under subsection (2) is non-conformity substantially impairing the value of the installment in question. However, an installment agreement may require accurate conformity in quality as a condition to the right to acceptance if the need for such conformity is made clear either by express provision or by the circumstances. In such a case the effect of the agreement is to define explicitly what amounts to substantial impairment of value impossible to cure. A clause requiring accurate compliance as a condition to the right to acceptance must, however, have some basis in reason, must avoid imposing hardship by surprise and is subject to waiver or to displacement by practical construction.

Substantial impairment of the value of an installment can turn not only on the quality of the goods but also on such factors as time, quantity, assortment, and the like. It must be judged in terms of the normal or specifically known purposes of the contract. The defect in required documents refers to such matters as the absence of insurance documents under a C.I.F. contract, falsity of a bill of lading, or one failing to show shipment within the contract period or to the contract destination. Even in such cases, however, the provisions on cure of tender apply if appropriate documents are readily procurable.

5. Under subsection (2) an installment delivery must be accepted if the non-conformity is curable and the seller gives adequate assurance of cure. Cure of non-conformity of an installment in the first instance can usually be afforded by an allowance against the price, or in the case of reasonable discrepancies in quantity either by a further delivery or a partial rejection. This Chapter requires reasonable action by a buyer in regard to discrepant delivery and good faith requires that the buyer make any reasonable minor outlay of time or money necessary to cure an overshipment by severing out an acceptable percentage thereof. The seller must take over a cure which involves any material burden; the buyer's obligation reaches only to cooperation. Adequate assurance for purposes of subsection (2) is measured by the same standards as under the section on right to adequate assurance of performance.

6. Subsection (3) is designed to further the continuance of the contract in the absence of an overt cancellation. The question arising when an action is brought as to a single installment only is resolved by making such action waive the right of cancellation. This involves merely a defect in one or more installments, as contrasted with the situation where there is a true repudiation within the section on anticipatory repudiation. Whether the non-conformity in any given installment justifies cancellation as to the future depends, not on whether such non-conformity indicates an intent or likelihood that the future deliveries will also be defective, but whether the non-conformity substantially impairs the value of the whole contract. If only the seller's security in regard to future installments is impaired, he has the right to demand adequate assurances of proper future performance but has not an immediate right to cancel the entire contract. It is clear under this Chapter, however, that defects in prior installments are cumulative in effect, so that acceptance does not wash out the defect "waived." Prior policy is continued, putting the rule as to buyer's default on the same footing as that in regard to seller's default.

7. Under the requirement of seasonable notification of cancellation under subsection (3), a buyer who accepts a non-conforming installment which substantially impairs the value of the entire contract should properly be permitted to withhold his decision as to whether or not to cancel pending a response from the seller as to his claim for cure or adjustment. Similarly, a seller may withhold a delivery pending payment for prior ones, at the same time delaying his decision as to cancellation. A reasonable time for notifying of cancellation, judged by commercial standards under the section on good faith, extends of course to include the time covered by any

reasonable negotiation in good faith. However, during this period the defaulting party is entitled, on request, to know whether the contract is still in effect, before he can be required to perform further.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

30-2-613. Casualty to identified goods.

Official Comment

Prior Uniform Statutory Provision: Sections 7 and 8, Uniform Sales Act.

Changes: Rewritten, the basic policy being continued but the test of a "divisible" or "indivisible" sale or contract being abandoned in favor of adjustment in business terms.

Purposes of Changes:

1. Where goods whose continued existence is presupposed by the agreement are destroyed without fault of either party, the buyer is relieved from his obligation but may at his option take the surviving goods at a fair adjustment. "Fault" is intended to include negligence and not merely wilful wrong. The buyer is expressly given the right to inspect the goods in order to determine whether he wishes to avoid the contract entirely or to take the goods with a price adjustment.

2. The section applies whether the goods were already destroyed at the time of contracting without the knowledge of either party or whether they are destroyed subsequently but before the risk of loss passes to the buyer. Where under the agreement, including of course usage of trade, the risk has passed to the buyer before the casualty, the section has no application. Beyond this, the essential question in determining whether the rules of this section are to be applied is whether the seller has or has not undertaken the responsibility for the continued existence of the goods in proper condition through the time of agreed or expected delivery.

3. The section on the term "no arrival, no sale" makes clear that delay in arrival, quite as much as physical change in the goods, gives the buyer the options set forth in this section.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

30-2-614. Substituted performance.

Official Comment

Prior Uniform Statutory Provision: None.

Purposes:

1. Subsection (1) requires the tender of a commercially reasonable substituted performance where agreed to facilities have failed or become commercially impracticable. Under this Chapter, in the absence of specific agreement, the normal or usual facilities enter into the agreement either through the circumstances, usage of trade or prior course of dealing.

This section appears between Section 30-2-613 on casualty to identified goods and the next section on excuse by failure of presupposed conditions, both of which deal with excuse and complete avoidance of the contract where the occurrence or non-occurrence of a contingency which was a basic assumption of the contract makes the expected performance impossible. The distinction between the present section and those sections lies in whether the failure or impossibility of performance arises in connection with an incidental matter or goes to the very heart of the agreement. The differing lines of solution are contrasted in a comparison of International Paper Co. v. Rockefeller, 161 App. Div. 180, 146 N.Y.S. 371 (1914) and Meyer v. Sullivan, 40 Cal. App. 723, 181 P. 847 (1919). In the former case a contract for the sale of spruce to be cut from a particular tract of land was involved. When a fire destroyed the trees growing on that tract the seller was held excused since performance was impossible. In the latter case the contract called for delivery of wheat "f.o.b. Kosmos Steamer at Seattle." The war led to cancellation of that line's sailing schedule after space had been duly engaged and the buyer was held entitled to demand substituted delivery at the warehouse on the line's loading dock. Under this Chapter, of course, the seller would also be entitled, had the market gone the other way, to make a substituted tender in that manner.

There must, however, be a true commercial impracticability to excuse the agreed to performance and justify a substituted performance. When this is the case a reasonable substituted performance tendered by either party should excuse him from strict compliance with contract terms which do not go to the essence of the agreement.

2. The substitution provided in this section as between buyer and seller does not carry over into the obligation of a financing agency under a letter of credit, since such an agency is entitled to performance which is plainly adequate on its face and without need to look into commercial evidence outside of the documents. See Chapter 5, especially Sections 30-5-102, 30-5-103, 30-5-109, 30-5-110, 30-5-114 [all repealed, see 30-5-122 and 30-5-124].

3. Under subsection (2) where the contract is still executory on both sides, the seller is permitted to withdraw unless the buyer can provide him with a commercially equivalent return despite the governmental regulation. Where, however, only the debt for the price remains, a larger leeway is permitted. The buyer may pay in the manner provided by the regulation even though this may not be commercially equivalent provided that the regulation is not "discriminatory, oppressive or predatory."

30-2-615. Excuse by failure of presupposed conditions.

Official Comment

Prior Uniform Statutory Provision: None.

Purposes:

1. This section excuses a seller from timely delivery of goods contracted for, where his performance has become commercially impracticable because of unforeseen supervening circumstances not within the contemplation of the parties at the time of contracting. The destruction of specific goods and the problem of the use of substituted performance on points other than delay or quantity, treated elsewhere in this Chapter, must be distinguished from the matter covered by this section.

2. The present section deliberately refrains from any effort at an exhaustive expression of contingencies and is to be interpreted in all cases sought to be brought within its scope in terms of its underlying reason and purpose.

3. The first test for excuse under this Chapter in terms of basic assumption is a familiar one. The additional test of commercial impracticability (as contrasted with "impossibility," "frustration of performance" or "frustration of the venture") has been adopted in order to call attention to the commercial character of the criterion chosen by this Chapter.

4. Increased cost alone does not excuse performance unless the rise in cost is due to some unforeseen contingency which alters the essential nature of the performance. Neither is a rise or a collapse in the market in itself a justification, for that is exactly the type of business risk which business contracts made at fixed prices are intended to cover. But a severe shortage of raw materials or of supplies due to a contingency such as war, embargo, local crop failure, unforeseen shutdown of major sources of supply or the like, which either causes a marked increase in cost or altogether prevents the seller from securing supplies necessary to his performance, is within the contemplation of this section. (See Ford & Sons, Ltd., v. Henry Leetham & Sons, Ltd., 21 Com. Cas. 55 (1915, K.B.D.).)

5. Where a particular source of supply is exclusive under the agreement and fails through casualty, the present section applies rather than the provision on destruction or deterioration of specific goods. The same holds true where a particular source of supply is shown by the circumstances to have been contemplated or assumed by the parties at the time of contracting. (See Davis Co. v. Hoffmann-LaRoche Chemical Works, 178 App.Div. 855, 166 N.Y.S. 179 (1917) and International Paper Co. v. Rockefeller, 161 App.Div. 180, 146 N.Y.S. 371 (1914).) There is no excuse under this section, however, unless the seller has employed all due measures to assure himself that his source will not fail. (See Canadian Industrial Alcohol Co., Ltd., v. Dunbar Molasses Co., 258 N.Y. 194, 179 N.E. 383, 80 A.L.R. 1173 (1932) and Washington Mfg. Co. v. Midland Lumber Co., 113 Wash. 593, 194 P. 777 (1921).)

In the case of failure of production by an agreed source for causes beyond the seller's control, the seller should, if possible, be excused since production by an agreed source is without more a basic assumption of the contract. Such excuse should not result in relieving the defaulting supplier from liability nor in dropping into the seller's lap an unearned bonus of damages over. The flexible adjustment machinery of this Chapter provides the solution under the provision on the obligation of good faith. A condition to his making good the claim of excuse is the turning over to the buyer of his rights against the defaulting source of supply to the extent of the buyer's contract in relation to which excuse is being claimed.

6. In situations in which neither sense nor justice is served by either answer when the issue is posed in flat terms of "excuse" or "no excuse," adjustment under the various provisions of this Chapter is necessary, especially the sections on good faith, on insecurity and assurance and on

the reading of all provisions in the light of their purposes, and the general policy of this Act to use equitable principles in furtherance of commercial standards and good faith.

7. The failure of conditions which go to convenience or collateral values rather than to the commercial practicability of the main performance does not amount to a complete excuse. However, good faith and the reason of the present section and of the preceding one may properly be held to justify and even to require any needed delay involved in a good faith inquiry seeking a readjustment of the contract terms to meet the new conditions.

8. The provisions of this section are made subject to assumption of greater liability by agreement and such agreement is to be found not only in the expressed terms of the contract but in the circumstances surrounding the contracting, in trade usage and the like. Thus the exemptions of this section do not apply when the contingency in question is sufficiently foreshadowed at the time of contracting to be included among the business risks which are fairly to be regarded as part of the dickered terms, either consciously or as a matter of reasonable, commercial interpretation from the circumstances. (See Madeirense Do Brasil, S. A. v. Stulman-Emrick Lumber Co., 147 F.2d 399 (C.C.A., 2 Cir., 1945).) The exemption otherwise present through usage of trade under the present section may also be expressly negated by the language of the agreement. Generally, express agreements as to exemptions designed to enlarge upon or supplant the provisions of this section are to be read in the light of mercantile sense and reason, for this section itself sets up the commercial standard for normal and reasonable interpretation and provides a minimum beyond which agreement may not go.

Agreement can also be made in regard to the consequences of exemption as laid down in paragraphs (b) and (c) and the next section on procedure on notice claiming excuse.

9. The case of a farmer who has contracted to sell crops to be grown on designated land may be regarded as falling either within the section on casualty to identified goods or this section, and he may be excused, when there is a failure of the specific crop, either on the basis of the destruction of identified goods or because of the failure of a basic assumption of the contract.

Exemption of the buyer in the case of a "requirements" contract is covered by the "Output and Requirements" section both as to assumption and allocation of the relevant risks. But when a contract by a manufacturer to buy fuel or raw material makes no specific reference to a particular venture and no such reference may be drawn from the circumstances, commercial understanding views it as a general deal in the general market and not conditioned on any assumption of the continuing operation of the buyer's plant. Even when notice is given by the buyer that the supplies are needed to fill a specific contract of a normal commercial kind, commercial understanding does not see such a supply contract as conditioned on the continuance of the buyer's further contract for outlet. On the other hand, where the buyer's contract is in reasonable commercial understanding conditioned on a definite and specific venture or assumption as, for instance, a war procurement subcontract known to be based on a prime contract which is subject to termination, or a supply contract for a particular construction venture, the reason of the present section may well apply and entitle the buyer to the exemption.

10. Following its basic policy of using commercial practicability as a test for excuse, this section recognizes as of equal significance either a foreign or domestic regulation and disregards any technical distinctions between "law," "regulation," "order" and the like. Nor does it make the present action of the seller depend upon the eventual judicial determination of the legality of the particular governmental action. The seller's good faith belief in the validity of the regulation is the test under this Chapter and the best evidence of his good faith is the general commercial acceptance of the regulation. However, governmental interference cannot excuse unless it truly "supervenes" in such a manner as to be beyond the seller's assumption of risk. And any action by the party claiming excuse which causes or colludes in inducing the governmental action preventing his performance would be in breach of good faith and would destroy his exemption.

11. An excused seller must fulfill his contract to the extent which the supervening contingency permits, and if the situation is such that his customers are generally affected he must take account of all in supplying one. Subsections (a) and (b), therefore, explicitly permit in any proration a fair and reasonable attention to the needs of regular customers who are probably relying on spot orders for supplies. Customers at different stages of the manufacturing process may be fairly treated by including the seller's manufacturing requirements. A fortiori, the seller may also take account of contracts later in date than the one in question. The fact that such spot orders may be closed at an advanced price causes no difficulty, since any allocation which exceeds normal past requirements will not be reasonable. However, good faith requires, when prices have advanced, that the seller exercise real care in making his allocations, and in case of doubt his contract customers should be favored and supplies prorated evenly among them regardless of

price. Save for the extra care thus required by changes in the market, this section seeks to leave every reasonable business leeway to the seller.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Standard for Excusable Delay and Default — Failure to Deliver Siding: Morin Building Products Company's failure to deliver the metal siding is not excused by the problems it experienced with its subcontractors and suppliers. It is this court's conclusion that the problems encountered in manufacturing this siding were or should have been contemplated by Morin at the time the contract was formed. As established in Eastern Air Lines, Inc. v. McDonnell Douglas Corp., 532 F2d 957 (5th Cir. 1976), the standard for excusable delay and default is commercial impracticability. Morin Bldg. Prod. Co., Inc. v. Volk Constr. Co., Inc., 500 F. Supp. 82, 37 St. Rep. 1803 (D.C. Mont 1980).

30-2-616. Procedure on notice claiming excuse.

Official Comment

Prior Uniform Statutory Provision: None.

Purposes:

This section seeks to establish simple and workable machinery for providing certainty as to when a supervening and excusing contingency "excuses" the delay, "discharges" the contract, or may result in a waiver of the delay by the buyer. When the seller notifies, in accordance with the preceding section, claiming excuse, the buyer may acquiesce, in which case the contract is so modified. No consideration is necessary in a case of this kind to support such a modification. If the buyer does not elect so to modify the contract, he may terminate it and under subsection (2) his silence after receiving the seller's claim of excuse operates as such a termination. Subsection (3) denies effect to any contract clause made in advance of trouble which would require the buyer to stand ready to take delivery whenever the seller is excused from delivery by unforeseen circumstances.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

Part 7
Remedies

30-2-701. Remedies for breach of collateral contracts not impaired.

Official Comment

Prior Uniform Statutory Provision: None.

Purposes:

Whether a claim for breach of an obligation collateral to the contract for sale requires separate trial to avoid confusion of issues is beyond the scope of this Chapter; but contractual arrangements which as a business matter enter vitally into the contract should be considered a part thereof in so far as cross-claims or defenses are concerned.

30-2-702. Seller's remedies on discovery of buyer's insolvency.

Official Comment

Prior Uniform Statutory Provision: Subsection (1)—Sections 53(1)(b), 54(1)(c) and 57, Uniform Sales Act; Subsection (2)—none; Subsection (3)—Section 76(3), Uniform Sales Act.

Changes: Rewritten, the protection given to a seller who has sold on credit and has delivered goods to the buyer immediately preceding his insolvency being extended.

Purposes of Changes and New Matter: To make it clear that:

1. The seller's right to withhold the goods or to stop delivery except for cash when he discovers the buyer's insolvency is made explicit in subsection (1) regardless of the passage of title, and the concept of stoppage has been extended to include goods in the possession of any bailee who has not yet attorned to the buyer.

2. Subsection (2) takes as its base line the proposition that any receipt of goods on credit by an insolvent buyer amounts to a tacit business misrepresentation of solvency and therefore is fraudulent as against the particular seller. This Chapter makes discovery of the buyer's

insolvency and demand within a ten day period a condition of the right to reclaim goods on this ground. The ten day limitation period operates from the time of receipt of the goods.

An exception to this time limitation is made when a written misrepresentation of solvency has been made to the particular seller within three months prior to the delivery. To fall within the exception the statement of solvency must be in writing, addressed to the particular seller and dated within three months of the delivery.

3. Because the right of the seller to reclaim goods under this section constitutes preferential treatment as against the buyer's other creditors subsection (3) provides that such reclamation bars all his other remedies as to the goods involved.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

1983 Amendment: In (3), deleted "or lien creditor" after "good faith purchaser".

Conformity to Montana's Statute: This section was amended by sec. 6, Ch. 402, L. 1983, to conform Montana's statute to the 1966 amendment promulgated by the National Conference of Commissioners on Uniform State Laws.

30-2-703. Seller's remedies in general.

Official Comment

Prior Uniform Statutory Provision: No comparable index section. See Section 53, Uniform Sales Act.

Purposes:

1. This section is an index section which gathers together in one convenient place all of the various remedies open to a seller for any breach by the buyer. This Chapter rejects any doctrine of election of remedy as a fundamental policy and thus the remedies are essentially cumulative in nature and include all of the available remedies for breach. Whether the pursuit of one remedy bars another depends entirely on the facts of the individual case.

2. The buyer's breach which occasions the use of the remedies under this section may involve only one lot or delivery of goods, or may involve all of the goods which are the subject matter of the particular contract. The right of the seller to pursue a remedy as to all the goods when the breach is as to only one or more lots is covered by the section on breach in installment contracts. The present section deals only with the remedies available after the goods involved in the breach have been determined by that section.

3. In addition to the typical case of refusal to pay or default in payment, the language in the preamble, "fails to make a payment due," is intended to cover the dishonor of a check on due presentment, or the non-acceptance of a draft, and the failure to furnish an agreed letter of credit.

4. It should also be noted that this Act requires its remedies to be liberally administered and provides that any right or obligation which it declares is enforceable by action unless a different effect is specifically prescribed (Section 30-1-106).

Case Notes

Instruction on Damages Given in Permissive Language Held Error: Where the defendant county refused to accept delivery of a rock crusher it had previously agreed to purchase and the plaintiff brought an action for damages, it was error for the District Court to instruct the jury that it could award damages for lost net profits and incidental damages. The possible measures of damages under the U.C.C. are not stated in permissive language but are mandatory and specifically state the amount of recoverable damage, depending upon the remedy the seller has pursued. The District Court's use of the words "may award any of the following" implied to the jury that they were not required by law to award specific damages. The instruction was therefore erroneous as contrary to the U.C.C. Modern Mach. v. Flathead County, 202 M 140, 656 P2d 206, 39 St. Rep. 2383 (1982).

Contract for Scrap Metal — Resale After Breach — Measure of Damages: Where plaintiff and defendant entered into a contract whereby defendant was to purchase crushed auto bodies from plaintiff and where defendant refused to accept approximately one-half of the bodies at the agreed price, the plaintiff was entitled to damages representing the difference in price between what he actually received for the auto bodies upon resale, after the defendant refused to accept them, and what he would have received had the defendant not breached the contract. The plaintiff was not required to resell the bodies to the defendant. Weissman & Sons, Inc. v. Pepper, 480 F. Supp. 1364 (D.C. Mont. 1979).

30-2-704. Seller's right to identify goods to the contract notwithstanding breach or to salvage unfinished goods.

Official Comment

Prior Uniform Statutory Provision: Sections 63(3) and 64(4), Uniform Sales Act.

Changes: Rewritten, the seller's rights being broadened.

Purposes of Changes:

1. This section gives an aggrieved seller the right at the time of breach to identify to the contract any conforming finished goods, regardless of their resalability, and to use reasonable judgment as to completing unfinished goods. It thus makes the goods available for resale under the resale section, the seller's primary remedy, and in the special case in which resale is not practicable, allows the action for the price which would then be necessary to give the seller the value of his contract.

2. Under this Chapter the seller is given express power to complete manufacture or procurement of goods for the contract unless the exercise of reasonable commercial judgment as to the facts as they appear at the time he learns of the breach makes it clear that such action will result in a material increase in damages. The burden is on the buyer to show the commercially unreasonable nature of the seller's action in completing manufacture.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

Case Notes

Duty to Mitigate Damages — Burden of Proof: Where the defendant county refused to accept delivery of a rock crusher it had earlier agreed to purchase and the plaintiff brought an action for damages, it was error for the District Court to instruct the jury on the duty of the plaintiff alone to mitigate damages. The county had the opportunity at an early date to take affirmative action to affirm or repudiate the contract and failed to do so. The comments to 30-2-704 state that the burden is upon the buyer to show the commercially unreasonable nature of the seller's action. The instruction placing the entire burden of mitigation upon the plaintiff was therefore in error. Modern Mach. v. Flathead County, 202 M 140, 656 P2d 206, 39 St. Rep. 2383 (1982).

30-2-705. Seller's stoppage of delivery in transit or otherwise.

Official Comment

[*Corresponding U.C.C. Section:* Section 2-705, U.C.C.]

[*Code Commissioner Note:* In 2005, Montana adopted Alternative B of the 2003 revision to Article 7 for this section.]

Prior Uniform Statutory Provision: Sections 57-59, Uniform Sales Act; see also Sections 12, 14 and 42, Uniform Bills of Lading Act and Sections 9, 11 and 49, Uniform Warehouse Receipts Act.

Changes: This section continues and develops the above sections of the Uniform Sales Act in the light of the other uniform statutory provisions noted.

Purposes: To make it clear that:

1. Subsection (1) applies the stoppage principle to other bailees as well as carriers.

It also expands the remedy to cover the situations, in addition to buyer's insolvency, specified in the subsection. But since stoppage is a burden in any case to carriers, and might be a very heavy burden to them if it covered all small shipments in all these situations, the right to stop for reasons other than insolvency is limited to carload, truckload, planeload or larger shipments. The seller shipping to a buyer of doubtful credit can protect himself by shipping C.O.D.

Where stoppage occurs for insecurity it is merely a suspension of performance, and if assurances are duly forthcoming from the buyer the seller is not entitled to resell or divert.

Improper stoppage is a breach by the seller if it effectively interferes with the buyer's right to due tender under the section on manner of tender of delivery. However, if the bailee obeys an unjustified order to stop he may also be liable to the buyer. The measure of his obligation is dependent on the provisions of the Documents of Title Chapter (Section 30-7-303). Subsection 3(b) therefore gives him a right of indemnity as against the seller in such a case.

2. "Receipt by the buyer" includes receipt by the buyer's designated representative, the sub-purchaser, when shipment is made direct to him and the buyer himself never receives the goods. It is entirely proper under this Chapter that the seller, by making such direct shipment to the sub-purchaser, be regarded as acquiescing in the latter's purchase and as thus barred from stoppage of the goods as against him.

As between the buyer and the seller, the latter's right to stop the goods at any time until they reach the place of final delivery is recognized by this section.

Under subsection (3)(c) and (d), the carrier is under no duty to recognize the stop order of a person who is a stranger to the carrier's contract. But the seller's right as against the buyer to stop delivery remains, whether or not the carrier is obligated to recognize the stop order. If the carrier does obey it, the buyer cannot complain merely because of that circumstance; and the seller becomes obligated under subsection (3)(b) to pay the carrier any ensuing damages or charges.

3. A diversion of a shipment is not a "reshipment" under subsection (2)(c) when it is merely an incident to the original contract of transportation. Nor is the procurement of "exchange bills" of lading which change only the name of the consignee to that of the buyer's local agent but do not alter the destination of a reshipment.

Acknowledgment by the carrier as a "warehouse" within the meaning of this Chapter requires a contract of a truly different character from the original shipment, a contract not in extension of transit but as a warehouse.

4. Subsection (3)(c) makes the bailee's obedience of a notification to stop conditional upon the surrender of possession or control of any outstanding negotiable document.

5. Any charges or losses incurred by the carrier in following the seller's orders, whether or not he was obligated to do so, fall to the seller's charge.

6. After an effective stoppage under this section the seller's rights in the goods are the same as if he had never made a delivery.

Compiler's Comments

2005 Amendment: Chapter 575 in (2)(c) at end substituted "a warehouse" for "warehouseman"; in (3)(c) near end inserted "possession or control of"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-2-706. Seller's resale including contract for resale.

Official Comment

Prior Uniform Statutory Provision: Section 60, Uniform Sales Act.

Changes: Rewritten.

Purposes of Changes: To simplify the prior statutory provision and to make it clear that:

1. The only condition precedent to the seller's right of resale under subsection (1) is a breach by the buyer within the section on the seller's remedies in general or insolvency. Other meticulous conditions and restrictions of the prior uniform statutory provision are disapproved by this Chapter and are replaced by standards of commercial reasonableness. Under this section the seller may resell the goods after any breach by the buyer. Thus, an anticipatory repudiation by the buyer gives rise to any of the seller's remedies for breach, and to the right of resale. This principle is supplemented by subsection (2) which authorizes a resale of goods which are not in existence or were not identified to the contract before the breach.

2. In order to recover the damages prescribed in subsection (1) the seller must act "in good faith and in a commercially reasonable manner" in making the resale. This standard is intended to be more comprehensive than that of "reasonable care and judgment" established by the prior uniform statutory provision. Failure to act properly under this section deprives the seller of the measure of damages here provided and relegates him to that provided in Section 30-2-708.

Under this Chapter the seller resells by authority of law, in his own behalf, for his own benefit and for the purpose of fixing his damages. The theory of a seller's agency is thus rejected.

3. If the seller complies with the prescribed standard of duty in making the resale, he may recover from the buyer the damages provided for in subsection (1). Evidence of market or current prices at any particular time or place is relevant only on the question of whether the seller acted in a commercially reasonable manner in making the resale.

The distinction drawn by some courts between cases where the title had not passed to the buyer and the seller had resold as owner, and cases where the title had passed and the seller had resold by virtue of his lien on the goods, is rejected.

4. Subsection (2) frees the remedy of resale from legalistic restrictions and enables the seller to resell in accordance with reasonable commercial practices so as to realize as high a price as possible in the circumstances. By "public" sale is meant a sale by auction. A "private" sale may be effected by solicitation and negotiation conducted either directly or through a broker. In choosing between a public and private sale the character of the goods must be considered and relevant trade practices and usages must be observed.

5. Subsection (2) merely clarifies the common law rule that the time for resale is a reasonable time after the buyer's breach, by using the language "commercially reasonable." What is such a reasonable time depends upon the nature of the goods, the condition of the market and the other circumstances of the case; its length cannot be measured by any legal yardstick or divided into degrees. Where a seller contemplating resale receives a demand from the buyer for inspection under the section of preserving evidence of goods in dispute, the time for resale may be appropriately lengthened.

On the question of the place for resale, subsection (2) goes to the ultimate test, the commercial reasonableness of the seller's choice as to the place for an advantageous resale. This Chapter rejects the theory that the seller is required to resell at the agreed place for delivery and that a resale elsewhere can be permitted only in exceptional cases.

6. The purpose of subsection (2) being to enable the seller to dispose of the goods to the best advantage, he is permitted in making the resale to depart from the terms and conditions of the original contract for sale to any extent "commercially reasonable" in the circumstances.

7. The provision of subsection (2) that the goods need not be in existence to be resold applies when the buyer is guilty of anticipatory repudiation of a contract for future goods, before the goods or some of them have come into existence. In such a case the seller may exercise the right of resale and fix his damages by "one or more contracts to sell" the quantity of conforming future goods affected by the repudiation. The companion provision of subsection (2) that resale may be made although the goods were not identified to the contract prior to the buyer's breach, likewise contemplates an anticipatory repudiation by the buyer but occurring after the goods are in existence. If the goods so identified conform to the contract, their resale will fix the seller's damages quite as satisfactorily as if they had been identified before the breach.

8. Where the resale is to be by private sale, subsection (3) requires that reasonable notification of the seller's intention to resell must be given to the buyer. The length of notification of a private sale depends upon the urgency of the matter. Notification of the time and place of this type of sale is not required.

Subsection (4)(b) requires that the seller give the buyer reasonable notice of the time and place of a public resale so that he may have an opportunity to bid or to secure the attendance of other bidders. An exception is made in the case of goods "which are perishable or threaten to decline speedily in value."

9. Since there would be no reasonable prospect of competitive bidding elsewhere, subsection (4) requires that a public resale "must be made at a usual place or market for public sale if one is reasonably available;" i.e., a place or market which prospective bidders may reasonably be expected to attend. Such a market may still be "reasonably available" under this subsection, though at a considerable distance from the place where the goods are located. In such a case the expense of transporting the goods for resale is recoverable from the buyer as part of the seller's incidental damages under subsection (1). However, the question of availability is one of commercial reasonableness in the circumstances and if such "usual" place or market is not reasonably available, a duly advertised public resale may be held at another place if it is one which prospective bidders may reasonably be expected to attend, as distinguished from a place where there is no demand whatsoever for goods of the kind.

Paragraph (a) of subsection (4) qualifies the last sentence of subsection (2) with respect to resales of unidentified and future goods at public sale. If conforming goods are in existence the seller may identify them to the contract after the buyer's breach and then resell them at public sale. If the goods have not been identified, however, he may resell them at public sale only as "future" goods and only where there is a recognized market for public sale of futures in goods of the kind.

The provisions of paragraph (c) of subsection (4) are intended to permit intelligent bidding.

The provision of paragraph (d) of subsection (4) permitting the seller to bid and, of course, to become the purchaser, benefits the original buyer by tending to increase the resale price and thus decreasing the damages he will have to pay.

10. This Chapter departs in subsection (5) from the prior uniform statutory provision in permitting a good faith purchaser at resale to take a good title as against the buyer even though the seller fails to comply with the requirements of this section.

11. Under subsection (6), the seller retains profit, if any, without distinction based on whether or not he had a lien since this Chapter divorces the question of passage of title to the buyer from the seller's right of resale or the consequences of its exercise. On the other hand, where "a person in the position of a seller" or a buyer acting under the section on buyer's remedies, exercises his right of resale under the present section he does so only for the limited purpose of obtaining cash for his "security interest" in the goods. Once that purpose has been accomplished any excess in the resale price belongs to the seller to whom an accounting must be made as provided in the last sentence of subsection (6).

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

Case Notes

Damages Not Supported by Substantial Credible Evidence: Where the defendant county refused to accept delivery of a rock crusher it had earlier agreed to purchase and the plaintiff brought an action for damages, it was error for the jury to award the plaintiff $10,000 in damages. The measure of damages would be the contract price of $305,725 plus incidental damages less the resale price of $186,499.86 and expenses saved as a consequence of the breach, or would have been the plaintiff's anticipated profit of $78,879.56 plus incidental damages. Under either measure of damages, the record shows the damages to have been far in excess of the $10,000 awarded and there is no substantial credible evidence to support the verdict. Modern Mach. v. Flathead County, 202 M 140, 656 P2d 206, 39 St. Rep. 2383 (1982).

Instruction on Damages Given in Permissive Language Held Error: Where the defendant county refused to accept delivery of a rock crusher it had previously agreed to purchase and the plaintiff brought an action for damages, it was error for the District Court to instruct the jury that it could award damages for lost net profits and incidental damages. The possible measures of damages under the U.C.C. are not stated in permissive language but are mandatory and specifically state the amount of recoverable damage, depending upon the remedy the seller has pursued. The District Court's use of the words "may award any of the following" implied to the jury that they were not required by law to award specific damages. The instruction was therefore erroneous as contrary to the U.C.C. Modern Mach. v. Flathead County, 202 M 140, 656 P2d 206, 39 St. Rep. 2383 (1982).

Contract for Scrap Metal — Resale After Breach — Measure of Damages: Where plaintiff and defendant entered into a contract whereby defendant was to purchase crushed auto bodies from plaintiff and where defendant refused to accept approximately one-half of the bodies at the agreed price, the plaintiff was entitled to damages representing the difference in price between what he actually received for the auto bodies upon resale, after the defendant refused to accept them, and what he would have received had the defendant not breached the contract. The plaintiff was not required to resell the bodies to the defendant. Weissman & Sons, Inc. v. Pepper, 480 F. Supp. 1364 (D.C. Mont. 1979).

30-2-707. "Person in the position of a seller".

Official Comment

Prior Uniform Statutory Provision: Section 52(2), Uniform Sales Act.

Changes: Rewritten.

Purposes of Changes: To make it clear that:

In addition to following in general the prior uniform statutory provision, the case of a financing agency which has acquired documents by honoring a letter of credit for the buyer or by discounting a draft for the seller has been included in the term "a person in the position of a seller."

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

30-2-708. Seller's damages for nonacceptance or repudiation.

Official Comment

Prior Uniform Statutory Provision: Section 64, Uniform Sales Act.

Changes: Rewritten.

Purposes of Changes: To make it clear that:

1. The prior uniform statutory provision is followed generally in setting the current market price at the time and place for tender as the standard by which damages for non-acceptance are to be determined. The time and place of tender is determined by reference to Section 30-2-503 on manner of tender of delivery, and to the sections on the effect of such terms as FOB, FAS, CIF, C & F, Ex Ship and No Arrival, No Sale.

In the event that there is no evidence available of the current market price at the time and place of tender, proof of a substitute market may be made under the section on determination and proof of market price. Furthermore, the section on the admissibility of market quotations is intended to ease materially the problem of providing competent evidence.

2. The provision of this section permitting recovery of expected profit including reasonable overhead where the standard measure of damages is inadequate, together with the new requirement that price actions may be sustained only where resale is impractical, are designed to eliminate the unfair and economically wasteful results arising under the older law when fixed price articles were involved. This section permits the recovery of lost profits in all appropriate cases, which would include all standard priced goods. The normal measure there would be list price less cost to the dealer or list price less manufacturing cost to the manufacturer. It is not necessary to a recovery of "profit" to show a history of earnings, especially if a new venture is involved.

3. In all cases the seller may recover incidental damages.

Case Notes

Interpretation and Adoption of Lost Volume Seller Theory — No Error in Instructing Jury on Theory in Conjunction With Instruction on Mitigation of Damages Doctrine: The lost volume seller theory (see Restatement (Second) of Contracts 347, 350) allows a jury to consider the fact that an injured party, under certain circumstances, may not be made whole if its subsequent contracts diminish its losses. The traditional rule is that an injured party may not recover damages for breach of contract that the injured party could reasonably have avoided by entering into a subsequent contract. The lost volume seller theory provides only a limited exception to the traditional rule and does not undermine the requirement that an injured party must attempt to mitigate its damages in breach of contract claims, but instead allows a party to keep the monetary benefits of a breached contract, undiminished by the doctrine of mitigation of damages, if the party could have and would have entered into a second contract simultaneously with the breached contract. In addition, the theory applies with equal force to goods and services. Defendant in this case asserted that it was error for the trial court to instruct the jury on the lost volume seller theory. The Supreme Court noted that the trial court gave instructions on both the mitigation of damages doctrine and the lost volume seller theory and held that both instructions represented correct statements of the law. It was the jury's role to resolve factual disputes regarding plaintiff's duty to mitigate its losses and its alleged ability to profitably service the contract entered with defendant and the contract entered after defendant's breach, but it was not error for the trial court to give both instructions as statements of the applicable law. Bitterroot Int'l Sys., Ltd. v. W. Star Trucks, Inc., 2007 MT 48, 336 M 145, 153 P3d 627 (2007).

Damages Not Supported by Substantial Credible Evidence: Where the defendant county refused to accept delivery of a rock crusher it had earlier agreed to purchase and the plaintiff brought an action for damages, it was error for the jury to award the plaintiff $10,000 in damages. The measure of damages would be the contract price of $305,725 plus incidental damages less the resale price of $186,499.86 and expenses saved as a consequence of the breach, or would have been the plaintiff's anticipated profit of $78,879.56 plus incidental damages. Under either measure of damages, the record shows the damages to have been far in excess of the $10,000 awarded and there is no substantial credible evidence to support the verdict. Modern Mach. v. Flathead County, 202 M 140, 656 P2d 206, 39 St. Rep. 2383 (1982).

Instruction on Damages Given in Permissive Language Held Error: Where the defendant county refused to accept delivery of a rock crusher it had previously agreed to purchase and the plaintiff brought an action for damages, it was error for the District Court to instruct the jury that it could award damages for lost net profits and incidental damages. The possible measures of damages under the U.C.C. are not stated in permissive language but are mandatory and specifically state the amount of recoverable damage, depending upon the remedy the seller has pursued. The District Court's use of the words "may award any of the following" implied to the jury that they were not required by law to award specific damages. The instruction was therefore erroneous as contrary to the U.C.C. Modern Mach. v. Flathead County, 202 M 140, 656 P2d 206, 39 St. Rep. 2383 (1982).

30-2-709. Action for the price.

Official Comment

Prior Uniform Statutory Provision: Section 63, Uniform Sales Act.

Changes: Rewritten, important commercially needed changes being incorporated.

Purposes of Changes: To make it clear that:

1. Neither the passing of title to the goods nor the appointment of a day certain for payment is now material to a price action.
2. The action for the price is now generally limited to those cases where resale of the goods is impracticable except where the buyer has accepted the goods or where they have been destroyed after risk of loss has passed to the buyer.
3. This section substitutes an objective test by action for the former "not readily resalable" standard. An action for the price under subsection (1)(b) can be sustained only after a "reasonable effort to resell" the goods "at reasonable price" has actually been made or where the circumstances "reasonably indicate" that such an effort will be unavailing.
4. If a buyer is in default not with respect to the price, but on an obligation to make an advance, the seller should recover not under this section for the price as such, but for the default in the collateral (though coincident) obligation to finance the seller. If the agreement between the parties contemplates that the buyer will acquire, on making the advance, a security interest in the goods, the buyer on making the advance has such an interest as soon as the seller has rights in the agreed collateral. See Section 30-9-204 [now repealed, see 30-9A-204].
5. "Goods accepted" by the buyer under subsection (1) (a) include only goods as to which there has been no justified revocation of acceptance, for such a revocation means that there has been a default by the seller which bars his rights under this section. "Goods lost or damaged" are covered by the section on risk of loss. "Goods identified to the contract" under subsection (1)(b) are covered by the section on identification and the section on identification notwithstanding breach.
6. This section is intended to be exhaustive in its enumeration of cases where an action for the price lies.
7. If the action for the price fails, the seller may nonetheless have proved a case entitling him to damages for non-acceptance. In such a situation, subsection (3) permits recovery of those damages in the same action.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

Case Notes

Delivery Versus Acceptance: The Supreme Court rejected defendant's contention that Montana Seeds, Inc., failed to establish its claim for goods "sold and delivered" by not proving actual delivery. The determining factor was whether defendant "accepted" the goods. Here there were two shipments. Only the second shipment's acceptance was challenged by defendant based on his contention that it was misdelivered. However, defendant bore the risk of loss because he did not specify a particular destination. His cause of action for misdelivery was against the carrier. Mont. Seeds, Inc. v. Holliday, 178 M 119, 582 P2d 1223 (1978).

Definite Balance Due — When Presumed: Although Montana law is that "the single indispensable ingredient in an account stated is an exact, certain, and definite balance arrived at by the debtor and creditor", Nelson v. Mont. Iron Mining Co., 140 M 331, 371 P2d 874 (1962), this ingredient may be presumed when the debtor acquiesces to a statement of the balance due submitted by the creditor. Mont. Seeds, Inc. v. Holliday, 178 M 119, 582 P2d 1223 (1978).

30-2-710. Seller's incidental damages.

Official Comment

Prior Uniform Statutory Provision: See Sections 64 and 70, Uniform Sales Act.

Purposes:

To authorize reimbursement of the seller for expenses reasonably incurred by him as a result of the buyer's breach. The section sets forth the principal normal and necessary additional elements of damage flowing from the breach but intends to allow all commercially reasonable expenditures made by the seller.

Case Notes

Contract for Scrap Metal — Expenses of Resale — Vandalism: Where plaintiff and defendant entered into a contract whereby defendant was to purchase crushed auto bodies from the plaintiff and where, as a result of defendant's refusal to accept approximately half of the bodies, the plaintiff was forced to resell the auto bodies to another buyer, the plaintiff was entitled to recover from the defendant the costs directly incurred in resale but not entitled to recover damages for vandalism done to his equipment, as the vandalism was not occasioned by the breach of contract or foreseen by the parties. Weissman & Sons, Inc. v. Pepper, 480 F. Supp. 1364 (D.C. Mont. 1979).

30-2-711. Buyer's remedies in general — buyer's security interest in rejected goods.

Official Comment

Prior Uniform Statutory Provision: No comparable index section; Subsection (3)—Section 69(5), Uniform Sales Act.

Changes: The prior uniform statutory provision is generally continued and expanded in Subsection (3).

Purposes of Changes and New Matter:

1. To index in this section the buyer's remedies, subsection (1) covering those remedies permitting the recovery of money damages, and subsection (2) covering those which permit reaching the goods themselves. The remedies listed here are those available to a buyer who has not accepted the goods or who has justifiably revoked his acceptance. The remedies available to a buyer with regard to goods finally accepted appear in the section dealing with breach in regard to accepted goods. The buyer's right to proceed as to all goods when the breach is as to only some of the goods is determined by the section on breach in installment contracts and by the section on partial acceptance.

Despite the seller's breach, proper retender of delivery under the section on cure of improper tender or replacement can effectively preclude the buyer's remedies under this section, except for any delay involved.

2. To make it clear in subsection (3) that the buyer may hold and resell rejected goods if he has paid a part of the price or incurred expenses of the type specified. "Paid" as used here includes acceptance of a draft or other time negotiable instrument or the signing of a negotiable note. His freedom of resale is coextensive with that of a seller under this Chapter except that the buyer may not keep any profit resulting from the resale and is limited to retaining only the amount of the price paid and the costs involved in the inspection and handling of the goods. The buyer's security interest in the goods is intended to be limited to the items listed in subsection (3), and the buyer is not permitted to retain such funds as he might believe adequate for his damages. The buyer's right to cover, or to have damages for non-delivery, is not impaired by his exercise of his right of resale.

3. It should also be noted that this Act requires its remedies to be liberally administered and provides that any right or obligation which it declares is enforceable by action unless a different effect is specifically prescribed (Section 30-1-106).

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

Case Notes

Finding of Fact Inconsistent With Conclusions of Law: The lower court found that defendant allowed plaintiff to take a silage chopper on a "tryout" basis to determine whether the rpm requirements of the chopper were compatible with plaintiff's tractor power takeoff capacity. The Supreme Court held it was inconsistent for the lower court to proceed from that finding and conclude, as a matter of law, that defendant was liable based on breach of implied warranty of fitness, negligent misrepresentation, and constructive fraud. As to liability for breach of warranty, the claim would lie only after acceptance of goods. In this case, a finding of taking goods on a "tryout" basis was contradictory to the acceptance requirement. Because acceptance was critical to the outcome of that cause of action and the other causes of action, the conflicting findings and conclusions constituted error. Nelson v. Davis Modern Mach., 220 M 347, 715 P2d 1052, 43 St. Rep. 423 (1986).

30-2-712. "Cover" — buyer's procurement of substitute goods.

Official Comment

Prior Uniform Statutory Provision: None.

Purposes:

1. This section provides the buyer with a remedy aimed at enabling him to obtain the goods he needs thus meeting his essential need. This remedy is the buyer's equivalent of the seller's right to resell.

2. The definition of "cover" under subsection (1) envisages a series of contracts or sales, as well as a single contract or sale; goods not identical with those involved but commercially usable as reasonable substitutes under the circumstances of the particular case; and contracts on credit or delivery terms differing from the contract in breach, but again reasonable under the circumstances. The test of proper cover is whether at the time and place the buyer acted in good faith and in a reasonable manner, and it is immaterial that hindsight may later prove that the method of cover used was not the cheapest or most effective.

The requirement that the buyer must cover "without unreasonable delay" is not intended to limit the time necessary for him to look around and decide as to how he may best effect cover. The test here is similar to that generally used in this Chapter as to reasonable time and seasonable action.

3. Subsection (3) expresses the policy that cover is not a mandatory remedy for the buyer. The buyer is always free to choose between cover and damages for non-delivery under the next section.

However, this subsection must be read in conjunction with the section which limits the recovery of consequential damages to such as could not have been obviated by cover. Moreover, the operation of the section on specific performance of contracts for "unique" goods must be considered in this connection for availability of the goods to the particular buyer for his particular needs is the test for that remedy and inability to cover is made an express condition to the right of the buyer to replevy the goods.

4. This section does not limit cover to merchants, in the first instance. It is the vital and important remedy for the consumer buyer as well. Both are free to use cover: the domestic or non-merchant consumer is required only to act in normal good faith while the merchant buyer must also observe all reasonable commercial standards of fair dealing in the trade, since this falls within the definition of good faith on his part.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

Case Notes

Failure to Notify Grain Buyer of Intent to Breach Oral Agreement Within Reasonable Time — Oral Contract Enforceable: ConAgra, Inc. (ConAgra), contended that it had an oral telephone contract with Nierenberg to purchase 12,500 bushels of wheat and filed an action to recover losses incurred when Nierenberg sold the wheat to someone else, requiring ConAgra to purchase other wheat for resale at a higher price to fulfill its sale obligations pursuant to its purchase of Nierenberg's wheat. The District Court determined that Nierenberg was a merchant within the context of the Uniform Commercial Code and that, although both parties were merchants, the written sale confirmation received by Nierenberg 10 days after the telephone conversation was not within a reasonable time. Nierenberg never objected in writing to the written confirmation. The Supreme Court noted that the merchant exception in 30-2-201 does not dictate which party must send the written confirmation, but rather that in order to create an enforceable oral contract and avoid the signed writing requirement, one of the parties must send written confirmation to the other party. A farmer as well as a buyer may lock in an oral contract price as the market fluctuates up or down, and both parties equally possess the power to bind the other party. In this case, ConAgra did not immediately mail a written agreement, but instead waited about 6 days for Nierenberg to come to the elevator and sign the contract in person before mailing it. Although a court must look at the broad nature, purpose, and circumstances in determining whether written confirmation was received within a reasonable time, two specific factors may be examined: (1) the merchant's usual practice or policy following such transactions; and (2) the merchant's excuse for not following its practice or policy. The slight delay in Nierenberg's receipt of the confirmation because of an apparent misunderstanding was not seen as an unreasonable deviation from ConAgra's usual practices under the circumstances. However, Nierenberg chose to simply not honor his contractual obligation without notifying ConAgra of his true intentions. Nierenberg's mistake was to act outside of accepted commercial grain sales practices and not give ConAgra prompt notice of his breach so that his obligation for expectancy damages would be fixed. The written confirmation became an enforceable binding contract when Nierenberg failed to respond in writing with his objections within the stated 10-day period. The Supreme Court reversed the District Court's finding that the oral agreement could not be enforced. ConAgra, Inc. v. Nierenberg, 2000 MT 213, 301 M 55, 7 P3d 369, 57 St. Rep. 842 (2000).

Summary Judgment That Plaintiff Not Entitled to Damages Upheld: Lewis entered into a contract to log the timber on property of the Nine Mile Mines. Nine Mile learned that Lewis was staking mining claims on adjacent property and, pursuant to a noninterference clause in the contract, refused to let Lewis on its property to log the timber. Lewis filed suit for damages due to the cancellation, and Nine Mile moved for summary judgment on the issue of damages. The Supreme Court held that the contract was subject to U.C.C. provisions and that Lewis was not entitled to damages because he had failed to cover by purchasing substitute goods and because he relied only on his own speculative testimony to prove that he could not reasonably have procured cover and therefore had not raised any genuine issue of material fact. Lewis v. Nine Mile Mines, Inc., 268 M 336, 886 P2d 912, 51 St. Rep. 1283 (1994).

Damages Based on Cost to Replace Undelivered Grain: Defendants orally agreed to sell 6,500 bushels of wheat to Columbia Grain International (Columbia Grain), a Great Falls grain elevator, at $4.05 a bushel. Relying on the oral agreement, Columbia Grain sold the wheat in open market. When defendants refused to deliver the wheat, Columbia Grain purchased wheat from another seller for $4.68 a bushel. In an action to recover damages for breach of contract, the District Court awarded Columbia Grain the difference between the contract price of $4.05 and the replacement price of $4.68. On appeal, defendants claimed that the District Court erred in recognizing the existence of a contract, in failing to apply the statute of frauds defense, and in calculating damages. The Supreme Court affirmed, finding that an oral contract existed based on the parties' prior course of dealings and general industry practices and that defendants had waived their right to rely on the statute of frauds defense by not affirmatively pleading the defense. Damages are properly based on the cost of Columbia Grain to cover the undelivered grain. Columbia Grain Int'l v. Cereck, 258 M 414, 852 P2d 676, 50 St. Rep. 591 (1993).

30-2-713. Buyer's damages for nondelivery or repudiation.

Official Comment

Prior Uniform Statutory Provision: Section 67(3), Uniform Sales Act.

Changes: Rewritten.

Purposes of Changes: To clarify the former rule so that:

1. The general baseline adopted in this section uses as a yardstick the market in which the buyer would have obtained cover had he sought that relief. So the place for measuring damages is the place of tender (or the place of arrival if the goods are rejected or their acceptance is revoked after reaching their destination) and the crucial time is the time at which the buyer learns of the breach.
2. The market or current price to be used in comparison with the contract price under this section is the price for goods of the same kind and in the same branch of trade.
3. When the current market price under this section is difficult to prove the section on determination and proof of market price is available to permit a showing of a comparable market price or, where no market price is available, evidence of spot sale prices is proper. Where the unavailability of a market price is caused by a scarcity of goods of the type involved, a good case is normally made for specific performance under this Chapter. Such scarcity conditions, moreover, indicate that the price has risen and under the section providing for liberal administration of remedies, opinion evidence as to the value of the goods would be admissible in the absence of a market price and a liberal construction of allowable consequential damages should also result.
4. This section carries forward the standard rule that the buyer must deduct from his damages any expenses saved as a result of the breach.
5. The present section provides a remedy which is completely alternative to cover under the preceding section and applies only when and to the extent that the buyer has not covered.

Case Notes

Buyer Entitled to Damages for Shipment of Damaged Plants: Reed owned a greenhouse and ordered a shipment of poinsettias from McCalif for Christmas. When the plants arrived, many were damaged. Reed refused to pay $3,027.09 for the marketable plants that he kept and resold, contending that he had lost $8,683.95 on the damaged plants for which he had already received purchase orders from other buyers. The Supreme Court held that the record proved that there was no other source for replacement of the damaged plants and that McCalif was aware of that fact and the fact that Reed had entered into contracts for the resale of the plants. The Supreme Court ruled that Reed had the right to accept part of the plants received and reject the rest and that Reed was entitled to incidental and consequential damages because of McCalif's breach. The measure of damages was the difference between what Reed owed for the plants that he kept and what he lost on the orders that he could not fill. McCalif Grower Supplies, Inc. v. Reed, 272 M 254, 900 P2d 880, 52 St. Rep. 659 (1995).

Summary Judgment That Plaintiff Not Entitled to Damages Upheld: Lewis entered into a contract to log the timber on property of the Nine Mile Mines. Nine Mile learned that Lewis was staking mining claims on adjacent property and, pursuant to a noninterference clause in the contract, refused to let Lewis on its property to log the timber. Lewis filed suit for damages due to the cancellation, and Nine Mile moved for summary judgment on the issue of damages. The Supreme Court held that the contract was subject to U.C.C. provisions and that Lewis was not entitled to damages because he had failed to cover by purchasing substitute goods and because he relied only on his own speculative testimony to prove that he could not reasonably have procured cover and therefore had not raised any genuine issue of material fact. Lewis v. Nine Mile Mines, Inc., 268 M 336, 886 P2d 912, 51 St. Rep. 1283 (1994).

Damages Based on Cost to Replace Undelivered Grain: Defendants orally agreed to sell 6,500 bushels of wheat to Columbia Grain International (Columbia Grain), a Great Falls grain elevator, at $4.05 a bushel. Relying on the oral agreement, Columbia Grain sold the wheat in open market. When defendants refused to deliver the wheat, Columbia Grain purchased wheat from another seller for $4.68 a bushel. In an action to recover damages for breach of contract, the District Court awarded Columbia Grain the difference between the contract price of $4.05 and the replacement price of $4.68. On appeal, defendants claimed that the District Court erred in recognizing the existence of a contract, in failing to apply the statute of frauds defense, and in calculating damages. The Supreme Court affirmed, finding that an oral contract existed based on the parties' prior course of dealings and general industry practices and that defendants had waived their right to rely on the statute of frauds defense by not affirmatively pleading the defense. Damages are properly based on the cost of Columbia Grain to cover the undelivered grain. Columbia Grain Int'l v. Cereck, 258 M 414, 852 P2d 676, 50 St. Rep. 591 (1993).

Buyer's Right to Rely on Contract — Damages for Breach: The seller argued on appeal from a verdict for the purchaser in a breach of contract action that the buyer's complaint sought damages due to the buyer's detrimental reliance upon the contract, in that the buyer had obligated himself to resell the calves, which obligation the buyer then was unable to fulfill and for which the buyer was liable. The seller argued that, based upon the buyer's own pleadings, the buyer could not recover because he could not detrimentally rely on the contract; the seller had warned him he could not fulfill the contract. The Supreme Court said that argument was beside the point. Damages were determined ultimately on the simple basis of difference between market prices on the date of delivery and the date of execution, as provided by 30-2-713. Although the trial court's method of resolving damages did not conform precisely with the buyer's complaint, the action was proper. Under former Rule 8(f), M.R.Civ.P. (now superseded), pleadings are to be construed to do substantial justice. The real purpose of the claim as a whole was to be considered and honored. Here the purpose and spirit behind the complaint were recovery for breach of contract, and damages based upon the changes in the market were within the scope of the complaint. Miller v. Titeca, 192 M 357, 628 P2d 670, 38 St. Rep. 853 (1981).

Determination of Damages — Resale Contract Not Germane: The seller argued on appeal in a breach of contract action that the buyer never purchased the replacement calves that had been discussed in order to fulfill his contract for resale of the seller's calves to a feeder. As a consequence, he contended the failure to mitigate damages should have been taken into consideration. But damages, the Supreme Court said, were calculated on the basis of change in market price alone, pursuant to 30-2-713. The buyer's capacity to fulfill his own contract for resale was not an issue here. Accordingly, the trial court was upheld. Miller v. Titeca, 192 M 357, 628 P2d 670, 38 St. Rep. 853 (1981).

30-2-714. Buyer's damages for breach in regard to accepted goods.

Official Comment

Prior Uniform Statutory Provision: Section 69(6) and (7), Uniform Sales Act.

Changes: Rewritten.

Purposes of Changes:

1. This section deals with the remedies available to the buyer after the goods have been accepted and the time for revocation of acceptance has gone by. In general this section adopts the rule of the prior uniform statutory provision for measuring damages where there has been a

breach of warranty as to goods accepted, but goes further to lay down an explicit provision as to the time and place for determining the loss.

The section on deduction of damages from price provides an additional remedy for a buyer who still owes part of the purchase price, and frequently the two remedies will be available concurrently. The buyer's failure to notify of his claim under the section on effects of acceptance, however, operates to bar his remedies under either that section or the present section.

2. The "non-conformity" referred to in subsection (1) includes not only breaches of warranties but also any failure of the seller to perform according to his obligations under the contract. In the case of such non-conformity, the buyer is permitted to recover for his loss "in any manner which is reasonable."

3. Subsection (2) describes the usual, standard and reasonable method of ascertaining damages in the case of breach of warranty but it is not intended as an exclusive measure. It departs from the measure of damages for non-delivery in utilizing the place of acceptance rather than the place of tender. In some cases the two may coincide, as where the buyer signifies his acceptance upon the tender. If, however, the non-conformity is such as would justify revocation of acceptance, the time and place of acceptance under this section is determined as of the buyer's decision not to revoke.

4. The incidental and consequential damages referred to in subsection (3), which will usually accompany an action brought under this section, are discussed in detail in the comment on the next section.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

Case Notes

Jury Instruction Based on Statute Inapplicable: The trial court correctly refused to advise the jury on what damages a buyer may recover for nonconforming goods because there was no claim that the goods, in this case telephone systems, were inadequate. Rather, the claim was that the seller made untrue oral representations regarding distribution of the systems, installation and repair of the systems, refunds for unsold systems, and documentation and information permitting the telephone systems to be connected to telephone company lines. Webcor Electronics, Inc. v. Home Electronics, Inc., 231 M 377, 754 P2d 491, 45 St. Rep. 695 (1988).

Finding of Fact Inconsistent With Conclusions of Law: The lower court found that defendant allowed plaintiff to take a silage chopper on a "tryout" basis to determine whether the rpm requirements of the chopper were compatible with plaintiff's tractor power takeoff capacity. The Supreme Court held it was inconsistent for the lower court to proceed from that finding and conclude, as a matter of law, that defendant was liable based on breach of implied warranty of fitness, negligent misrepresentation, and constructive fraud. As to liability for breach of warranty, the claim would lie only after acceptance of goods. In this case, a finding of taking goods on a "tryout" basis was contradictory to the acceptance requirement. Because acceptance was critical to the outcome of that cause of action and the other causes of action, the conflicting findings and conclusions constituted error. Nelson v. Davis Modern Mach., 220 M 347, 715 P2d 1052, 43 St. Rep. 423 (1986).

Acceptance of Nonconforming Goods — Recovery of Damages Not Precluded — Notice: Respondent Meland received building materials on July 7, 1981. About 10 days later, he began assembling the building and discovered that the materials did not conform to the contract terms, at which time he immediately notified appellant Intermountain of the problem. He then proceeded with construction, using the component parts to produce a building height he desired. Under 30-2-606(1)(c), acceptance of goods occurs when the buyer does any act inconsistent with the seller's ownership. Meland's use of the delivered goods to construct a building was inconsistent with Intermountain's ownership and constituted acceptance. Intermountain argued that once there is acceptance no damages may be had. The Supreme Court ruled that under 30-2-607(2) acceptance precludes rejection of the goods or revocation if made with the knowledge of the nonconformity unless there is a reasonable assumption that the nonconformity may be reasonably cured, but does not preclude recovery for damages due. When a buyer has accepted goods and given notification, he may recover damages for any nonconformity under 30-2-714(1). Section 30-2-607(3) requires that the buyer must notify the seller within a reasonable time after he discovers any breach. In this case, notice was sufficient and the award of damages was affirmed. Meland v. Intermtn. Sys., Inc., 219 M 242, 712 P2d 1295, 42 St. Rep. 1987 (1985).

No Award of Attorney Fees Absent Statutory or Contract Provisions: Under 30-1-106, remedies under the U.C.C. shall be liberally administered to the end that the aggrieved party may be put in as good a position as if the other party had fully performed, but neither consequential, special, nor penal damages may be had except as specifically provided in the U.C.C. or by other rule of law. Although 30-2-714 allows recovery of incidental and consequential damages when accepted goods are in issue, the definitions of incidental and consequential damages contained in 30-2-715 do not include the award of attorney fees. In this case, the District Court awarded damages for delivery of nonconforming goods, plus attorney fees. The Supreme Court affirmed the award of damages but reversed the award of attorney fees as costs or damages absent any statutory or contract provisions, citing Martin v. Crown Life Ins. Co., 202 M 461, 658 P2d 1099 (1983). Meland v. Intermtn. Sys., Inc., 219 M 242, 712 P2d 1295, 42 St. Rep. 1987 (1985).

Reliance on Expertise — Implied Warranty of Fitness for Particular Purpose: Defendant relied on plaintiff's expertise to select an affordable fire alarm system that would provide reliable protection for the hotel's property and guests. Where the seller is aware that the buyer is relying upon the seller's judgment to select suitable goods, an implied warranty that the goods are fit for that particular purpose is created. The system installed was complicated, difficult to use, and frequently malfunctioned. Defendant advised plaintiff of the failure of the system after a fire in the snack bar, which was prior to the fire in a guest room that eventually resulted in this action. Plaintiff's own records showed repeated notifications of problems with the system. This was reasonable notice under 30-2-607(3). The implied warranty of fitness for a particular purpose was breached, and defendant was entitled to recover loss in value of the goods plus consequential and incidental damages. Fire Supply & Serv., Inc. v. Chico Hot Springs, 196 M 435, 639 P2d 1160, 39 St. Rep. 231 (1982).

Modular Home — Applicable Warranty Law: Sale of modular home manufactured at defendant's plant and delivered to plaintiffs' building site was governed by the U.C.C. warranty provisions and not the warranty provisions of Title 30, ch. 11, part 2, which are made inapplicable by 30-11-224. The fact that defendant had charge of the home until after it was affixed to plaintiffs' foundation and no longer had mobility did not affect the applicability of the U.C.C. warranty provisions, for the home was manufactured to plaintiffs' specifications, was thus identified to the contract under the U.C.C. at the time of the first step of its production, was movable at that time, and thus was "goods" the sale of which the U.C.C. applied. Little v. Grizzly Mfg., 195 M 419, 636 P2d 839, 38 St. Rep. 1994 (1981).

Breach of Casket Warranty — Mental Suffering: A contract for the sale of a casket is one of those rare contracts which could give rise to a cause of action for liability based on mental suffering alone and the seller's warranty of casket seal can be recovered upon by members of the family of the buyer. Hirst v. Elgin Metal Casket Co., 438 F. Supp. 906 (D.C. Mont. 1977).

30-2-715. Buyer's incidental and consequential damages.

Official Comment

Prior Uniform Statutory Provision: Subsection (2)(b)—Sections 69(7) and 70, Uniform Sales Act.

Changes: Rewritten.

Purposes of Changes and New Matter:

1. Subsection (1) is intended to provide reimbursement for the buyer who incurs reasonable expenses in connection with the handling of rightfully rejected goods or goods whose acceptance may be justifiably revoked, or in connection with effecting cover where the breach of the contract lies in non-conformity or non-delivery of the goods. The incidental damages listed are not intended to be exhaustive but are merely illustrative of the typical kinds of incidental damage.

2. Subsection (2) operates to allow the buyer, in an appropriate case, any consequential damages which are the result of the seller's breach. The "tacit agreement" test for the recovery of consequential damages is rejected. Although the older rule at common law which made the seller liable for all consequential damages of which he had "reason to know" in advance is followed, the liberality of that rule is modified by refusing to permit recovery unless the buyer could not reasonably have prevented the loss by cover or otherwise. Subparagraph (2) carries forward the provisions of the prior uniform statutory provision as to consequential damages resulting from breach of warranty, but modifies the rule by requiring first that the buyer attempt to minimize his damages in good faith, either by cover or otherwise.

3. In the absence of excuse under the section on merchant's excuse by failure of presupposed conditions, the seller is liable for consequential damages in all cases where he had reason to know of the buyer's general or particular requirements at the time of contracting. It is not necessary that

there be a conscious acceptance of an insurer's liability on the seller's part, nor is his obligation for consequential damages limited to cases in which he fails to use due effort in good faith.

Particular needs of the buyer must generally be made known to the seller while general needs must rarely be made known to charge the seller with knowledge.

Any seller who does not wish to take the risk of consequential damages has available the section on contractual limitation of remedy.

4. The burden of proving the extent of loss incurred by way of consequential damage is on the buyer, but the section on liberal administration of remedies rejects any doctrine of certainty which requires almost mathematical precision in the proof of loss. Loss may be determined in any manner which is reasonable under the circumstances.

5. Subsection (2)(b) states the usual rule as to breach of warranty, allowing recovery for injuries "proximately" resulting from the breach. Where the injury involved follows the use of goods without discovery of the defect causing the damage, the question of "proximate" cause turns on whether it was reasonable for the buyer to use the goods without such inspection as would have revealed the defects. If it was not reasonable for him to do so, or if he did in fact discover the defect prior to his use, the injury would not proximately result from the breach of warranty.

6. In the case of sale of wares to one in the business of reselling them, resale is one of the requirements of which the seller has reason to know within the meaning of subsection (2)(a).

Case Notes

Foreseeability Not Required in Breach of Contract Action Under Uniform Commercial Code When Injury Results From Breach of Warranty: A breach of contract action under the Uniform Commercial Code does not require foreseeability if injury to person or property proximately results from any breach of warranty. Rothing v. Kallestad, 2007 MT 109, 337 M 193, 159 P3d 222 (2007).

Buyer Entitled to Damages for Shipment of Damaged Plants: Reed owned a greenhouse and ordered a shipment of poinsettias from McCalif for Christmas. When the plants arrived, many were damaged. Reed refused to pay $3,027.09 for the marketable plants that he kept and resold, contending that he had lost $8,683.95 on the damaged plants for which he had already received purchase orders from other buyers. The Supreme Court held that the record proved that there was no other source for replacement of the damaged plants and that McCalif was aware of that fact and the fact that Reed had entered into contracts for the resale of the plants. The Supreme Court ruled that Reed had the right to accept part of the plants received and reject the rest and that Reed was entitled to incidental and consequential damages because of McCalif's breach. The measure of damages was the difference between what Reed owed for the plants that he kept and what he lost on the orders that he could not fill. McCalif Grower Supplies, Inc. v. Reed, 272 M 254, 900 P2d 880, 52 St. Rep. 659 (1995).

Summary Judgment That Plaintiff Not Entitled to Damages Upheld: Lewis entered into a contract to log the timber on property of the Nine Mile Mines. Nine Mile learned that Lewis was staking mining claims on adjacent property and, pursuant to a noninterference clause in the contract, refused to let Lewis on its property to log the timber. Lewis filed suit for damages due to the cancellation, and Nine Mile moved for summary judgment on the issue of damages. The Supreme Court held that the contract was subject to U.C.C. provisions and that Lewis was not entitled to damages because he had failed to cover by purchasing substitute goods and because he relied only on his own speculative testimony to prove that he could not reasonably have procured cover and therefore had not raised any genuine issue of material fact. Lewis v. Nine Mile Mines, Inc., 268 M 336, 886 P2d 912, 51 St. Rep. 1283 (1994).

Doctrine of Avoidable Consequences — Prudent Person Standard: In determining whether consequential damages resulting from a seller's breach of warranty were justified, the Supreme Court cited Harrington v. Holiday Rambler Corp., 176 M 37, 575 P2d 578 (1978), regarding the doctrine of avoidable consequences, stating that the "duty to reduce or mitigate damages is a positive one upon the injured person, but it has limits". The test is what an ordinary prudent person would be expected to do, if capable, under the circumstances. Melotz v. Scheckla, 245 M 327, 801 P2d 593, 47 St. Rep. 2165 (1990).

No Award of Attorney Fees Absent Statutory or Contract Provisions: Under 30-1-106, remedies under the U.C.C. shall be liberally administered to the end that the aggrieved party may be put in as good a position as if the other party had fully performed, but neither consequential, special, nor penal damages may be had except as specifically provided in the U.C.C. or by other rule of law. Although 30-2-714 allows recovery of incidental and consequential damages when accepted goods are in issue, the definitions of incidental and consequential damages contained in 30-2-715 do not include the award of attorney fees. In this case, the District Court awarded damages for delivery of nonconforming goods, plus attorney fees. The Supreme Court affirmed the award of damages but reversed the award of attorney fees as costs or damages absent any statutory or contract provisions, citing Martin v. Crown Life Ins. Co., 202 M 461, 658 P2d 1099 (1983). Meland v. Intermtn. Sys., Inc., 219 M 242, 712 P2d 1295, 42 St. Rep. 1987 (1985).

Breach of Casket Warranty — Mental Suffering: A contract for the sale of a casket is one of those rare contracts which could give rise to a cause of action for liability based on mental suffering alone and the seller's warranty of casket seal can be recovered upon by members of the family of the buyer. Hirst v. Elgin Metal Casket Co., 438 F. Supp. 906 (D.C. Mont. 1977).

Consequential Damages — Defective Semen for Cattle Breeding: Consequential damages are those that ordinarily follow the breach of a contract in the usual course of events or that reasonable men would have foreseen as a probable result of the breach, and thus in the case of defective semen sold for artificial insemination, the loss of a calf crop would be reasonably foreseeable, but the loss of a second calf crop which might have been produced by the unborn calf crop is not reasonably foreseeable. Baden v. Curtiss Breeding Serv., 380 F. Supp. 243 (D. C. Mont. 1974).

30-2-716. Buyer's right to specific performance or recovery of goods.

Official Comment

Prior Uniform Statutory Provision: Section 68, Uniform Sales Act.

Changes: Rephrased.

Purposes of Changes: To make it clear that:

1. The present section continues in general prior policy as to specific performance and injunction against breach. However, without intending to impair in any way the exercise of the court's sound discretion in the matter, this Chapter seeks to further a more liberal attitude than some courts have shown in connection with the specific performance of contracts of sale.

2. In view of this Chapter's emphasis on the commercial feasibility of replacement, a new concept of what are "unique" goods is introduced under this section. Specific performance is no longer limited to goods which are already specific or ascertained at the time of contracting. The test of uniqueness under this section must be made in terms of the total situation which characterizes the contract. Output and requirements contracts involving a particular or peculiarly available source or market present today the typical commercial specific performance situation, as contrasted with contracts for the sale of heirlooms or priceless works of art which were usually involved in the older cases. However, uniqueness is not the sole basis of the remedy under this section for the relief may also be granted "in other proper circumstances" and inability to cover is strong evidence of "other proper circumstances".

3. The legal remedy of replevin is given to the buyer in cases in which cover is reasonably unavailable and goods have been identified to the contract. This is in addition to the buyer's right to recover identified goods under Section 30-2-502. For consumer goods, the buyer's right to replevin vests upon the buyer's acquisition of a special property, which occurs upon identification of the goods to the contract. See Section 30-2-501. Inasmuch as a secured party normally acquires no greater rights in its collateral that its debtor had or had power to convey, see Section 30-2-403(1) (first sentence), a buyer who acquires a right of replevin under subsection (3) will take free of a security interest created by the seller if it attaches to the goods after the goods have been identified to the contract. The buyer will take free, even if the buyer does not buy in ordinary course and even if the security interest is perfected. Of course, to the extent that the buyer pays the price after the security interest attaches, the payments will constitute proceeds of the security interest.

4. This section is intended to give the buyer rights to the goods comparable to the seller's rights to the price.

5. If a negotiable document of title is outstanding, the buyer's right of replevin relates of course to the document not directly to the goods. See Chapter 7, especially Section 30-7-602.

Compiler's Comments

1999 Amendment: Chapter 305 inserted last sentence concerning household goods; and made minor changes in style. Amendment effective July 1, 2001.

30-2-717. Deduction of damages from the price.

Official Comment

Prior Uniform Statutory Provision: See Section 69(1) (a), Uniform Sales Act.

Purposes:

1. This section permits the buyer to deduct from the price damages resulting from any breach by the seller and does not limit the relief to cases of breach of warranty as did the prior uniform statutory provision. To bring this provision into application the breach involved must be of the same contract under which the price in question is claimed to have been earned.

2. The buyer, however, must give notice of his intention to withhold all or part of the price if he wishes to avoid a default within the meaning of the section on insecurity and right to assurances. In conformity with the general policies of this Chapter, no formality of notice is required and any language which reasonably indicates the buyer's reason for holding up his payment is sufficient.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

Case Notes

Modular Home — Applicable Warranty Law: Sale of modular home manufactured at defendant's plant and delivered to plaintiffs' building site was governed by the U.C.C. warranty provisions and not the warranty provisions of Title 30, ch. 11, part 2, which are made inapplicable by 30-11-224. The fact that defendant had charge of the home until after it was affixed to plaintiffs' foundation and no longer had mobility did not affect the applicability of the U.C.C. warranty provisions, for the home was manufactured to plaintiffs' specifications, was thus identified to the contract under the U.C.C. at the time of the first step of its production, was movable at that time, and thus was "goods" the sale of which the U.C.C. applied. Little v. Grizzly Mfg., 195 M 419, 636 P2d 839, 38 St. Rep. 1994 (1981).

30-2-718. Liquidation or limitation of damages — deposits.

Official Comment

Prior Uniform Statutory Provision: None.

Purposes:

1. Under subsection (1) liquidated damage clauses are allowed where the amount involved is reasonable in the light of the circumstances of the case. The subsection sets forth explicitly the elements to be considered in determining the reasonableness of a liquidated damage clause. A term fixing unreasonably large liquidated damages is expressly made void as a penalty. An unreasonably small amount would be subject to similar criticism and might be stricken under the section on unconscionable contracts or clauses.

2. Subsection (2) refuses to recognize a forfeiture unless the amount of the payment so forfeited represents a reasonable liquidation of damages as determined under subsection (1). A special exception is made in the case of small amounts (20% of the price or $500, whichever is smaller) deposited as security. No distinction is made between cases in which the payment is to be applied on the price and those in which it is intended as security for performance. Subsection (2) is applicable to any deposit or down or part payment. In the case of a deposit or turn in of goods resold before the breach, the amount actually received on the resale is to be viewed as the deposit rather than the amount allowed the buyer for the trade in. However, if the seller knows of the breach prior to the resale of the goods turned in, he must make reasonable efforts to realize their true value, and this is assured by requiring him to comply with the conditions laid down in the section on resale by an aggrieved seller.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-2-719. Contractual modification or limitation of remedy.

Official Comment

Prior Uniform Statutory Provision: None.

Purposes:

1. Under this section parties are left free to shape their remedies to their particular requirements and reasonable agreements limiting or modifying remedies are to be given effect.

However, it is of the very essence of a sales contract that at least minimum adequate remedies be available. If the parties intend to conclude a contract for sale within this Chapter they must accept the legal consequence that there be at least a fair quantum of remedy for breach of the obligations or duties outlined in the contract. Thus any clause purporting to modify or limit the remedial provisions of this Chapter in an unconscionable manner is subject to deletion and in that event the remedies made available by this Chapter are applicable as if the stricken clause had never existed. Similarly, under subsection (2), where an apparently fair and reasonable clause because of circumstances fails in its purpose or operates to deprive either party of the substantial value of the bargain, it must give way to the general remedy provisions of this Chapter.

2. Subsection (1)(b) creates a presumption that clauses prescribing remedies are cumulative rather than exclusive. If the parties intend the term to describe the sole remedy under the contract, this must be clearly expressed.

3. Subsection (3) recognizes the validity of clauses limiting or excluding consequential damages but makes it clear that they may not operate in an unconscionable manner. Actually such terms are merely an allocation of unknown or undeterminable risks. The seller in all cases is free to disclaim warranties in the manner provided in Section 30-2-316.

Case Notes

Other Remedies Available When Not Limited by Parties: Vendees leased a printing press from the vendor under a lease agreement that contained an option to purchase for a small sum at the end of the lease agreement. On appeal, the agreement was considered a sales contract and thus subject to the sales provisions of the U.C.C. Although a disclaimer in the contract deprived the vendees/lessees from asserting a defense based on breach of implied warranties, the clause did not attempt to deprive them of all remedies available under the U.C.C. The parties did not further limit or modify the remedies available to either party upon breach under this section; therefore, under 30-2-601 and 30-2-602, the vendees still possessed the right to reject the printing press, provided the rejection was timely and proper. Beneficial Commercial Corp. v. Cottrell, 212 M 493, 688 P2d 1254, 41 St. Rep. 1888 (1984).

When Limitation of Remedies Permissible — Equipment Sales — Factors: In a case stemming from an accident involving a hay baler, one issue on appeal was the limitation of remedies. Although limitation of damages for personal injuries in the case of consumer goods is prima facie unconscionable under 30-2-719, farm equipment is defined as "equipment". The limitation of remedy provisions could as a matter of law be found unconscionable. Accordingly, the court ordered an evidentiary hearing on the remedy limitations. Factors under 30-2-302 were to be considered at the hearing. Schlenz v. John Deere Co., 511 F. Supp. 224, 38 St. Rep. 579 (D.C. Mont. 1981).

Effect of "As Is" Clause in Used Car Sales Agreement: When defendant failed to inspect a car for defects before sale to plaintiff and the defect that was the proximate cause of plaintiff's accident and subsequent injuries would have been discovered in a reasonable safety inspection, defendant should not be allowed to hide behind the cloak of a simple "as is" disclaimer. Public policy requires a used car dealer to inspect the cars he sells and to make sure they are in safe, working condition. Kopischke v. First Cont. Corp., 187 M 471, 610 P2d 668 (1980).

Disclaimer Received After Sale Ineffective: A disclaimer or limitation of warranty contained in a manufacturer's manual received by the purchasers subsequent to the sale does not limit recovery for implied or express warranties made prior to or at the time of the sale. Whitaker v. Farmhand, Inc., 173 M 345, 567 P2d 916 (1977), followed in Vandalia Ranch, Inc. v. Farmers Union Oil & Supply Co., 221 M 253, 718 P2d 647, 43 St. Rep. 790 (1986).

Limitation of Damages: Clause in telephone company contract for "yellow pages" advertising, limiting liability for errors and omissions in advertising was a valid and binding limitation rather than a contract fixing damages. State ex rel. Mtn. St. Tel. & Tel. Co. v. District Court, 160 M 443, 503 P2d 526 (1972).

30-2-720. Effect of "cancellation" or "rescission" on claims for antecedent breach.

Official Comment

Prior Uniform Statutory Provision: None.

Purposes:

This section is designed to safeguard a person holding a right of action from any unintentional loss of rights by the ill-advised use of such terms as "cancellation", "rescission", or the like. Once a party's rights have accrued they are not to be lightly impaired by concessions made in business decency and without intention to forego them. Therefore, unless the cancellation of a contract expressly declares that it is "without reservation of rights", or the like, it cannot be considered to be a renunciation under this section.

30-2-721. Remedies for fraud.

Official Comment

Prior Uniform Statutory Provision: None.

Purposes: To correct the situation by which remedies for fraud have been more circumscribed than the more modern and mercantile remedies for breach of warranty. Thus the remedies for fraud are extended by this section to coincide in scope with those for non-fraudulent breach. This section thus makes it clear that neither rescission of the contract for fraud nor rejection of the goods bars other remedies unless the circumstances of the case make the remedies incompatible.

30-2-722. Who can sue third parties for injury to goods.

Official Comment

Prior Uniform Statutory Provision: None.

Purposes: To adopt and extend somewhat the principle of the statutes which provide for suit by the real party in interest. The provisions of this section apply only after identification of the goods. Prior to that time only the seller has a right of action. During the period between identification and final acceptance (except in the case of revocation of acceptance) it is possible for both parties to have the right of action. Even after final acceptance both parties may have the right of action if the seller retains possession or otherwise retains an interest.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

30-2-723. Proof of market price — time and place.

Official Comment

Prior Uniform Statutory Provision: None.

Purposes: To eliminate the most obvious difficulties arising in connection with the determination of market price, when that is stipulated as a measure of damages by some provision of this Chapter. Where the appropriate market price is not readily available the court is here granted reasonable leeway in receiving evidence of prices current in other comparable markets or at other times comparable to the one in question. In accordance with the general principle of this Chapter against surprise, however, a party intending to offer evidence of such a substitute price must give suitable notice to the other party.

This section is not intended to exclude the use of any other reasonable method of determining market price or of measuring damages if the circumstances of the case make this necessary.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

30-2-724. Admissibility of market quotations.

Official Comment

Prior Uniform Statutory Provision: None.

Purposes: To make market quotations admissible in evidence while providing for a challenge of the material by showing the circumstances of its preparation.

No explicit provision as to the weight to be given to market quotations is contained in this section, but such quotations, in the absence of compelling challenge, offer an adequate basis for a verdict.

Market quotations are made admissible when the price or value of goods traded "in any established market" is in issue. The reason of the section does not require that the market be closely organized in the manner of a produce exchange. It is sufficient if transactions in the commodity are frequent and open enough to make a market established by usage in which one price can be expected to affect another and in which an informed report of the range and trend of prices can be assumed to be reasonably accurate.

This section does not in any way intend to limit or negate the application of similar rules of admissibility to other material, whether by action of the courts or by statute. The purpose of the present section is to assure a minimum of mercantile administration in this important situation and not to limit any liberalizing trend in modern law.

30-2-725. Statute of limitations in contracts for sale.

Official Comment

Prior Uniform Statutory Provision: None.

Purposes: To introduce a uniform statute of limitations for sales contracts, thus eliminating the jurisdictional variations and providing needed relief for concerns doing business on a nationwide scale whose contracts have heretofore been governed by several different periods of limitation depending upon the state in which the transaction occurred. This Chapter takes sales contracts out of the general laws limiting the time for commencing contractual actions and selects a four year period as the most appropriate to modern business practice. This is within the normal commercial record keeping period.

Subsection (1) permits the parties to reduce the period of limitation. The minimum period is set at one year. The parties may not, however, extend the statutory period.

Subsection (2), providing that the cause of action accrues when the breach occurs, states an exception where the warranty extends to future performance.

Subsection (3) states the saving provision included in many state statutes and permits an additional short period for bringing new actions, where suits begun within the four year period have been terminated so as to leave a remedy still available for the same breach.

Subsection (4) makes it clear that this Chapter does not purport to alter or modify in any respect the law on tolling of the Statute of Limitations as it now prevails in the various jurisdictions.

Case Notes

Argument That Ratepayers Were Improperly Charged Franchise Fees on City Services — Commonality Found: The city of Billings appealed a District Court order certifying three classes of ratepayers who challenged certain franchise fees the city charged on city services, such as water, solid waste disposal, and wastewater. The city argued that the ratepayers should not be certified as a class because they did not share common questions of law and fact, or commonality. Specifically, Billings argued that the statute of limitations found in 30-2-725 controlled and that the start date for the class should be modified accordingly from the District Court determination. The Supreme Court did not find this argument persuasive and it affirmed, stating that the District Court is able on remand to modify a class definition to address statute of limitation concerns or other concerns addressing commonality. The city of Billings also argued that the ratepayers lacked commonality of claims because the claims involved legislative and administrative claims and Billings has legislative immunity under 2-9-111. The Supreme Court stated that whether legislative immunity applies is a merits argument that would be determined during the litigation and would apply equally to all ratepayers. Further, no evidence was presented regarding legislative versus administrative claims and thus the case was entirely focused on whether the franchise fees were legal. Houser v. Billings, 2020 MT 51, 399 Mont. 140, 458 P.3d 1031.

Statute of Limitations Applicable to Contract for Sale of Wheat: The appropriate statute of limitations applicable to a proceeding concerning an alleged contract for the sale of wheat is the 4-year period provided for in this section that specifically applies to contracts for the sale of goods, rather than the general statute of limitations contained in 27-2-202 covering actions on contracts. Mogan v. Cargill, Inc., 259 M 400, 856 P2d 973, 50 St. Rep. 851 (1993).

Lack of Contract — Breach of Warranty Sounded in Tort Rather Than Contract: Plaintiff was injured in 1979 while spraying weeds. He brought suit in 1984 against the producers, distributors, and sellers of the herbicide and spraying equipment, claiming counts in strict liability in tort, tortious misrepresentation, negligence, and contract for breach of sellers' warranty. Plaintiff had no direct written contract with any of the defendants. The District Court found that there was no contract from which to imply the warranties which plaintiff claimed were breached. The court reasoned that without a contract the breach of warranty claims sounded in tort rather than contract; therefore, the warranty claims were barred by the 3-year tort Statute of Limitations. On appeal, plaintiff contended that one of the longer contract Statutes of Limitations in 27-2-202 or 30-2-725 should apply. The Supreme Court disagreed, noting that the implied covenants of good faith and fair dealing, fitness for a particular purpose, merchantability, and workmanlike performance are imposed by law regardless of contract and that, absent a contract, breach of the implied covenants sounds in tort, not contract. The District Court judgment was affirmed. Bennett v. Dow Chem. Co., 220 M 117, 713 P2d 992, 43 St. Rep. 221 (1986).

Motion In Limine — Irrelevant Evidence on Statute of Limitations and Release Properly Excluded: Where the plaintiff brought a third-party action against the defendant for breach of a warranty of performance of certain air pollution control equipment, the District Court properly granted the plaintiff's motion in limine to exclude evidence of the plaintiff's release from liability signed by the plaintiff in the original action and evidence that the date of delivery of the equipment was the starting time of the running of the Statute of Limitations. While the defendant argues that this evidence shows a lack of any real liability to the plaintiff in the original action and therefore a lack of liability of the defendant, the evidence shows that the release had nothing to do with the issue of the warranty and that the evidence concerning the date of delivery was excluded as irrelevant because the trial court properly found that a cause of action for breach of warranty of performance began when the breach was discovered and not when the equipment was delivered. Iowa Mfg. Co. v. Joy Mfg. Co., 206 M 26, 669 P2d 1057, 40 St. Rep. 1479 (1983).

Warranty of Performance — Action Not Barred by Statute: Where the plaintiff brought an action against the defendant for breach of warranty of certain air pollution control equipment sold to the plaintiff more than 4 years prior to the commencement of the action, the District Court did not err in ruling that the action was not foreclosed by the Statute of Limitations. The warranty offered by the defendant was a warranty of performance, which contemplated operation of the equipment for at least as long as it would take to discover any breach. The District Court held that the statute ran from discovery of any breach, and this holding was correct. Iowa Mfg. Co. v. Joy Mfg. Co., 206 M 26, 669 P2d 1057, 40 St. Rep. 1479 (1983).

Breach of Contractual Warranties — Proper Parties — Statute of Frauds: Plaintiffs in an action for breach of express and implied warranties were farmers. Defendants manufactured farm implements. One of the plaintiffs had an arm severed in an accident involving the defendants' machinery. On appeal, the defendants argued that the injured plaintiff was not a party to the purchase contract. The plaintiff alleged the salesman knew that he and the party who actually signed the purchase order were to be co-owners of the hay baler in question. The signature was for the one co-owner for himself and as agent for the plaintiff as well. Because principal and agent law supplements the Montana U.C.C. which covers the purchase of the baler, the court considered applying 28-10-203, which prevents oral authorization to contract when the contract itself must be written, as here. It noted exceptions to the Statute of Frauds, however. The question of whether payment of the purchase price took this contract out of the Statute of Frauds was a genuine issue of material fact preventing a summary judgment for the defendants under the Federal Rules of Civil Procedure. Holding the question one of law, the court said it had to hold an evidentiary hearing on the issues. Because the cause of action was based on breach of contractual warranties, this section rather than 27-2-204 was the applicable Statute of Limitations. Schlenz v. John Deere Co., 511 F. Supp. 224, 38 St. Rep. 579 (D.C. Mont. 1981).

Laches and Statute of Limitations Adequately Pleaded: Plaintiffs' suit for rescission was barred by laches and their action for damages for breach of contract was barred by the 4-year Statute of Limitations. Since defendant's affirmative defenses revealed that plaintiffs had adequate notice of the defenses of laches and Statute of Limitations, although not specifically denominated as such, summary judgment was properly granted to defendants. Brabender v. Kit Mfg. Co., 174 M 63, 568 P2d 547 (1977).

CHAPTER 2A
UNIFORM COMMERCIAL CODE LEASES

Chapter Compiler's Comments

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

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Part 1
General Provisions

30-2A-101. Short title.

Official Comment

Source: Section 2A-101, U.C.C.

Rationale for Codification:

There are several reasons for codifying the law with respect to leases of goods. An analysis of the case law as it applies to leases of goods suggests at least three significant issues to be resolved by codification. First, what is a lease? It is necessary to define lease to determine whether a transaction creates a lease or a security interest disguised as a lease. If the transaction creates a security interest disguised as a lease, the lessor will be required to file a financing statement or take other action to perfect its interest in the goods against third parties. There is no such requirement with respect to leases. Yet the distinction between a lease and a security interest disguised as a lease is not clear. Second, will the lessor be deemed to have made warranties to the lessee? If the transaction is a sale the express and implied warranties of Article 2 [Title 30, chapter 2] of the Uniform Commercial Code apply. However, the warranty law with respect to leases is uncertain. Third, what remedies are available to the lessor upon the lessee's default? If the transaction is a security interest disguised as a lease, the answer is stated in Part 5 of the Article on Secured Transactions (Article 9 [Title 30, chapter 9A]). There is no clear answer with respect to leases.

There are reasons to codify the law with respect to leases of goods in addition to those suggested by a review of the reported cases. The answer to this important question should not be limited to the issues raised in these cases. Is it not also proper to determine the remedies available to the lessee upon the lessor's default? It is, but that issue is not reached through a review of the reported cases. This is only one of the many issues presented in structuring, negotiating and documenting a lease of goods.

Statutory Analogue:

After it was decided to proceed with the codification project, the drafting committee of the National Conference of Commissioners on Uniform State Laws looked for a statutory analogue, gradually narrowing the focus to the Article on Sales (Article 2 [Title 30, chapter 2]) and the Article on Secured Transactions (Article 9 [Title 30, chapter 9A]). A review of the literature with respect to the sale of goods reveals that Article 2 [Title 30, chapter 2] is predicated upon certain assumptions: Parties to the sales transaction frequently are without counsel; the agreement of the parties often is oral or evidenced by scant writings; obligations between the parties are bilateral; applicable law is influenced by the need to preserve freedom of contract. A review of the literature with respect to personal property security law reveals that Article 9 [Title 30, chapter 9A] is predicated upon very different assumptions: Parties to a secured transaction regularly are represented by counsel; the agreement of the parties frequently is reduced to a writing, extensive in scope; the obligations between the parties are essentially unilateral; and applicable law seriously limits freedom of contract.

The lease is closer in spirit and form to the sale of goods than to the creation of a security interest. While parties to a lease are sometimes represented by counsel and their agreement is often reduced to a writing, the obligations of the parties are bilateral and the common law of leasing is dominated by the need to preserve freedom of contract. Thus the drafting committee concluded that Article 2 [Title 30, chapter 2] was the appropriate statutory analogue.

Issues: The drafting committee then identified and resolved several issues critical to codification:

Scope: The scope of the Article was limited to leases (Section 2A-102 [30-2A-102]). There was no need to include leases intended as security, *i.e.*, security interests disguised as leases, as they are adequately treated in Article 9 [Title 30, chapter 9A]. Further, even if leases intended as security were included, the need to preserve the distinction would remain, as policy suggests treatment significantly different from that accorded leases.

Definition of Lease: Lease was defined to exclude leases intended as security (Section 2A-103(1)(j) [30-2A-103(1)(j)]). Given the litigation to date a revised definition of security interest was suggested for inclusion in the Act. (Section 1-201(37) [30-1-201(37)]). This revision sharpens the distinction between leases and security interests disguised as leases.

Filing: The lessor was not required to file a financing statement against the lessee or take any other action to protect the lessor's interest in the goods (Section 2A-301 [30-2A-301]). The refined definition of security interest will more clearly signal the need to file to potential lessors of goods. Those lessors who are concerned will file a protective financing statement (Section 9-408 [30-9-408, now repealed]).

Warranties: All of the express and implied warranties of the Article on Sales (Article 2 [Title 30, chapter 2]) were included (Sections 2A-210 through 2A-216 [30-2A-210 through 30-2A-216]), revised to reflect differences in lease transactions. The lease of goods is sufficiently similar to the sale of goods to justify this decision. Further, many courts have reached the same decision.

Certificate of Title Laws: Many leasing transactions involve goods subject to certificate of title statutes. To avoid conflict with those statutes, this Article is subject to them (Section 2A-104(1)(b) [30-2A-104(1)(b)]).

Consumer Leases: Many leasing transactions involve parties subject to consumer protection statutes. To avoid conflict with those statutes this Article is subject to them (Section 2A-104(1)(a) and (d) [30-2A-104(1)(a)]). Further, certain consumer protections have been incorporated in the Article.

Finance Leases: Certain leasing transactions substitute the seller of the goods for the lessor as the party responsible to the lessee with respect to warranties and the like. The definition of finance lease (Section 2A-103(1)(g) [30-2A-103(1)(g)]) was developed to describe these transactions. Various sections of the Article implement the substitution of the seller for the lessor, including Sections 2A-209 and 2A-407 [30-2A-209 and 30-2A-407]. No attempt was made to fashion a special rule where the finance lessor is an affiliate of the seller of goods; this is to be developed by the courts, case by case.

Sale and Leaseback: Sale and leaseback transactions are becoming increasingly common. A number of state statutes treat transactions where possession is retained by the seller as fraudulent *per se* or *prima facie* fraudulent. That position is not balanced and thus is changed by the Article "if the buyer bought for value and in good faith" (Section 2A-308(3) [30-2A-308(3)]).

Remedies: The Article has not only provided for lessor's remedies upon default by the lessee (Sections 2A-523 through 2A-531 [30-2A-523 through 30-2A-531]), but also for lessee's remedies upon default by the lessor (Sections 2A-508 through 2A-522 [30-2A-508 through 30-2A-522]). This is a significant departure from Article 9 [Title 30, chapter 9A], which provides remedies only for the secured party upon default by the debtor. This difference is compelled by the bilateral nature of the obligations between the parties to a lease.

Damages: Many leasing transactions are predicated on the parties' ability to stipulate an appropriate measure of damages in the event of default. The rule with respect to sales of goods (Section 2-718 [30-2-718]) is not sufficiently flexible to accommodate this practice. Consistent with the common law emphasis upon freedom to contract, the Article has created a revised rule that allows greater flexibility with respect to leases of goods (Section 2A-504(1) [30-2A-504(1)]).

History:

This Article is a revision of the Uniform Personal Property Leasing Act, which was approved by the National Conference of Commissioners on Uniform State Laws in August, 1985. However, it was believed that the subject matter of the Uniform Personal Property Leasing Act would be better treated as an article of this Act. Thus, although the Conference promulgated the Uniform Personal Property Leasing Act as a Uniform Law, activity was modest to allow time to restate the Uniform Personal Property Leasing Act as Article 2A [Title 30, chapter 2A].

In August, 1986 the Conference approved and recommended this Article (including conforming amendments to Article 1 and Article 9 [Title 30, chapters 1 and 9A]) for promulgation as an amendment to this Act. In December, 1986 the Council of the American Law Institute approved and recommended this Article (including conforming amendments to Article 1 and Article 9 [Title 30, chapters 1 and 9A]), with official comments, for promulgation as an amendment to this Act. In March, 1987 the Permanent Editorial Board for the Uniform Commercial Code approved and recommended this Article (including conforming amendments to Article 1 and Article 9 [Title 30, chapters 1 and 9A]), with official comments, for promulgation as an amendment to this Act. In May, 1987 the American Law Institute approved and recommended this Article (including conforming amendments to Article 1 and Article 9 [Title 30, chapters 1 and 9A]), with official comments, for promulgation as an amendment to this Act. In August, 1987 the Conference confirmed its approval of the final text of this Article.

Relationship of Article 2A [Title 30, chapter 2A] to Other Articles:

The Article on Sales provided a useful point of reference for codifying the law of leases. Many of the provisions of that Article were carried over, changed to reflect differences in style, leasing terminology or leasing practices. Thus, the official comments to those sections of Article 2 [Title 30, chapter 2] whose provisions were carried over are incorporated by reference in Article 2A [Title 30, chapter 2A], as well; further, any case law interpreting those provisions should be viewed as persuasive but not binding on a court when deciding a similar issue with respect to leases. Any change in the sequence that has been made when carrying over a provision from Article 2 [Title 30, chapter 2] should be viewed as a matter of style, not substance. This is not to suggest that in other instances Article 2A [Title 30, chapter 2A] did not also incorporate substantially revised provisions of Article 2 [Title 30, chapter 2], Article 9 [Title 30, chapter 9A] or otherwise where the revision was driven by a concern over the substance; but for the lack of a mandate, the drafting committee would have made the same or a similar change in the statutory analogue. Those sections in Article 2A [Title 30, chapter 2A] include Sections 2A-104, 2A-105, 2A-106, 2A-108(2) and (4), 2A-109(2), 2A-208, 2A-214(2) and (3)(a), 2A-216, 2A-303, 2A-306, 2A-503, 2A-504(3)(b), 2A-506(2), and 2A-515 [30-2A-104 through 30-2A-106, 30-2A-108(2) and (4), 30-2A-109(2), 30-2A-208, 30-2A-214(2) and (3)(a), 30-2A-216, 30-2A-303, 30-2A-306, 30-2A-503, 30-2A-504(3)(b), 30-2A-506(2), and 30-2A-515]. For lack of relevance or significance not all of the provisions of Article 2 [Title 30, chapter 2] were incorporated in Article 2A [Title 30, chapter 2A].

This codification was greatly influenced by the fundamental tenet of the common law as it has developed with respect to leases of goods: freedom of the parties to contract. Note that, like all other Articles of this Act, the principles of construction and interpretation contained in Article 1 [Title 30, chapter 1] are applicable throughout Article 2A [Title 30, chapter 2A] (Section 2A-103(4) [30-2A-103(4)]). These principles include the ability of the parties to vary the effect of the provisions of Article 2A [Title 30, chapter 2A], subject to certain limitations including those that relate to the obligations of good faith, diligence, reasonableness and care (Section 1-102(3) [30-1-102(3)]). Consistent with those principles no negative inference is to be drawn by the episodic use of the phrase "unless otherwise agreed" in certain provisions of Article 2A [Title 30, chapter 2A]. Section 1-102(4) [30-1-102(4)]. Indeed, the contrary is true, as the general rule in the Act, including this Article, is that the effect of the Act's provisions may be varied by agreement. Section 1-102(3) [30-1-102(3)]. This conclusion follows even where the statutory analogue contains the phrase and the correlative provision in Article 2A [Title 30, chapter 2A] does not.

30-2A-102. Scope.

Official Comment

Source: Section 2A-102, U.C.C.

Uniform Statutory Source: Section 9-102(1)[, U.C.C.]. Throughout this Article, unless otherwise stated, references to "Section" are to other sections of this Act.

Changes: Substantially revised.

Purposes: This Article governs transactions as diverse as the lease of a hand tool to an individual for a few hours and the leveraged lease of a complex line of industrial equipment to a multi-national organization for a number of years.

To achieve that end it was necessary to provide that this Article applies to any transaction, regardless of form, that creates a lease. Since lease is defined as a transfer of an interest in goods (Section 2A-103(1)(j) [30-2A-103(1)(j)]) and goods is defined to include fixtures (Section 2A-103(1)(h) [30-2A-103(1)(h)]), application is limited to the extent the transaction relates to goods, including fixtures. Further, since the definition of lease does not include a sale (Section 2-106(1) [30-2-106(1)]) or retention or creation of a security interest (Section 1-201(37) [30-1-201(37)]), application is further limited; sales and security interests are governed by other Articles of this Act.

Finally, in recognition of the diversity of the transactions to be governed, the sophistication of many of the parties to these transactions, and the common law tradition as it applies to the bailment for hire or lease, freedom of contract has been preserved. DeKoven, Proceedings After Default by the Lessee Under a True Lease of Equipment, in 1C P. Coogan, W. Hogan, D. Vagts, *Secured Transactions Under the Uniform Commercial Code,* § 29B.02[2] (1986). Thus, despite the extensive regulatory scheme established by this Article, the parties to a lease will be able to create private rules to govern their transaction. Sections 2A-103(4) [30-2A-103(4)] and 1-102(3) [30-1-102(3)]. However, there are special rules in this Article governing consumer leases, as well as other state and federal statutes, that may further limit freedom of contract with respect to consumer leases.

A court may apply this Article by analogy to any transaction, regardless of form, that creates a lease of personal property other than goods, taking into account the expressed intentions of the parties to the transaction and any differences between a lease of goods and a lease of other property. Such application has precedent as the provisions of the Article on Sales (Article 2 [Title 30, chapter 2]) have been applied by analogy to leases of goods. *E.g.*, Hawkland, *The Impact of the Uniform Commercial Code on Equipment Leasing*, 1972 Ill. L.F. 446; Murray, *Under the Spreading Analogy of Article 2 [Title 30, chapter 2] of the Uniform Commercial Code*, 39 Fordham L.Rev. 447 (1971). Whether such application would be appropriate for other bailments of personal property, gratuitous or for hire, should be determined by the facts of each case. *See Mieske v. Bartell Drug Co.*, 92 Wash.2d 40, 46-48, 593 P.2d 1308, 1312 (1979).

Further, parties to a transaction creating a lease of personal property other than goods, or a bailment of personal property may provide by agreement that this Article applies. Upholding the parties' choice is consistent with the spirit of this Article.

30-2A-103. Definitions and index of definitions.

Official Comment

Source: Section 2A-103, U.C.C.

Official Comment:

(a) "Buyer in ordinary course of business". Section 1-201(9) [30-1-201(9)].

(b) "Cancellation". Section 2-106(4) [30-2-106(4)].

(c) "Commercial unit". Section 2-105(6) [30-2-105(6)].

(d) "Conforming". Section 2-106(2) [30-2-106(2)].

(e) "Consumer lease". New. This Article includes a subset of rules that applies only to consumer leases. Sections 2A-106, 2A-108(2), 2A-108(4), 2A-109(2), 2A-221, 2A-309, 2A-406, 2A-407, 2A-504(3)(b), and 2A-516(3)(b) [30-2A-106, 30-2A-108(2) and (4), 30-2A-109(2), 30-2A-221, 30-2A-309, 30-2A-406, 30-2A-407, 30-2A-504(3)(b), and 30-2A-516(3)(b)].

For a transaction to qualify as a consumer lease it must first qualify as a lease. Section 2A-103(1)(j) [30-2A-103(1)(j)]. Note that this Article regulates the transactional elements of a lease, including a consumer lease; consumer protection statutes—present and future—are unaffected by this Article. Section 2A-104(1)(a) and (d) [30-2A-104(1)(a) and (1)(d)].

This definition is modeled after the definition of consumer lease in the Consumer Leasing Act, 15 U.S.C. § 1667 (1982), and in the Unif. Consumer Credit Code § 1.301(14), 7A U.L.A. 43 (1974). However, this definition of consumer lease differs from its models in several respects: the lessor can be a person regularly engaged either in the business of leasing or of selling goods, the lease need not be for a term exceeding four months, a lease primarily for an agricultural purpose is not covered and the limitation of $25,000 is not subject to adjustment as the Consumer Price Index changes.

This definition focuses on the parties as well as the transaction. If a lease is within this definition, the lessor must be regularly engaged in the business of leasing or selling, and the lessee must be an individual not an organization; note that a lease to two or more individuals having a common interest through marriage or the like should not be considered excluded as a lease to an organization under Section 1-201(28) [30-1-201(28)]. The lessee must take the interest primarily for a personal, family or household purpose. Further, total payments under the lease contract, excluding payments for options to renew or buy, cannot exceed $25,000.

(f) "Fault". Section 1-201(16) [30-1-201(16)].

(g) "Finance Lease". New. This Article includes a subset of rules that applies only to finance leases. Sections 2A-209, 2A-211(2), 2A-212(1), 2A-213, 2A-219(1), 2A-220(1)(a), 2A-221, 2A-405(c), 2A-407, 2A-516(2) and 2A-517(1)(a) [30-2A-209, 30-2A-211(2), 30-2A-212(1), 30-2A-213, 30-2A-219(1), 30-2A-220(1)(a), 30-2A-221, 30-2A-405(3), 30-2A-407, 30-2A-516(2), and 30-2A-517(1)(a)].

For a transaction to qualify as a finance lease it must first qualify as a lease. Section 2A-103(1)(j) [30-2A-103(1)(j)]. Unless the lessor is comfortable that the transaction will qualify as a finance lease, the lease agreement should include provisions giving the lessor the benefits created by the subset of rules applicable to the transaction that qualifies as a finance lease under this Article.

A finance lease is the product of a three party transaction. The supplier manufactures or supplies the goods pursuant to the lessee's specification, perhaps even pursuant to a purchase order, sales agreement or lease agreement between the supplier and the lessee. After the prospective finance lease is negotiated, a purchase order, sales agreement, or lease agreement is entered into by the lessor (as buyer or prime lessee) or an existing order, agreement or lease is assigned by the lessee to the lessor, and the lessor and the lessee then enter into a lease or sublease of the goods. Due to the limited function usually performed by the lessor, the lessee looks almost entirely to the supplier for representations, covenants and warranties. Yet, this definition does not restrict the lessor's function solely to the supply of funds; if the lessor undertakes or performs other functions, express warranties, covenants and the common law will protect the lessee.

This definition focuses on the transaction, not the status of the parties; to avoid confusion it is important to note that in other contexts, e.g., tax and accounting, the term finance lease has been used to connote different types of lease transactions, including leases that are disguised secured transactions. M. Rice, *Equipment Financing*, 62-71 (1981). A lessor who is a merchant with respect to goods of the kind subject to the lease may be a lessor under a finance lease. Many leases that are leases back to the seller of goods (Section 2A-308(3) [30-2A-308(3)]) will be finance leases. This conclusion is easily demonstrated by a hypothetical. Assume that B has bought goods from C pursuant to a sales contract. After delivery to and acceptance of the goods by B, B negotiates to sell the goods to A and simultaneously to lease the goods back from A, on terms and conditions that, we assume, will qualify the transaction as a lease. Section 2A-103(1)(j) [30-2A-103(1)(j)]. In documenting the sale and lease back, B assigns the original sales contract between B, as buyer, and C, as seller, to A. A review of these facts leads to the conclusion that the lease from A to B qualifies as a finance lease, as all three conditions of the definition are satisfied. Subparagraph (i) [subsection (1)(g)(i) of this section] is satisfied as A, the lessor, had nothing to do with the selection, manufacture, or supply of the equipment. Subparagraph (ii) [subsection (1)(g)(ii) of this section] is satisfied as A, the lessor, bought the equipment at the same time that A leased the equipment to B, which certainly is in connection with the lease. Finally, subparagraph (iii) [subsection (1)(g)(iii) of this section] is satisfied as A entered into the sales contract with B at the same time that A leased the equipment back to B. B, the lessee, will have received a copy of the sales contract in a timely fashion.

Subsection (i) [subsection (1)(g)(i) of this section] requires the lessor to remain outside the selection, manufacture and supply of the goods; that is the rationale for releasing the lessor from most of its traditional liability. The lessor is not prohibited from possession, maintenance or operation of the goods, as policy does not require such prohibition. To insure the lessee's reliance on the supplier, and not on the lessor, subsection (ii) [subsection (1)(g)(ii) of this section] requires that the goods (where the lessor is the buyer of the goods) or that the right to possession and use of the goods (where the lessor is the prime lessee and the sublessor of the goods) be acquired in connection with the lease (or sublease) to qualify as a finance lease. The scope of the phrase "in connection with" is to be developed by the courts, case by case. Finally, as the lessee generally relies almost entirely upon the supplier for representations, covenants and warranties with respect to the goods, subsection (iii) [subsection (1)(g)(iii) of this section] requires that the lessee receive a copy of the supply contract on or before signing the lease contract or that the lessee's approval of the supply contract is a condition to the effectiveness of the lease contract. Thus, even where oral supply orders or computer placed supply orders are compelled by custom and usage the transaction may still qualify as a finance lease if the lessee approves the supply contract before the lease contract is effective and such approval was a condition to the effectiveness of the lease contract.

If a transaction does not qualify as a finance lease, the parties may achieve the same result by agreement; no negative implications are to be drawn if the transaction does not qualify. Further, absent the application of special rules (fraud, duress, and the like), a lease that qualifies as a finance lease and is assigned by the lessor or the lessee to a third party does not lose its status as a finance lease under this Article. Finally, this Article creates no special rule where the lessor is an affiliate of the supplier; whether the transaction qualifies as a finance lease will be determined by the facts of each case.

(h) "Goods". Section 9-105(1)(h) [30-9-105(1)(h), now repealed, see 30-9A-102]. See Section 2A-103(3) [30-2A-103(3)] for reference to the definition of "Accounts", "Chattel paper", "Documents", "General intangibles" and "Instruments". See Section 2A-217 [30-2A-217] for determination of the time and manner of identification.

(i) "Installment lease contract". Section 2-612(1) [30-2-612(1)].

(j) "Lease". New. There are several reasons to codify the law with respect to leases of goods. An analysis of the case law as it applies to leases of goods suggests at least several significant issues to be resolved by codification. First and foremost is the definition of a lease. It is necessary to define lease to determine whether a transaction creates a lease or a security interest disguised as a lease. If the transaction creates a security interest disguised as a lease, the transaction will be governed by the Article on Secured Transactions (Article 9 [Title 30, chapter 9A]) and the lessor will be required to file a financing statement or take other action to perfect its interest in the goods against third parties. There is no such requirement with respect to leases under the common law and, except with respect to leases of fixtures (Section 2A-309 [30-2A-309]), this Article imposes no such requirement. Yet the distinction between a lease and a security interest disguised as a lease is not clear from the case law at the time of the promulgation of this Article. DeKoven, *Leases of Equipment: Puritan Leasing Company v. August, A Dangerous Decision*, 12 U.S.F. L.Rev. 257 (1978).

At common law a lease of personal property is a bailment for hire. While there are several definitions of bailment for hire, all require a thing to be let and a price for the letting. Thus, in modern terms and as provided in this definition, a lease is created when the lessee agrees to furnish consideration for the right to the possession and use of goods over a specified period of time. Mooney, *Personal Property Leasing: A Challenge*, 36 Bus.Law. 1605, 1607 (1981). Further, a lease is neither a sale (Section 2-106(1) [30-2-106(1)]) nor a retention or creation of a security interest (Section 1-201(37) [30-1-201(37)]). Due to extensive litigation to distinguish true leases from security interests, an amendment to Section 1-201(37) [30-1-201(37)] has been promulgated with this Article to create a sharper distinction.

This section as well as Section 1-201(37) [30-1-201(37)] must be examined to determine whether the transaction in question creates a lease or a security interest. The following hypotheticals indicate the perimeters of the issue. Assume that A has purchased a number of copying machines, new, for $1,000 each; the machines have an estimated useful economic life of three years. A advertises that the machines are available to rent for a minimum of one month and that the monthly rental is $100.00. A intends to enter into leases where A provides all maintenance, without charge to the lessee. Further, the lessee will rent the machine, month to month, with no obligation to renew. At the end of the lease term the lessee will be obligated to return the machine to A's place of business. This transaction qualifies as a lease under the first half of the definition, for the transaction includes a transfer by A to a prospective lessee of possession and use of the machine for a stated term, month to month. The machines are goods (Section 2A-103(1)(h) [30-2A-103(1)(h)]). The lessee is obligated to pay consideration in return, $100.00 for each month of the term.

However, the second half of the definition provides that a sale or a security interest is not a lease. Since there is no passing of title, there is no sale. Sections 2A-103(3) and 2-106(1) [30-2A-103(3) and 30-2-106(1)]. Under pre-Act security law this transaction would have created a bailment for hire or a true lease and not a conditional sale. *Da Rocha v. Macomber*, 330 Mass. 611, 614-15, 116 N.E.2d 139, 142 (1953). Under Section 1-201(37) [30-1-201(37)], as amended with the promulgation of this Article, the same result would follow. While the lessee is obligated to pay rent for the one month term of the lease, one of the other four conditions of the second paragraph of Section 1-201(37) [30-1-201(37)] must be met and none is. The term of the lease is one month and the economic life of the machine is 36 months; thus, subparagraph (a) of Section 1-201(37) [30-1-201(37)(a)] is not now satisfied. Considering the amount of the monthly rent, absent economic duress or coercion, the lessee is not bound either to renew the lease for the remaining economic life of the goods or to become the owner. If the lessee did lease the machine for 36 months, the lessee would have paid the lessor $3,600 for a machine that could have been purchased for $1,000; thus, subparagraph (b) of Section 1-201(37) [30-1-201(37)(b)] is not satisfied. Finally, there are no options; thus, subparagraphs (c) and (d) of Section 1-201(37) [30-1-201(37)(c) and (37)(d)] are not satisfied. This transaction creates a lease, not a security interest. However, with each renewal of the lease the facts and circumstances at the time of each renewal must be examined to determine if that conclusion remains accurate, as it is possible that a transaction that first creates a lease, later creates a security interest.

Assume that the facts are changed and that A requires each lessee to lease the goods for 36 months, with no right to terminate. Under pre-Act security law this transaction would have created a conditional sale, and not a bailment for hire or true lease. *Hervey v. Rhode Island Locomotive Works*, 93 U.S. 664, 672-73 (1876). Under this subsection, and Section 1-201(37) [30-1-201(37)], as amended with the inclusion of this Article in the Act, the same result would follow. The lessee's obligation for the term is not subject to termination by the lessee and the term is equal to the economic life of the machine.

Between these extremes there are many transactions that can be created. Some of the transactions have not been properly categorized by the courts in applying the 1978 and earlier Official Texts of Section 1-201(37) [30-1-201(37)]. This subsection, together with Section 1-201(37) [30-1-201(37)], as amended with the promulgation of this Article, draws a brighter line, which should create a clearer signal to the professional lessor and lessee.

(k) "Lease agreement". This definition is derived from the first sentence of Section 1-201(3) [30-1-201(3)]. Because the definition of lease is broad enough to cover future transfers, lease agreement includes an agreement contemplating a current or subsequent transfer. Thus it was not necessary to make an express reference to an agreement for the future lease of goods (Section 2-106(1) [30-2-106(1)]). This concept is also incorporated in the definition of lease contract. Note that the definition of lease does not include transactions in ordinary building materials that are incorporated into an improvement on land. Section 2A-309(2) [30-2A-309(2)].

The provisions of this Article, if applicable, determine whether a lease agreement has legal consequences; otherwise the law of bailments and other applicable law determine the same. Sections 2A-103(4) and 1-103 [30-2A-103(4) and 30-1-103].

(l) "Lease contract". This definition is derived from the definition of contract in Section 1-201(11) [30-1-201(11)]. Note that a lease contract may be for the future lease of goods, since this notion is included in the definition of lease.

(m) "Leasehold interest". New.

(n) "Lessee". New.

(o) "Lessee in ordinary course of business". Section 1-201(9) [sic. New.].

(p) "Lessor". New.

(q) "Lessor's residual interest". New.

(r) "Lien". New. This term is used in Section 2A-307 [30-2A-307] (Priority of Liens Arising by Attachment or Levy on, Security Interests in, and Other Claims to Goods).

(s) "Lot". Section 2-105(5) [30-2-105(5)].

(t) "Merchant lessee". New. This term is used in Section 2A-511 [30-2A-511] (Merchant Lessee's Duties as to Rightfully Rejected Goods). A person may satisfy the requirement of dealing in goods of the kind subject to the lease as lessor, lessee, seller, or buyer.

(u) "Present value". New. Authorities agree that present value should be used to determine fairly the damages payable by the lessor or the lessee on default. *E.g.*, *Taylor v. Commercial Credit Equip. Corp.*, 170 Ga.App. 322, 316 S.E.2d 788 (Ct.App.1984). Present value is defined to mean an amount that represents the discounted value as of a date certain of one or more sums payable in the future. This is a function of the economic principle that a dollar today is more valuable to the holder than a dollar payable in two years. While there is no question as to the principle, reasonable people would differ as to the rate of discount to apply in determining the value of that future dollar today. To minimize litigation, this Article allows the parties to specify the discount or interest rate, if the rate was not manifestly unreasonable at the time the transaction was entered into. In all other cases, the interest rate will be a commercially reasonable rate that takes into account the facts and circumstances of each case, as of the time the transaction was entered into.

(v) "Purchase". Section 1-201(32) [30-1-201(32)]. This definition omits the reference to lien contained in the definition of purchase in Article 1 [Title 30, chapter 1] (Section 1-201(32) [30-1-201(32)]). This should not be construed to exclude consensual liens from the definition of purchase in this Article; the exclusion was mandated by the scope of the definition of lien in Section 2A-103(1)(r) [30-2A-103(1)(r)]. Further, the definition of purchaser in this Article adds a reference to lease; as purchase is defined in Section 1-201(32) [30-2A-201(32)] to include any other voluntary transaction creating an interest in property, this addition is not substantive.

(w) "Sublease". New.

(x) "Supplier". New.

(y) "Supply contract". New.

(z) "Termination". Section 2-106(3) [30-2-106(3)].

Compiler's Comments

2013 Amendment: Chapter 75 in (3)(m) substituted "30-9A-102(1)(qqq)" for "30-9A-102(1)(ppp)". Amendment effective July 1, 2013.

Saving Clause: Section 26, Ch. 75, L. 2013, provided: "(1) Except as otherwise provided in [sections 19 through 25] [Title 30, chapter 9A, part 8], this chapter applies to a transaction or lien within its scope, even if the transaction or lien was entered into or created before [the effective of this act] [July 1, 2013].

(2) This chapter does not affect an action, case, or proceeding commenced before [the effective date of this act] [July 1, 2013]."

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

2005 Amendment: Chapter 575 in definition of buyer in ordinary course of business near middle of second sentence substituted "acquiring" for "receiving"; in definition of lessee at end substituted "sublease" for "sublessee"; in definition of lessee in ordinary course of business in second sentence substituted "acquiring" for "receiving"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

1999 Amendment: Chapter 305 in (3) in reference to "account" substituted "30-9-122(1)(b)" (renumbered 30-9A-102(1)(b)) for "30-9-106", in reference to "chattel paper" substituted "30-9-122(1)(k)" (renumbered 30-9A-102(1)(k)) for "30-9-105(1)(b)", in reference to "consumer goods" substituted "30-9-122(1)(w)" (renumbered 30-9A-102(1)(w)) for "30-9-109(1)", in reference to "document" substituted "30-9-122(1)(dd)" (renumbered 30-9A-102(1)(dd)) for "30-9-105(1)(f)", in reference to "general intangible" substituted "30-9-122(1)(pp)" (renumbered 30-9A-102(1)(pp)) for "30-9-106", in reference to "instrument" substituted "30-9-122(1)(uu)" (renumbered 30-9A-102(1)(uu)) for "30-9-105(1)(i)", and in reference to "mortgage" substituted "30-9-122(1)(ccc)" (renumbered 30-9A-102(1)(ccc)) for "30-9-105(1)(j)"; and made minor changes in style. Amendment effective July 1, 2001.

Case Notes

Principal's Impairment or Suspension of Rights of Guarantor — Exoneration of Guarantor Proper: Ace Leasing, Inc. (Ace), funded a lease to O'Neill for $45,000 for business equipment. Boustead was guarantor of the lease agreement. If O'Neill failed to perform, the lease provided that Ace could proceed directly against Boustead. O'Neill failed to make timely payments. Ace canceled the lease. O'Neill and Ace then discussed the matter, and O'Neill explained that the late payments were the result of the late arrival of the ordered equipment. Ace agreed to accept several late payments, but Boustead was not part of the negotiations. O'Neill again missed several payments, and Ace requested that Boustead pay off the lease. Boustead refused to pay on grounds that the cancellation letter and acceptance of late payments without Boustead's knowledge, as well as the method of purchasing the equipment, constituted a material change in the agreement and in Boustead's obligations as guarantor. The District Court agreed and exonerated Boustead as guarantor under 28-11-211. The court also held that Boustead's risk was increased because Ace did not own the equipment, so the transaction between Ace and O'Neill constituted a loan rather than a lease. Ace appealed the findings regarding ownership and alteration of the agreement. The Supreme Court affirmed. Under 30-2-401, the title of goods passes to the buyer at the time that and place at which the seller completes performance with reference to physical delivery of the goods, unless the agreement provides otherwise. Here, neither Ace nor O'Neill conformed to the purchase provision of the agreement. Because Ace failed to obtain title, Ace could not assume the role of lessor and, while retaining title and ownership, transfer to O'Neill merely the right of possession and use of the equipment, so the transaction effectively became a loan agreement between the parties with O'Neill holding title to the equipment according to the default provisions of the Uniform Commercial Code. Further, Ace's actions in accepting late payments after canceling the agreement and in failing to comply with the terms of the lease requiring Ace to purchase the equipment and retain ownership to secure its interest were a material alteration in the agreement as affecting Boustead. Ace impaired or suspended its rights and remedies against O'Neill and, without Boustead's consent, impaired or suspended Boustead's rights as well, which was sufficient to exonerate Boustead as guarantor under 28-11-211. Ace Leasing, Inc. v. Boustead, 2002 MT 213, 311 M 285, 55 P3d 371 (2002).

30-2A-104. Leases subject to other law.

Official Comment

Source: Section 2A-104, U.C.C.

Uniform Statutory Source: Sections 9-203(4) and 9-302(3)(b) and (c)[, U.C.C.].

Changes: Substantially revised.

Purposes: This Article creates a comprehensive scheme for the regulation of transactions that create leases. Section 2A-102 [30-2A-102]. Thus, the Article supersedes all prior legislation dealing with leases, except to the extent set forth in this Section.

Subsection (1) states the general rule that a lease, although governed by the scheme of this Article, is also governed by certain other applicable statutes. This may occur in the case of a consumer lease. Section 2A-103(1)(e) [30-2A-103(1)(e)].

An illustration of a statute of the United States that governs consumer leases is the Consumer Leasing Act, 15 U.S.C. §§ 1667-1667(e) (1982) and its implementing regulation, Regulation M, 12 C.F.R. §§ 213 (1986); the statute mandates disclosures of certain lease terms, delimits the liability of a lessee in leasing personal property, and regulates the advertising of lease terms. An illustration of a state statute that governs consumer leases is the Unif. Consumer Credit Code, which includes many provisions similar to those of the Consumer Leasing Act, *e.g.*, Unif. Consumer Credit Code §§ 3.202, 3.209, 3.401, 7A U.L.A. 108-09, 115, 125 (1974), as well as provisions in addition to those of the Consumer Leasing Act, *e.g.*, Unif. Consumer Credit Code §§ 5.109-.111, 7A U.L.A. 171-76 (1974) (the right to cure a default). Such statutes may define consumer lease so as to govern transactions within and without the definition of consumer lease under this Article.

Under subsection (2), subject to certain limited exclusions, in case of conflict the provisions of such a statute prevail over the provisions of this Article. For example, a provision like Unif. Consumer Credit Code, § 5.112, 7A U.L.A. 176 (1974), limiting self-help repossession, prevails over Section 2A-525(3) [30-2A-525(3)].

Consumer protection in lease transactions is primarily left to other law. However, several provisions of this Article do contain special rules that may not be varied by agreement in the case of a consumer lease. *E.g.*, Sections 2A-106, 2A-108, and 2A-109(2) [30-2A-106, 30-2A-108, and 30-2A-109(2)]. Were that not so, the ability of the parties to govern their relationship by agreement together with the position of the lessor in a consumer lease too often could result in a one-sided lease agreement.

In construing this provision the reference to statute should be deemed to include applicable regulations.

30-2A-105. Territorial application of chapter to goods covered by certificate of title.

Official Comment

Source: Section 2A-105, U.C.C.

Uniform Statutory Source: Section 9-103(2)(a) and (b)[, U.C.C.].

Changes: Substantially revised. The provisions of the last sentence of Section 9-103(2)(b) [30-9-103(2)(b), now repealed, see 30-9A-303] have not been incorporated as it is superfluous in this context. The provisions of Section 9-103(2)(d) [30-9-103(2)(d), now repealed, see 30-9A-337] have not been incorporated because the problems dealt with are adequately addressed by this section and Sections 2A-304(3) and 305(3) [30-2A-304(3) and 30-2A-305(3)].

Purposes: The new certificate referred to in (b) [subsection (2) of this section] must be permanent, not temporary. Generally, the lessor or creditor whose interest is indicated on the most recently issued certificate of title will prevail over interests indicated on certificates issued previously by other jurisdictions. This provision reflects a policy that it is reasonable to require holders of interests in goods covered by a certificate of title to police the goods or risk losing their interests when a new certificate of title is issued by another jurisdiction.

30-2A-106. Limitation on power of parties to consumer lease to choose applicable law and judicial forum.

Official Comment

Source: Section 2A-106, U.C.C.

Uniform Statutory Source: Unif. Consumer Credit Code § 1.201(8), 7A U.L.A. 36 (1974).

Changes: Substantially revised.

Purposes: There is a real danger that a lessor may induce a consumer lessee to agree that the applicable law will be a jurisdiction that has little effective consumer protection, or to agree that the applicable forum will be a forum that is inconvenient for the lessee in the event of litigation. As a result, this section invalidates these choice of law or forum clauses, except where the law chosen is that of the state of the consumer's residence or where the goods will be kept, or the forum chosen is one that otherwise would have jurisdiction over the lessee.

Subsection (1) limits potentially abusive choice of law clauses in consumer leases. The 30-day rule in subsection (1) was suggested by Section 9-103(1)(c) [30-9-103(1)(c), now repealed]. This section has no effect on choice of law clauses in leases that are not consumer leases. Such clauses would be governed by other law.

Subsection (2) prevents enforcement of potentially abusive jurisdictional consent clauses in consumer leases. By using the term judicial forum, this section does not limit selection of a nonjudicial forum, such as arbitration. This section has no effect on choice of forum clauses in leases that are not consumer leases; such clauses are, as a matter of current law, "prima facie valid". *The Bremen v. Zapata Off-Shore, Co.*, 407 U.S. 1, 10 (1972). Such clauses would be governed by other law, including the Model Choice of Forum Act (1968).

30-2A-107. Waiver or renunciation of claim or right after default.

Official Comment

Source: Section 2A-107, U.C.C.

Uniform Statutory Source: Section 1-107[, U.C.C.].

Changes: Revised to reflect leasing practices and terminology. This clause is used throughout the official comments to this Article to indicate the scope of change in the provisions of the Uniform Statutory Source included in the section; these changes range from one extreme, *e.g.*, a significant difference in practice (a warranty as to merchantability is not implied in a finance lease (Section 2A-212 [30-2A-212])) to the other extreme, *e.g.*, a modest difference in style or terminology (the transaction governed is a lease not a sale (Section 2A-203 [30-2A-203])).

30-2A-108. Unconscionability.

Official Comment

Source: Section 2A-108, U.C.C.

Uniform Statutory Source: Section 2-302[, U.C.C.] and Unif. Consumer Credit Code § 5.108, 7A U.L.A. 167-69 (1974).

Changes: Subsection (1) is taken almost verbatim from the provisions of Section 2-302(1) [30-2-302(1)]. Subsection (2) is suggested by the provisions of Unif. Consumer Credit Code § 5.108(1), (2), 7A U.L.A. 167 (1974). Subsection (3), taken from the provisions of Section 2-302(2) [30-2-302(2)], has been expanded to cover unconscionable conduct. Unif. Consumer Credit Code § 5.108(3), 7A U.L.A. 167 (1974). The provision for the award of attorney's fees to consumers, subsection (4), covers unconscionability under subsection (1) as well as (2). Subsection (4) is modeled on the provisions of Unif. Consumer Credit Code § 5.108(6), 7A U.L.A. 169 (1974).

Purposes: Subsections (1) and (3) of this section apply the concept of unconscionability reflected in the provisions of Section 2-302 [30-2-302] to leases. *See Dillman & Assocs. v. Capitol Leasing Co.*, 110 Ill.App.3d 335, 342, 442 N.E.2d 311, 316 (App.Ct.1982). Subsection (3) omits the adjective "commercial" found in subsection 2-302(2) [30-2-302(2)] because subsection (3) is concerned with all leases and the relevant standard of conduct is determined by the context.

The balance of the section is modeled on the provisions of Unif. Consumer Credit Code § 5.108, 7A U.L.A. 167-69 (1974). Thus subsection (2) recognizes that a consumer lease or a clause in a consumer lease may not itself be unconscionable but that the agreement would never have been entered into if unconscionable means had not been employed to induce the consumer to agree. To make a statement to induce the consumer to lease the goods, in the expectation of invoking an integration clause in the lease to exclude the statement's admissibility in a subsequent dispute, may be unconscionable. Subsection (2) also provides a consumer remedy for unconscionable conduct, such as using or threatening to use force or violence, in the collection of a claim arising from a lease contract. These provisions are not exclusive. The remedies of this section are in addition to remedies otherwise available for the same conduct under other law, for example, an action in tort for abusive debt collection or under another statute of this State for such conduct. The reference to appropriate relief in subsection (2) is intended to foster liberal administration of this remedy. Sections 2A-103(4) and 1-106(1) [30-2A-103(4) and 30-1-106(1)].

Subsection (4) authorizes an award of reasonable attorney's fees if the court finds unconscionability with respect to a consumer lease under subsections (1) or (2). Provision is also made for recovery by the party against whom the claim was made if the court does not find unconscionability and does find that the consumer knew the action to be groundless. Further, subsection (4)(b) is independent of, and thus will not override, a term in the lease agreement that provides for the payment of attorney's fees.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

30-2A-109. Option to accelerate at will.

Official Comment

Source: Section 2A-109, U.C.C.

Uniform Statutory Source: Section 1-208[, U.C.C.] and Unif. Consumer Credit Code § 5.109(2), 7A U.L.A. 171 (1974).

Purposes: Subsection (1) reflects modest changes in style to the provisions of the first sentence of Section 1-208 [30-1-208].

Subsection (2), however, reflects a significant change in the provisions of the second sentence of Section 1-208 [30-1-208] by creating a new rule with respect to a consumer lease. A lease provision allowing acceleration at the will of the lessor or when the lessor deems itself insecure is of critical importance to the lessee. In a consumer lease it is a provision that is not usually agreed to by the parties but is usually mandated by the lessor. Therefore, where its invocation depends not on specific criteria but on the discretion of the lessor, its use should be regulated to prevent abuse. Subsection (1) imposes a duty of good faith upon its exercises. Subsection (2) shifts the burden of establishing good faith to the lessor in the case of a consumer lease, but not otherwise.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

Part 2

Formation and Construction of Lease Contract

30-2A-201. Statute of frauds.

Official Comment

Source: Section 2A-201, U.C.C.

Uniform Statutory Source: Sections 2-201, 9-203(1) and 9-110[, U.C.C.].

Changes: This section is modeled on Section 2-201 [30-2-201], with changes to reflect the differences between a lease contract and a contract for the sale of goods. In particular, subsection (1)(b) adds a requirement that the writing "describe the goods leased and the lease term", borrowing that concept, with revisions, from the provisions of Section 9-203(1)(a) [30-9-203(1)(a), now repealed, see 30-9A-203]. Subsection (2), relying on the statutory analogue in Section 9-110 [30-9-110, now repealed, see 30-9A-108], sets forth the minimum criterion for satisfying that requirement.

Purposes: The changes in this section conform the provisions of Section 2-201 [30-2-201] to custom and usage in lease transactions. Section 2-201(2) [30-2-201(2)], stating a special rule between merchants, was not included in this section as the number of such transactions involving leases, as opposed to sales, was thought to be modest. Subsection (4) creates no exception for transactions where payment has been made and accepted. This represents a departure from the analogue, Section 2-201(3)(c) [30-2-201(3)(c)]. The rationale for the departure is grounded in the distinction between sales and leases. Unlike a buyer in a sales transaction, the lessee does not tender payment in full for goods delivered, but only payment of rent for one or more months. It was decided that, as a matter of policy, this act of payment is not a sufficient substitute for the required memorandum. Subsection (5) was needed to establish the criteria for supplying the lease term if it is omitted, as the lease contract may still be enforceable under subsection (4).

Case Notes

Lessor Fully Compensated for Loss of Truck Under Rental Agreement — Agreed Value of Truck Inapplicable to Damage Claim: Plaintiff leased a truck to defendant for construction work. The truck had an agreed value of $250,000 and a rental rate of $12,000 a month. While in defendant's possession, the truck was heavily damaged. Plaintiff initially sought to repair the truck, but eventually it was stripped of usable parts, and the remaining shell was sold for $15,000. Plaintiff received $114,500 from its insurer, based on the insurer's calculation that the truck had a $126,000 cash replacement value minus the $2,500 policy deductible owed to plaintiff by defendant and minus a $9,000 salvage value. Plaintiff then sued defendant for the unpaid balance of the agreed value, including the monthly payments because the agreed value had not been paid. The District Court noted that even though the parties did not have a signed, enforceable, written contract, defendant had properly insured the truck pursuant to a reasonable lease term, identifying plaintiff as beneficiary, and held that defendant had no independent obligation to pay damages beyond the deductible. Because plaintiff had recovered all damages to which it was entitled, judgment was entered for defendant, and plaintiff appealed. The Supreme Court found that the language of the rental agreement did not require the lessee to pay the agreed value if the truck was damaged or destroyed, so defendant was not liable for the agreed value. Plaintiff failed to show the actual replacement cost of the truck and failed to establish that the District Court's finding was clearly erroneous, so the court did not err in holding that plaintiff was not entitled to additional compensation for replacing the truck. Additionally, plaintiff did not demonstrate what additional rental payments were owed, so defendant had no further obligation to pay damages for loss of use. The District Court did not err in holding that plaintiff was fully compensated under the rental agreement, and judgment was affirmed. Performance Mach. Co., Inc. v. Yellowstone Mtn. Club, LLC, 2007 MT 250, 339 M 259, 169 P3d 394 (2007).

30-2A-202. Final written expression — parol or extrinsic evidence.

Official Comment

Source: Section 2A-202, U.C.C.

Uniform Statutory Source: Section 2-202[, U.C.C.].

30-2A-203. Seals inoperative.

Official Comment

Source: Section 2A-203, U.C.C.

Uniform Statutory Source: Section 2-203[, U.C.C.].

Changes: Revised to reflect leasing practices and terminology.

30-2A-204. Formation in general.

Official Comment

Source: Section 2A-204, U.C.C.

Uniform Statutory Source: Section 2-204[, U.C.C.].

Changes: Revised to reflect leasing practices and terminology.

30-2A-205. Firm offers.

Official Comment

Source: Section 2A-205, U.C.C.

Uniform Statutory Source: Section 2-205[, U.C.C.].

Changes: Revised to reflect leasing practices and terminology.

30-2A-206. Offer and acceptance in formation of lease contract.

Official Comment

Source: Section 2A-206, U.C.C.

Uniform Statutory Source: Section 2-206(1)(a) and (2)[, U.C.C.].

Changes: Revised to reflect leasing practices and terminology.

30-2A-207. Course of performance or practical construction.

Official Comment

Source: Section 2A-207, U.C.C.

Uniform Statutory Source: Sections 2-208 and 1-205(4)[, U.C.C.].

Changes: Revised to reflect leasing practices and terminology, except that subsection (2) was further revised to make the subsection parallel the provisions of Section 1-205(4) [30-1-205(4)] by adding that course of dealing controls usage of trade.

Purposes: The section should be read in conjunction with Section 2A-208 [30-2A-208]. In particular, although a specific term may control over course of performance as a matter of lease construction under subsection (2), subsection (3) allows the same course of dealing to show a waiver or modification, if Section 2A-208 [30-2A-208] is satisfied.

30-2A-208. Modification, rescission, and waiver.

Official Comment

Source: Section 2A-208, U.C.C.

Uniform Statutory Source: Section 2-209[, U.C.C.].

Changes: Revised to reflect leasing practices and terminology, except that the provisions of subsection 2-209(3) [30-2-209(3)] were omitted.

Purposes: Section 2-209(3) [30-2-209(3)] provides that "the requirements of the statute of frauds section of this Article (Section 2-201 [30-2-201]) must be satisfied if the contract as modified is within its provisions." This provision was not incorporated as it is unfair to allow an oral modification to make the entire lease contract unenforceable, *e.g.*, if the modification takes it a few dollars over the dollar limit. At the same time, the problem could not be solved by providing that the lease contract would still be enforceable in its pre-modification state (if it then satisfied the statute of frauds) since in some cases that might be worse than no enforcement at all. Resolution of the issue is left to the courts based on the facts of each case.

30-2A-209. Lessee under finance lease as beneficiary of supply contract.

Official Comment

Source: Section 2A-209, U.C.C.

Changes: This section is modeled on Section 9-318 [30-9-318, now repealed, see 30-9A-404 through 30-9A-406], the Restatement (Second) of Contracts §§ 302-315 (1981), and leasing practices. *See Earman Oil Co. v. Burroughs Corp.*, 625 F.2d 1291, 1296-97 (5th Cir.1980).

Purposes: The function performed by the lessor in a finance lease is extremely limited. Section 2A-103(1)(g) [30-2A-103(1)(g)]. The lessee looks to the supplier of the goods for warranties and the like. That expectation is reflected in subsection (1), which is self-executing. As a matter of policy, the operation of this provision may not be excluded, modified or limited; however, an exclusion, modification, or limitation of any term of the supply contract, including any with respect to rights and remedies, effective against the lessor as buyer under the supply contract, is also effective against the lessee as the beneficiary designated under this provision. The supplier is not precluded from excluding or modifying an express or implied warranty under a supply contract. Sections 2-312(2) and 2-316 [30-2-312(2) and 30-2-316]. Further, the supplier is not precluded from limiting the rights and remedies of the lessor, as buyer, and from liquidating damages. Sections 2-718 and 2-719 [30-2-718 and 30-2-719]. If the supply contract excludes or modifies warranties, limits remedies for breach, or liquidates damages with respect to the lessor, such provisions are enforceable against the lessee as beneficiary. Thus, only selective discrimination against the beneficiaries designated under this section is precluded, *i.e.*, exclusion of the supplier's liability to the lessee with respect to warranties made to the lessor.

Enforcement of this benefit is by action. Sections 2A-103(4) and 1-106(2) [30-2A-103(4) and 30-1-106(2)].

The benefit extended by these provisions is not without a price, as this Article also provides in the case of a finance lease that is not a consumer lease that the lessee's promises to the lessor under the lease contract become irrevocable and independent upon the lessee's acceptance of the goods. Section 2A-407 [30-2A-407].

Subsection (2) limits the effect of subsection (1) on the supplier and the lessor by preserving, notwithstanding the transfer of the benefits of the supply contract to the lessee, all of the supplier's and the lessor's rights and obligations with respect to each other and others; it further absolves the lessee of any duties with respect to the supply contract that might have been inferred from the extension of the benefits thereof.

Subsections (2) and (3) also deal with difficult issues related to modification or rescission of the supply contract. Subsection (2) states a rule that determines the impact of the statutory extension of benefit contained in subsection (1) upon the relationship of the parties to the supply contract and, in a limited respect, upon the lessee. This statutory extension of benefit, like that contained in Sections 2A-216 and 2-318 [30-2A-216 and 30-2-318], is not a modification of the supply contract by the parties. Thus, subsection (3) states the rules that apply to a modification or rescission of the supply contract by the parties. Subsection (3) recognizes the lessee's potential causes of action against the lessor and the supplier arising from modification or rescission of the supply contract. The existence and extent of a cause of action by the supplier against the lessor is left to resolution by the courts based on the facts of each case.

30-2A-210. Express warranties.

Official Comment

Source: Section 2A-210, U.C.C.

Uniform Statutory Source: Section 2-313[, U.C.C.].

Changes: Revised to reflect leasing practices and terminology.

Purposes: All of the express and implied warranties of the Article on Sales (Article 2 [Title 30, chapter 2]) are included in this Article, revised to reflect the differences between a sale of goods and a lease of goods. Sections 2A-210 through 2A-216 [30-2A-210 through 30-2A-216]. The lease of goods is sufficiently similar to the sale of goods to justify this decision. Hawkland, *The Impact of the Uniform Commercial Code on Equipment Leasing*, 1972 Ill.L.F. 446, 459-60. Many state and federal courts have reached the same conclusion.

Value of the goods, as used in subsection (2), includes rental value.

30-2A-211. Warranties against interference and against infringement — lessee's obligation against infringement.

Official Comment

Source: Section 2A-211, U.C.C.

Uniform Statutory Source: Section 2-312[, U.C.C.].

Changes: This section is modeled on the provisions of Section 2-312 [30-2-312], with modifications to reflect the limited interest transferred by a lease contract and the total interest transferred by a sale. Section 2-312(2) [30-2-312(2)], which is omitted here, is incorporated in Section 2A-214 [30-2A-214]. The warranty of quiet possession was abolished with respect to sales of goods. Section 2-312 [30-2-312] official comment 1. Section 2A-211(1) [30-2A-211(1)] reinstates the warranty of quiet possession with respect to leases. Inherent in the nature of the limited interest transferred by the lease—the right to possession and use of the goods—that is the need of the lessee for protection greater than that afforded to the buyer. Since the scope of the protection is limited to claims or interests that arose from acts or omissions of the lessor, the lessor will be in position to evaluate the potential cost, certainly a far better position than that enjoyed by the lessee. Further, to the extent the market will allow, the lessor can attempt to pass on the anticipated additional cost to the lessee in the guise of higher rent.

Purposes: General language was chosen for subsection (1) that expresses the essence of the lessee's expectation: with an exception for infringement and the like, no person holding a claim or interest that arose from an act or omission of the lessor will be able to interfere with the lessee's use and enjoyment of the goods for the lease term. Subsection (2), like other similar provisions in later sections, excludes the finance lessor from extending this warranty; with few exceptions (Sections 2A-210 and 2A-211(1) [30-2A-210 and 30-2A-211(1)]), the lessee under a finance lease is to look to the supplier for warranties and the like. Subsections (2) and (3) are derived from Section 2-312(3) [30-2-312(3)]. These subsections, as well as the analogue, should be construed so that applicable principles of law and equity supplement their provisions. Sections 2A-103(4) and 1-103 [30-2A-103(4) and 30-1-103].

30-2A-212. Implied warranty of merchantability.

Official Comment

Source: Section 2A-212, U.C.C.

Uniform Statutory Source: Section 2-314[, U.C.C.].

Changes: Revised to reflect leasing practices and terminology. *E.g., Glenn Dick Equip. Co. v. Galey Constr., Inc.,* 97 Idaho 216, 225, 541 P.2d 1184, 1193 (1975) (implied warranty of merchantability (Article 2 [Title 30, chapter 2]) extends to lease transactions).

30-2A-213. Implied warranty of fitness for particular purpose.

Official Comment

Source: Section 2A-213, U.C.C.

Uniform Statutory Source: Section 2-315[, U.C.C.].

Changes: Revised to reflect leasing practices and terminology. *E.g., All-States Leasing Co. v. Bass,* 96 Idaho 873, 879, 538 P.2d 1177, 1183 (1975) (implied warranty of fitness for a particular purpose (Article 2 [Title 30, chapter 2]) extends to lease transactions).

Case Notes

Condition of Rental Equipment Not Misrepresented: Carl Weissman & Sons (CWS) agreed to rent a rock drill to D&L Thomas Equipment (D&L). A clause in the rental agreement required D&L to inspect the drill and notify CWS within 10 days specifying any defects and provided that if CWS was not notified, the drill would be conclusively presumed to have been accepted in its condition at the time of receipt. D&L contended that there were problems with the drill immediately after it was received, but did not notify CWS in writing within the 10-day period specified in the rental agreement. D&L asserted that CWS violated this section by delivering the drill in a condition not fit for its intended purpose and misrepresenting the condition of the drill. However, by accepting the drill in its condition upon receipt, D&L waived all warranties. Even if CWS had misrepresented the condition of the drill, D&L was required to assess its condition upon receipt and, under the contract terms, could not rely on previous representations by CWS. Carl Weissman & Sons, Inc. v. D&L Thomas Equip. Corp., 1998 MT 213, 290 M 433, 963 P2d 1263, 55 St. Rep. 896 (1998).

30-2A-214. Exclusion or modification of warranties.

Official Comment

Source: Section 2A-214, U.C.C.

Uniform Statutory Source: Sections 2-316 and 2-312(2)[, U.C.C.].

Changes: Subsection (2) requires that a disclaimer of the warranty of merchantability be conspicuous and in writing as is the case for a disclaimer of the warranty of fitness; this is contrary to the rule stated in Section 2-316(2) [30-2-316(2)] with respect to the disclaimer of the warranty of merchantability. This section also provides that to exclude or modify the implied warranty of merchantability, fitness or against interference or infringement the language must be in writing and conspicuous. There are, however, exceptions to the rule. *E.g.,* course of dealing, course of performance, or usage of trade may exclude or modify an implied warranty. Section 2A-214(3)(c) [30-2A-214(3)(c)]. The analogue of Section 2-312(2) [30-2-312(2)] has been moved to subsection (4) of this section for a more unified treatment of disclaimers; there is no policy with respect to leases of goods that would justify continuing certain distinctions found in the Article on Sales (Article 2 [Title 30, chapter 2]) regarding the treatment of the disclaimer of various warranties. *Compare* Sections 2-312(2) and 2-316(2) [30-2-312(2) and 30-2-316(2)]. Finally, the example of a disclaimer of the implied warranty of fitness stated in subsection (2) differs from the analogue stated in Section 2-316(2) [30-2-316(2)]; this example should promote a better understanding of the effect of the disclaimer.

Purposes: These changes were made to reflect leasing practices. *E.g., FMC Finance Corp. v. Murphree,* 632 F.2d 413, 418 (5th Cir. 1980) (disclaimer of implied warranty under lease transactions must be conspicuous and in writing). The omission of the provisions of Section 2-316(4) [30-2-316(4)] was not substantive. Sections 2A-503 and 2A-504 [30-2A-503 and 30-2A-504].

30-2A-215. Cumulation and conflict of warranties express or implied.

Official Comment

Source: Section 2A-215, U.C.C.

Uniform Statutory Source: Section 2-317[, U.C.C.].

30-2A-216. Third-party beneficiaries of express and implied warranties.

Official Comment

Source: Section 2A-216, U.C.C.

Uniform Statutory Source: Section 2-318[, U.C.C.].

Changes: The provisions of Section 2-318 [30-2-318] have been included in this section, modified in two respects: first, to reflect leasing practice, including the special practices of the lessor under a finance lease; second, to reflect and thus codify elements of the official comment to Section 2-318 [30-2-318] with respect to the effect of disclaimers and limitations of remedies against third parties.

Purposes: Alternative A is based on the 1962 version of Section 2-318 [30-2-318] and is least favorable to the injured person as the doctrine of privity imposed by other law is abrogated to only a limited extent. Alternatives B and C are based on later additions to Section 2-318 [30-2-318] and are more favorable to the injured person. In determining which alternative to select, the state legislature should consider making its choice parallel to the choice it made with respect to Section 2-318 [30-2-318], as interpreted by the courts.

The last sentence of each of Alternatives A, B and C does not preclude the lessor from excluding or modifying an express or implied warranty under a lease. Section 2A-214 [30-2A-214]. Further, that sentence does not preclude the lessor from limiting the rights and remedies of the lessee and from liquidating damages. Sections 2A-503 and 2A-504 [30-2A-503 and 30-2A-504]. If the lease excludes or modifies warranties, limits remedies for breach, or liquidates damages with respect to the lessee, such provisions are enforceable against the beneficiaries designated under this section. However, this last sentence forbids selective discrimination against the beneficiaries designated under this section, *i.e.*, exclusion of the lessor's liability to the beneficiaries with respect to warranties made by the lessor to the lessee.

Other law, including the Article on Sales (Article 2 [Title 30, chapter 2]), may apply in determining the extent to which a warranty to or for the benefit of the lessor extends to the lessee and third parties. This is in part a function of whether the lessor has bought or leased the goods.

This Article does not purport to change the development of the relationship of the common law, with respect to products liability, including strict liability in tort (as restated in Restatement (Second) of Torts, § 402A (1965)), to the provisions of this Act. Compare *Cline v. Prowler Indus. of Maryland*, 418 A.2d 968 (Del.1980) and *Hawkins Constr. Co. v. Matthews Co.*, 190 Neb. 546, 209 N.W.2d 643 (1973) with *Dippel v. Sciano*, 37 Wis.2d 443, 155 N.W.2d 55 (1967).

30-2A-217. Identification.

Official Comment

Source: Section 2A-217, U.C.C.

Uniform Statutory Source: Section 2-501[, U.C.C.].

Changes: This section, together with Section 2A-218 [30-2A-218], is derived from the provisions of Section 2-501 [30-2-501], with changes to reflect lease terminology; however, this section omits as irrelevant to leasing practice the treatment of special property.

Purposes: With respect to subsection (b) [subsection (2) of this section] there is a certain amount of ambiguity in the reference to when goods are designated, *e.g.*, when the lessor is both selling and leasing goods to the same lessee/buyer and has marked goods for delivery but has not distinguished between those related to the lease contract and those related to the sales contract. As in Section 2-501(1)(b) [30-2-501(1)(b)], this issue has been left to be resolved by the courts, case by case.

30-2A-218. Insurance and proceeds.

Official Comment

Source: Section 2A-218, U.C.C.

Uniform Statutory Source: Section 2-501[, U.C.C.].

Changes: This section, together with Section 2A-217 [30-2A-217], is derived from the provisions of Section 2-501 [30-2-501], with changes and additions to reflect leasing practices and terminology.

Purposes: Subsection (2) states a rule allowing substitution of goods by the lessor under certain circumstances, until default or insolvency of the lessor, or until notification to the lessee that identification is final. Subsection (3) states a rule regarding the lessor's insurable interest that, by virtue of the difference between a sale and a lease, necessarily is different from the rule stated in Section 2-501(2) [30-2-501(2)] regarding the seller's insurable interest. For this purpose the option to buy shall be deemed to have been exercised by the lessee when the resulting sale is closed, not when the lessee gives notice to the lessor. Further, subsection (5) is new and reflects the common practice of shifting the responsibility and cost of insuring the goods between the parties to the lease transaction.

Case Notes

Lessor Fully Compensated for Loss of Truck Under Rental Agreement — Agreed Value of Truck Inapplicable to Damage Claim: Plaintiff leased a truck to defendant for construction work. The truck had an agreed value of $250,000 and a rental rate of $12,000 a month. While in defendant's possession, the truck was heavily damaged. Plaintiff initially sought to repair the truck, but eventually it was stripped of usable parts, and the remaining shell was sold for $15,000. Plaintiff received $114,500 from its insurer, based on the insurer's calculation that the truck had a $126,000 cash replacement value minus the $2,500 policy deductible owed to plaintiff by defendant and minus a $9,000 salvage value. Plaintiff then sued defendant for the unpaid balance of the agreed value, including the monthly payments because the agreed value had not been paid. The District Court noted that even though the parties did not have a signed, enforceable, written contract, defendant had properly insured the truck pursuant to a reasonable lease term, identifying plaintiff as beneficiary, and held that defendant had no independent obligation to pay damages beyond the deductible. Because plaintiff had recovered all damages to which it was entitled, judgment was entered for defendant, and plaintiff appealed. The Supreme Court found that the language of the rental agreement did not require the lessee to pay the agreed value if the truck was damaged or destroyed, so defendant was not liable for the agreed value. Plaintiff failed to show the actual replacement cost of the truck and failed to establish that the District Court's finding was clearly erroneous, so the court did not err in holding that plaintiff was not entitled to additional compensation for replacing the truck. Additionally, plaintiff did not demonstrate what additional rental payments were owed, so defendant had no further obligation to pay damages for loss of use. The District Court did not err in holding that plaintiff was fully compensated under the rental agreement, and judgment was affirmed. Performance Mach. Co., Inc. v. Yellowstone Mtn. Club, LLC, 2007 MT 250, 339 M 259, 169 P3d 394 (2007).

30-2A-219. Risk of loss.

Official Comment

Source: Section 2A-219, U.C.C.

Uniform Statutory Source: Section 2-509(1) through (3)[, U.C.C.].

Changes: Subsection (1) is new. The introduction to subsection (2) is new, but subparagraph (a) incorporates the provisions of Section 2-509(1) [30-2-509(1)]; subparagraph (b) incorporates the provisions of Section 2-509(2) [30-2-509(2)] only in part, reflecting current practice in lease transactions.

Purposes: Subsection (1) states rules related to retention or passage of risk of loss consistent with current practice in lease transactions. The provisions of subsection (4) of Section 2-509 [30-2-509(4)] are not incorporated as they are not necessary. This section does not deal with responsibility for loss caused by the wrongful act of either the lessor or the lessee.

30-2A-220. Effect of default on risk of loss.

Official Comment

Source: Section 2A-220, U.C.C.

Uniform Statutory Source: Section 2-510[, U.C.C.].

Changes: Revised to reflect leasing practices and terminology. The rule in Section [subsection] (1)(b) does not allow the lessee under a finance lease to treat the risk of loss as having remained with the supplier from the beginning. This is appropriate given the limited circumstances under which the lessee under a finance lease is allowed to revoke acceptance. Section 2A-517 [30-2A-517] and Section 2A-516 [30-2A-516] official comment.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

30-2A-221. Casualty to identified goods.

Official Comment

Source: Section 2A-221, U.C.C.

Uniform Statutory Source: Section 2-613[, U.C.C.].

Changes: Revised to reflect leasing practices and terminology.

Purposes: Due to the vagaries of determining the amount of due allowance (Section 2-613(b) [30-2-613(b)]), no attempt was made in subsection (b) [subsection (2) of this section] to treat a problem unique to lease contracts and installment sales contracts: determining how to recapture the allowance, *e.g.*, application to the first or last rent payments or allocation, *pro rata,* to all rent payments.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

Part 3
Effect of Lease Contract

30-2A-301. Enforceability of lease contract.

Official Comment

Source: Section 2A-301, U.C.C.

Uniform Statutory Source: Section 9-201[, U.C.C.].

Changes: The first sentence of Section 9-201 [30-9-201, now repealed, see 30-9A-201] was incorporated, modified to reflect leasing terminology. The second sentence of Section 9-201 [30-9-201, now repealed, see 30-9A-201] was eliminated as not relevant to leasing practices.

Purposes: This section establishes a general rule regarding the validity and enforceability of a lease contract. The lease contract is effective and enforceable between the parties and against third parties. Exceptions to this general rule arise where there is a specific rule to the contrary in this Article. Enforceability is, thus, dependent upon the lease contract meeting the requirements of the Statute of Frauds provisions of Section 2A-201 [30-2A-201]. Enforceability is also a function of the lease contract conforming to the principles of construction and interpretation contained in the Article on General Provisions (Article 1 [Title 30, chapter 1]). Section 2A-103(4) [30-2A-103(4)].

The effectiveness or enforceability of the lease contract is not dependent upon the lease contract or any financing statement or the like being filed or recorded; however, the priority of the interest of a lessor of fixtures with respect to the interests of certain third parties in such fixtures is subject to the provisions of the Article on Secured Transactions (Article 9 [Title 30, chapter 9A]). Section 2A-309 [30-2A-309]. Prior to the adoption of this Article filing or recording was not required with respect to leases, only leases intended as security. The definition of security interest, as amended concurrently with the adoption of this Article, more clearly delineates leases and leases intended as security and thus signals the need to file. Section 1-201(37) [30-1-201(37)]. Those lessors who are concerned about whether the transaction creates a lease or a security interest will continue to file a protective financing statement. Section 9-408 [30-9-408, now repealed]. Coogan, Leasing and the Uniform Commercial Code, in *Equipment Leasing-Leveraged Leasing* 681, 744-46 (2d ed. 1980).

Hypothetical: 1. In construing this section it is important to recognize its relationship to other sections in this Article. This is best demonstrated by reference to a hypothetical. Assume that on February 1 A, a manufacturer of combines and other farm equipment, leased a fleet of six combines to B, a corporation engaged in the business of farming, for a 12 month term. Under the lease agreement between A and B, A agreed to defer B's payment of the first two months' rent to April 1. On March 1 B recognized that it would need only four combines and thus subleased two combines to C for an 11 month term.

2. This hypothetical raises a number of issues that are answered by the sections contained in this part. Since lease is defined to include sublease (Section 2A-103(1)(j) and (w) [30-2A-103(1)(j) and (1)(w)]), this section provides that the prime lease between A and B and the sublease between B and C are enforceable in accordance with their terms, except as otherwise provided in this Article; that exception, in this case, is one of considerable scope.

3. The separation of ownership, which is in A, and possession, which is in B with respect to four combines and which is in C with respect to two combines, is not relevant. Section 2A-302 [30-2A-302]. A's interest in the six combines cannot be challenged simply because A parted with possession to B, who in turn parted with possession of some of the combines to C. Yet it is important to note that by the terms of Section 2A-302 [30-2A-302] this conclusion is subject to change if otherwise provided in this Article.

4. B's entering the sublease with C raises an issue that is treated by this part. In a dispute over the leased combines A may challenge B's right to sublease. The general rule is permissive as to transfers of interests under a lease contract, including subleases. Section 2A-303(1)

[30-2A-303(1)]. However, the rule creates two significant exceptions. If the prime lease contract between A and B prohibits B from subleasing the combines, Section 2A-303(1)(a) [30-2A-303(1)(a)] applies, as the transfer is voluntary and prohibited; thus, B's interest under the prime lease may not be transferred under the sublease to C. Absent a prohibition in the prime lease contract A might be able to argue that the sublease to C materially increases A's risk; thus B's interest under the prime lease may not be transferred under the sublease to C, if after demand by A, C fails to provide the assurances required by Section 2A-303(2) [30-2A-303(2)]. Section 2A-303(1)(b) [30-2A-303(1)(b)].

5. Resolution of this issue is also a function of the section dealing with the sublease of goods by a prime lessee (Section 2A-305 [30-2A-305]). Subsection (1) of Section 2A-305 [30-2A-305(1)], which is subject to the rule of Section 2A-303 [30-2A-303] stated above, provides that C takes subject to the interest of A under the prime lease between A and B. However, there are two exceptions. First, if B is a merchant (Sections 2A-103(3) and 2-104(1) [30-2A-103(3) and 30-2-104(1)]) dealing in goods of that kind and C is a sublessee in the ordinary course of business (Sections 2A-103(1)(o) and 2A-103(1)(n) [30-2A-103(1)(o) and (1)(n)]), C takes free of the prime lease between A and B. Second, if B has rejected the six combines under the prime lease with A, and B disposes of the goods by sublease to C, C takes free of the prime lease if C can establish good faith. Section 2A-511(4) [30-2A-511(4)].

6. If the facts of this hypothetical are expanded and we assume that the prime lease obligated B to maintain the combines, an additional issue may be presented. Prior to entering the sublease, B, in satisfaction of its maintenance covenant, brought the two combines that it desired to sublease to a local independent dealer of A's. The dealer did the requested work for B. C inspected the combines on the dealer's lot after the work was completed. C signed the sublease with B two days later. C, however, was prevented from taking delivery of the two combines as B refused to pay the dealer's invoice for the repairs. The dealer furnished the repair service to B in the ordinary course of the dealer's business. If under applicable law the dealer has a lien on repaired goods in the dealer's possession, the dealer's lien will take priority over A's, B's and C's interests. Section 2A-306 [30-2A-306].

7. Now assume that C is in financial straits and one of C's creditors obtains a judgment against C. If the creditor levies on C's subleasehold interest in the two combines, who will prevail? Unless the levying creditor also holds a lien covered by Section 2A-306 [30-2A-306], discussed above, the judgment creditor will take its interest subject to B's rights under the sublease and A's rights under the prime lease. Section 2A-307(1) [30-2A-307(1)]. The hypothetical becomes more complicated if we assume that B is in financial straits and B's creditor holds the judgment. Here the judgment creditor takes subject to the sublease unless the lien attached to the two combines before the sublease contract became enforceable. Section 2A-307(2)(a) [30-2A-307(2)(a)]. However, B's judgment creditor cannot prime A's interest in the goods because, with respect to A, the judgment creditor is a creditor of B in its capacity as lessee under the prime lease between A and B. Thus, here the judgment creditor's interest is subject to the lease between A and B. Section 2A-307(1) [30-2A-307(1)].

8. Finally, assume that on April 1 B is unable to pay A the deferred rent then due under the prime lease, but that C is current in its payments under the sublease from B. What effect will B's default under the prime lease between A and B have on C's rights under the sublease between B and C? Section 2A-301 [30-2A-301] provides that a lease contract is effective against the creditors of either party. Since a lease contract includes a sublease contract (Section 2A-103(1)(l) [30-2A-103(1)(l)]), the sublease contract between B and C arguably could be enforceable against A, a prime lessor who has extended unsecured credit to B, the prime lessee/sublessor, if the sublease contract meets the requirements of Section 2A-201 [30-2A-201]. However, the rule stated in Section 2A-301 [30-2A-301] is subject to other provisions in this Article. Under Section 2A-305 [30-2A-305], C, as sublessee, would take subject to the prime lease contract in most cases. Thus, B's default under the prime lease will in most cases lead to A's recovery of the goods from C. Section 2A-523 [30-2A-523]. C's recourse will be to assert a claim for damages against B. Section 2A-508 [30-2A-508].

Relationship Between Sections: 1. As the analysis of the hypothetical demonstrates, Part 3 of the Article focuses on issues that relate to the enforceability of the lease contract (Sections 2A-301, 2A-302 and 2A-303 [30-2A-301 through 30-2A-303]) and to the priority of various claims to the goods subject to the lease contract (Sections 2A-304, 2A-305, 2A-306, 2A-307, 2A-308, 2A-309 and 2A-310 [30-2A-304 through 30-2A-310]).

2. This section states a general rule of enforceability, which is subject to specific rules to the contrary stated elsewhere in the Article. Section 2A-302 [30-2A-302] negates any notion that

the separation of title and possession is fraudulent as a rule of law. Finally, Section 2A-303 [30-2A-303] states a permissive rule with respect to the transfer of the lessor's interest (as well as the residual interest in the goods) or the lessee's interest under the lease contract. Conditions are imposed as a function of various issues including whether the transfer is voluntary or involuntary. In addition, a system of rules is created to deal with the rights and duties among assignor, assignee and the other party to the lease contract.

3. Sections 2A-304 and 2A-305 [30-2A-304 and 30-2A-305] are twins that deal with good faith transferees of goods subject to the lease contract. Section 2A-304 [30-2A-304] creates a set of rules with respect to transfers by the lessor of goods subject to a lease contract; the transferee considered is a subsequent lessee of the goods. The priority dispute covered here is between the subsequent lessee and the original lessee of the goods (or persons claiming through the original lessee). Section 2A-305 [30-2A-305] creates a set of rules with respect to transfers by the lessee of goods subject to a lease contract; the transferees considered are buyers of the goods or sublessees of the goods. The priority dispute covered here is between the transferee and the lessor of the goods (or persons claiming through the lessor).

4. Section 2A-306 [30-2A-306] creates a rule with respect to priority disputes between holders of liens for services or materials furnished with respect to goods subject to a lease contract and the lessor or the lessee under that contract. Section 2A-307 [30-2A-307] creates a rule with respect to priority disputes between the lessee and creditors of the lessor and priority disputes between the lessor and creditors of the lessee.

5. Section 2A-308 [30-2A-308] creates a series of rules relating to allegedly fraudulent transfers and preferences. The most significant rule is that set forth in subsection (3) [30-2A-308(2)] which validates sale-leaseback transactions if the buyer-lessor can establish that he or she bought for value and in good faith.

6. Finally, Sections 2A-309 and 2A-310 [30-2A-309 and 30-2A-310] create a series of rules with respect to priority disputes between various third parties and a lessor of fixtures or accessions, respectively, with respect thereto.

30-2A-302. Title to and possession of goods.

Official Comment

Source: Section 2A-302, U.C.C.

Uniform Statutory Source: Section 9-202[, U.C.C.].

Changes: Section 9-202 [30-9-202, now repealed, see 30-9A-202] was modified to reflect leasing terminology and to clarify the law of leases with respect to fraudulent conveyances or transfers.

Purposes: The separation of ownership and possession of goods between the lessor and the lessee (or a third party) has created problems under certain fraudulent conveyance statutes. *See, e.g., In re Ludlum Enters.*, 510 F.2d 996 (5th Cir.1975); *Suburbia Fed. Sav. & Loan Ass'n v. Bel-Air Conditioning Co.*, 385 So.2d 1151 (Fla.Dist.Ct.App.1980). This section provides, among other things, that separation of ownership and possession *per se* does not affect the enforceability of the lease contract. Sections 2A-301 and 2A-308 [30-2A-301 and 30-2A-308].

30-2A-303. Alienability of party's interest under lease contract or of lessor's residual interest in goods — delegation of performance — transfer of rights.

Official Comment

Source: Section 2A-303, U.C.C.

Uniform Statutory Source: Section 2-210[, U.C.C.].

Changes: The provisions of Sections 2-210 [30-2-210] and 9-311 [30-9-311, now repealed, see 30-9A-401] were incorporated in this section, with substantial modifications to reflect leasing terminology and practice and to harmonize the principles of the respective provisions, i.e., limitations on delegation of performance on the one hand and alienability of rights on the other. In addition, unlike Section 2-210 [30-2-210] which deals only with voluntary transfers, this section deals with involuntary as well as voluntary transfers. Moreover, the principle of Section 9-318(4) [30-9-318(4) now repealed, see 30-9A-406] denying effectiveness to contractual terms prohibiting assignments of receivables due and to become due also is implemented.

Purposes:

1. Subsection (2) states a rule, consistent with Section 9-401(b) [30-9A-401(2)], that voluntary and involuntary transfers of an interest of a party under the lease contract or of the lessor's residual interest, including by way of the creation or enforcement of a security interest, are effective, notwithstanding a provision in the lease agreement prohibiting the transfer or making the transfer an event of default. Although the transfers are effective, the provision in the lease agreement is nevertheless enforceable, but only as provided in subsection (4). Under

subsection (4) the prejudiced party is limited to the remedies on "default under the lease contract" in this Article [Title 30, Chapter 2A] and, except as limited by this Article [Title 30, Chapter 2A], as provided in the lease agreement, if the transfer has been made an event of default. Section 2A-501(2) [30-2A-501(2)]. Usually, there will be a specific provision to this effect or a general provision making a breach of a covenant an event of default. In those cases where the transfer is prohibited, but not made an event of default, the prejudiced party may recover damages; or, if the damage remedy would be ineffective adequately to protect that party, the court can order cancellation of the lease contract or enjoin the transfer. This rule that such provisions generally are enforceable is subject to subsection (3) and Section 9-407 [30-9A-407], which make such provisions unenforceable in certain instances.

2. Under Section 9-407 [30-9A-407], a provision in a lease agreement which prohibits the creation or enforcement of a security interest, including sales of lease contracts subject to Article 9 [Title 30, chapter 9A] (Section 9-109(a)(3) [30-9A-109(1)(c)]), or makes it an event of default is generally not enforceable, reflecting the policy of Section 9-406 and former Section 9-318(4) [30-9A-406 and 30-9-318(4), now repealed, see 30-9A-406].

3. Subsection (3) is based upon Section 2-210(2) [30-2-210(2)] and Section 9-406 [30-9A-406]. It makes unenforceable a prohibition against transfers of certain rights to payment or a provision making the transfer an event of default. It also provides that such transfers do not materially impair the prospect of obtaining return performance by, materially change the duty of, or materially increase the burden or risk imposed on, the other party to the lease contract so as to give rise to the rights and remedies stated in subsection (4). Accordingly, a transfer of a right to payment cannot be prohibited or made an event of default, or be one that materially impairs performance, changes duties or increases risk, if the right is already due or will become due without further performance being required by the party to receive payment. Thus, a lessor can transfer the right to future payments under the lease contract, including by way of a grant of a security interest, and the transfer will not give rise to the rights and remedies stated in subsection (4) if the lessor has no remaining performance under the lease contract. The mere fact that the lessor is obligated to allow the lessee to remain in possession and to use the goods as long as the lessee is not in default does not mean that there is remaining performance on the part of the lessor. Likewise, the fact that the lessor has potential liability under a "non-operating" lease contract for breaches of warranty does not mean that there is remaining performance. In contrast, the lessor would have remaining performance under a lease contract requiring the lessor to regularly maintain and service the goods or to provide "upgrades" of the equipment on a periodic basis in order to avoid obsolescence. The basic distinction is between a mere potential duty to respond which is not remaining performance, and an affirmative duty to render stipulated performance. Although the distinction may be difficult to draw in some cases, it is instructive to focus on the difference between "operating" and "non-operating" leases as generally understood in the marketplace. Even if there is remaining performance under a lease contract, a transfer for security of a right to payment that is made an event of default or that is in violation of a prohibition against transfer does not give rise to the rights and remedies under subsection (4) if it does not constitute an actual delegation of a material performance under Section 9-407 [30-9A-407].

4. The application of either the rule of Section 9-407 [30-9A-407] or the rule of subsection (3) to the grant by the lessor of a security interest in the lessor's right to future payment under the lease contract may produce the same result. Both provisions generally protect security transfers by the lessor in particular because the creation by the lessor of a security interest or the enforcement of that interest generally will not prejudice the lessee's rights if it does not result in a delegation of the lessor's duties. To the contrary, the receipt of loan proceeds or relief from the enforcement of an antecedent debt normally should enhance the lessor's ability to perform its duties under the lease contract. Nevertheless, there are circumstances where relief might be justified. For example, if ownership of the goods is transferred pursuant to enforcement of a security interest to a party whose ownership would prevent the lessee from continuing to possess the goods, relief might be warranted. See 49 U.S.C. § 1401(a) and (b) which places limitations on the operation of aircraft in the United States based on the citizenship or corporate qualification of the registrant.

5. Relief on the ground of material prejudice when the lease agreement does not prohibit the transfer or make it an event of default should be afforded only in extreme circumstances, considering the fact that the party asserting material prejudice did not insist upon a provision in the lease agreement that would protect against such a transfer.

6. Subsection (4) implements the rule of subsection (2). Subsection (2) provides that, even though a transfer is effective, a provision in the lease agreement prohibiting it or making it an event of default may be enforceable as provided in subsection (4). See Brummond v. First National Bank of Clovis, 656 P.2d 884, 35 U.C.C.Rep.Serv. (Callaghan) 1311 (N.Mex.1983), stating the analogous rule for Section 9-311 [30-9A-311]. If the transfer prohibited by the lease agreement is made an event of default, then, under subsection (4)(a), unless the default is waived or there is an agreement otherwise, the aggrieved party has the rights and remedies referred to in Section 2A-501(2) [30-2A-501(2)], viz. those in this Article [Title 30, chapter 2A] and, except as limited in the Article [Title 30, chapter 2A], those provided in the lease agreement. In the unlikely circumstance that the lease agreement prohibits the transfer without making a violation of the prohibition an event of default or, even if there is no prohibition against the transfer, and the transfer is one that materially impairs performance, changes duties, or increases risk (for example, a sublease or assignment to a party using the goods improperly or for an illegal purpose), then subsection (4)(b) is applicable. In that circumstance, unless the party aggrieved by the transfer has otherwise agreed in the lease contract, such as by assenting to a particular transfer or to transfers in general, or agrees in some other manner, the aggrieved party has the right to recover damages from the transferor and a court may, in appropriate circumstances, grant other relief, such as cancellation of the lease contract or an injunction against the transfer.

7. If a transfer gives rise to the rights and remedies provided in subsection (4), the transferee as an alternative may propose, and the other party may accept, adequate cure or compensation for past defaults and adequate assurance of future due performance under the lease contract. Subsection (4) does not preclude any other relief that may be available to a party to the lease contract aggrieved by a transfer subject to an enforceable prohibition, such as an action for interference with contractual relations.

8. Subsection (7) requires that a provision in a consumer lease prohibiting a transfer, or making it an event of default, must be specific, written and conspicuous. See Section 1-201(10) [30-1-201(10)]. This assists in protecting a consumer lessee against surprise assertions of default.

9. Subsection (5) is taken almost verbatim from the provisions of Section 2-210(5) [30-2-210(5)]. The subsection states a rule of construction that distinguishes a commercial assignment, which substitutes the assignee for the assignor as to rights and duties, and an assignment for security or financing assignment, which substitutes the assignee for the assignor only as to rights. Note that the assignment for security or financing assignment is a subset of all security interests. Security interest is defined to include "any interest of a buyer of . . . chattel paper". Section 1-201(37) [30-1-201(37)]. Chattel paper is defined to include a lease. Section 9-102 [30-9A-102]. Thus, a buyer of leases is the holder of a security interest in the leases. That conclusion should not influence this issue, as the policy is quite different. Whether a buyer of leases is the holder of a commercial assignment, or an assignment for security or financing assignment should be determined by the language of the assignment or the circumstances of the assignment.

Compiler's Comments

1999 Amendment: Chapter 305 at end of (1) substituted "30-9-129(1)(c)" (renumbered 30-9A-109(1)(c)) for "30-9-102(1)(b)"; in exception clause in (2) inserted reference to 30-9-447 (renumbered 30-9A-407); deleted former (3) that read: "(3)(a) A provision in a lease agreement that prohibits the creation or enforcement of a security interest in an interest of a party under the lease contract or in the lessor's residual interest in the goods or that makes such a transfer an event of default is not enforceable unless, and then only to the extent that, there is an actual transfer by the lessee of the lessee's right of possession or use of the goods in violation of the provision or an actual delegation of a material performance of either party to the lease contract in violation of the provision.

(b) Neither the granting nor the enforcement of a security interest in the lessor's interest under the lease contract or the lessor's residual interest in the goods is a transfer that materially impairs the prospect of obtaining return performance by, materially changes the duty of, or materially increases the burden or risk imposed on the lessee within the purview of subsection (5) unless, and then only to the extent that, there is an actual delegation of a material performance of the lessor"; in (4) inserted reference to 30-9-447 (renumbered 30-9A-407); and made minor changes in style. Amendment effective July 1, 2001.

30-2A-304. Subsequent lease of goods by lessor.

Official Comment

Source: Section 2A-304, U.C.C.

Uniform Statutory Source: Section 2-403[, U.C.C.].

Changes: While Section 2-403 [30-2-403] was used as a model for this section, the provisions of Section 2-403 [30-2-403] were significantly revised to reflect leasing practices and to integrate this Article with certificate of title statutes.

Purposes: This section must be read in conjunction with, as it is subject to, the provisions of Section 2A-303 [30-2A-303], which govern voluntary and involuntary transfers of rights and duties under a lease contract, including the lessor's residual interest in the goods.

This section must also be read in conjunction with Section 2-403 [30-2-403]. This section and Section 2A-305 [30-2A-305] are derived from Section 2-403 [30-2-403], which states a unified policy on good faith purchases of goods. Given the scope of the definition of purchaser (Section 1-201(33) [30-1-201(33)]), a person who bought goods to lease as well as a person who bought goods subject to an existing lease from a lessor will take pursuant to Section 2-403 [30-2-403]. Further, a person who leases such goods from the person who bought them should also be protected under Section 2-403 [30-2-403], first because the lessee's rights are derivative and second because the definition of purchaser should be interpreted to include one who takes by lease; no negative implication should be drawn from the inclusion of lease in the definition of purchase in this Article. Section 2A-103(1)(v) [30-2A-103(1)(v)].

There are hypotheticals that relate to an entrustee's unauthorized lease of entrusted goods to a third party that are outside the provisions of Sections 2-403, 2A-304 and 2A-305 [30-2-403, 30-2A-304, and 30-2A-305]. Consider a sale of goods by M, a merchant, to B, a buyer. After paying for the goods B allows M to retain possession of the goods as B is short of storage. Before B calls for the goods M leases the goods to L, a lessee. This transaction is not governed by Section 2-403(2) [30-2-403(2)] as L is not a buyer in the ordinary course of business. Section 1-201(9) [30-1-201(9)]. Further, this transaction is not governed by Section 2A-304(2) [30-2A-304(2)] as B is not an existing lessee. Finally, this transaction is not governed by Section 2A-305(2) [30-2A-305(2)] as B is not M's lessor. Section 2A-307(2) [30-2A-307(2)] resolves the potential dispute between B, M and L. By virtue of B's entrustment of the goods to M and M's lease of the goods to L, B has a cause of action against M under the common law. Sections 2A-103(4) and 1-103 [30-2A-103(4) and 30-1-103]. *See, e.g.*, Restatement (Second) of Torts §§ 222A-243. Thus, B is a creditor of M. Sections 2A-103(4) and 1-201(12) [30-2A-103(4) and 30-1-201(12)]. Section 2A-307(2) [30-2A-307(2)] provides that B, as M's creditor, takes subject to M's lease to L. Thus, if L does not default under the lease, L's enjoyment and possession of the goods should be undisturbed. However, B is not without recourse. B's action should result in a judgment against M providing, among other things, a turnover of all proceeds arising from M's lease to L, as well as a transfer of all of M's right, title and interest as lessor under M's lease to L, including M's residual interest in the goods. Section 2A-103(1)(q) [30-2A-103(1)(q)].

Subsection (1) states a rule with respect to the leasehold interest obtained by a subsequent lessee from a lessor of goods under an existing lease contract. The interest will include such leasehold interest as the lessor has in the goods as well as the leasehold interest that the lessor had the power to transfer. Thus, the subsequent lessee obtains unimpaired all rights acquired under the law of agency, apparent agency, ownership or other estoppel, whether based upon statutory provisions or upon case law principles. Sections 2A-103(4) and 1-103 [30-2A-103(4) and 30-1-103]. In general, the subsequent lessee takes subject to the existing lease contract, including the existing lessee's rights thereunder. Furthermore, the subsequent lease contract is, of course, limited by its own terms, and the subsequent lessee takes only to the extent of the leasehold interest transferred thereunder.

Subsection (1) further provides that a lessor with voidable title has power to transfer a good leasehold interest to a good faith subsequent lessee for value. In addition, subsections (1)(a) through (d) provide specifically for the protection of the good faith subsequent lessee for value in a number of specific situations which have been troublesome under prior law.

The position of an existing lessee who entrusts leased goods to its lessor is not distinguishable from the position of other entrusters. Thus, subsection (2) provides that the subsequent lessee in the ordinary course of business takes free of the existing lease contract between the lessor entrustee and the lessee entruster, if the lessor is a merchant dealing in goods of that kind. Further, the subsequent lessee obtains all of the lessor entrustee's and the lessee entruster's rights to the goods, but only to the extent of the leasehold interest transferred by the lessor entrustee. Thus, the lessor entrustee retains the residual interest in the goods. Section 2A-103(1)(q) [30-2A-103(1)(q)]. However, entrustment by the existing lessee must have occurred before the interest of the subsequent lessee became enforceable against the lessor. Entrusting is defined in Section 2-403(3) [30-2-403(3)] and that definition applies here. Section 2A-103(3) [30-2A-103(3)].

Subsection (3) states a rule with respect to a transfer of goods from a lessor to a subsequent lessee where the goods are subject to an existing lease and covered by a certificate of title. The subsequent lessee's rights are no greater than those provided by this section and the applicable certificate of title statute, including any applicable case law construing such statute. Where the relationship between the certificate of title statute and Section 2-403 [30-2-403], the statutory analogue to this section, has been construed by a court, that construction is incorporated here. Sections 2A-103(4) and 1-102(1) and (2) [30-2A-103(4) and 30-1-102(1) and (2)]. The better rule is that the certificate of title statutes are in harmony with Section 2-403 [30-2-403] and thus would be in harmony with this section. *E.g.*, *Atwood Chevrolet-Olds v. Aberdeen Mun. School Dist.*, 431 So.2d 926, 928 (Miss.1983); *Godfrey v. Gilsdorf*, 476 P.2d 3, 6, 86 Nev. 714, 718 (1970); *Martin v. Nager*, 192 N.J. Super. 189, 197-98, 469 A.2d 519, 523 (Super.Ct. Ch. Div.1983). Where the certificate of title statute is silent on this issue of transfer, this section will control.

30-2A-305. Sale or sublease of goods by lessee.

Official Comment

Source: Section 2A-305, U.C.C.

Uniform Statutory Source: Section 2-403[, U.C.C.].

Changes: While Section 2-403 [30-2-403] was used as a model for this section, the provisions of Section 2-403 [30-2-403] were significantly revised to reflect leasing practice and to integrate this Article with certificate of title statutes.

Purposes: This section, a companion to Section 2A-304 [30-2A-304], states the rule with respect to the leasehold interest obtained by a buyer or sublessee from a lessee of goods under an existing lease contract. *Cf.* Section 2A-304 [30-2A-304] official comment. Note that this provision is consistent with existing case law, which prohibits the bailee's transfer of title to a good faith purchaser for value under Section 2-403(1) [30-2-403(1)]. *Rohweder v. Aberdeen Product. Credit Ass'n*, 765 F.2d 109 (8th Cir.1985).

Subsection (2) is also consistent with existing case law. *American Standard Credit, Inc. v. National Cement Co.*, 643 F.2d 248, 269-70 (5th Cir.1981); *but cf. Exxon Co., U.S.A. v. TLW Computer Indus.*, 37 U.C.C. Rep. Serv. (Callaghan) 1052, 1057-58 (D.Mass.1983). Unlike Section 2A-304(2) [30-2A-304(2)], this subsection does not contain any requirement with respect to the time that the goods were entrusted to the merchant. In Section 2A-304(2) [30-2A-304(2)] the competition is between two customers of the merchant lessor; the time of entrusting was added as a criterion to create additional protection to the customer who was first in time: the existing lessee. In subsection (2) the equities between the competing interests were viewed as balanced.

There appears to be some overlap between Section 2-403(2) [30-2-403(2)] and Section 2A-305(2) [30-2A-305(2)] with respect to a buyer in the ordinary course of business. However, an examination of this Article's definition of buyer in the ordinary course of business (Section 2A-103(1)(a) [30-2A-103(1)(a)]) makes clear that this reference was necessary to treat entrusting in the context of a lease.

Subsection (3) states a rule of construction with respect to a transfer of goods from a lessee to a buyer or sublessee, where the goods are subject to an existing lease and covered by a certificate of title. *Cf.* Section 2A-304 [30-2A-304] official comment.

30-2A-306. Priority of certain liens arising by operation of law.

Official Comment

Source: Section 2A-306, U.C.C.

Uniform Statutory Source: Section 9-310[, U.C.C.].

Changes: The approach reflected in the provisions of Section 9-310 [30-9-310, now repealed, see 30-9A-333] was included, but revised to conform to leasing terminology and to expand the exception to the special priority granted to protected liens to cover liens created by rule of law as well as those created by statute.

Purposes: This section should be interpreted to allow a qualified lessor or a qualified lessee to be the competing lienholder if the statute or rule of law so provides. The reference to statute includes applicable regulations and cases; these sources must be reviewed in resolving a priority dispute under this section.

30-2A-307. Priority of liens arising by attachment or levy on, security interests in, and other claims to goods.

Official Comment

Source: Section 2A-307, U.C.C.

Uniform Statutory Source: None for subsections (1) and (2). Subsections (3) and (4) are derived from the provisions of Section 9-307(1) and (3)[, U.C.C.], respectively.

Changes: The provisions of Section 9-307(1) and (3) [30-9-307(1) and (3), now repealed, see 30-9A-320] were incorporated, and modified to reflect leasing terminology and the basic concepts reflected in this Article.

Purposes:

1. Subsection (1) states a general rule of priority that a creditor of the lessee takes subject to the lease contract. The term lessee (Section 2A-103(1)(n) [30-2A-103(1)(n)]) includes sublessee. Therefore, this subsection not only covers disputes between the prime lessor and a creditor of the prime lessee but also disputes between the prime lessor, or the sublessor, and a creditor of the sublessee. Section 2A-301 [30-2A-301] official comment 3(g). Further, by using the term creditor (Section 1-201(12) [30-1-201(12)]), this subsection will cover disputes with a general creditor, a secured creditor, a lien creditor and any representative of creditors. Section 2A-103(4) [30-2A-103(4)].

2. Subsection (2) states a general rule of priority that a creditor of a lessor takes subject to the lease contract. Note the discussion above with regard to the scope of these rules. Section 2A-301 [30-2A-301] official comment 3(g). Thus, the section will not only cover disputes between the prime lessee and a creditor of the prime lessor but also disputes between the prime lessee, or the sublessee, and a creditor of the sublessor.

3. To take priority over the lease contract, and the interests derived therefrom, the creditor must come within the exception stated in subsection (2) or within one of the provisions of Article 9 [Title 30, chapter 9A] mentioned in subsection (3). Subsection (2) provides that where the creditor holds a lien (Section 2A-103(1)(r)) that attached before the lease contract became enforceable (Section 2A-301), the creditor does not take subject to the lease. Subsection (3) provides that a lessee takes its leasehold interest subject to a security interest except as otherwise provided in Sections 9-317, 9-321, or 9-323 [30-9A-317, 30-9A-321, or 30-9A-323].

4. The rules of this section operate in favor of whichever party to the lease contract may enforce it, even if one party perhaps may not, e.g., under Section 2A-201(1)(b) [30-2A-201(1)(b)].

Compiler's Comments

1999 Amendment: Chapter 305 deleted former (2)(b) and (2)(c) that read: "(b) the creditor holds a security interest in the goods and the lessee did not give value and receive delivery of the goods without knowledge of the security interest; or

(c) the creditor holds a security interest in the goods that was perfected (30-9-303) before the lease contract became enforceable"; deleted former (3) and (4) that read: "(3) A lessee in the ordinary course of business takes the leasehold interest free of a security interest in the goods created by the lessor even though the security interest is perfected (30-9-303) and the lessee knows of its existence.

(4) A lessee other than a lessee in the ordinary course of business takes the leasehold interest free of a security interest to the extent that it secures future advances made after the secured party acquires knowledge of the lease or more than 45 days after the lease contract becomes enforceable, whichever occurs first, unless the future advances are made pursuant to a commitment entered into without knowledge of the lease and before the expiration of the 45-day period"; inserted (3) concerning lessee subject to security interest held by lessor's creditor; and made minor changes in style. Amendment effective July 1, 2001.

30-2A-308. Special rights of creditors.

Official Comment

Source: Section 2A-308, U.C.C.

Uniform Statutory Source: Section 2-402(2) and (3)(b)[, U.C.C.].

Changes: Rephrased and new material added to conform to leasing terminology and practice.

Purposes: Subsection (1) states a general rule of avoidance where the lessor has retained possession of goods if such retention is fraudulent under any statute or rule of law. However, the subsection creates an exception under certain circumstances for retention of possession of goods for a commercially reasonable time after the lease contract becomes enforceable.

Subsection (2) also preserves the possibility of an attack on the lease by creditors of the lessor if the lease was made in satisfaction of or as security for a pre-existing claim, and would constitute a fraudulent transfer or voidable preference under other law.

Finally, subsection (3) states a new rule with respect to sale-leaseback transactions, *i.e.*, transactions where the seller sells goods to a buyer but possession of the goods is retained by the seller pursuant to a lease contract between the buyer as lessor and the seller as lessee.

Notwithstanding any statute or rule of law that would treat such retention as fraud, whether *per se, prima facie,* or otherwise, the retention is not fraudulent if the buyer bought for value (Section 1-201(44) [30-1-201(44)]) and in good faith (Sections 1-201(19) and 2-103(1)(b) [30-1-201(19) and 30-2-103(1)(b)]). Section 2A-103(3) and (4) [30-2A-103(3) and (4)]. This provision overrides Section 2-402(2) [30-2-402(2)] to the extent it would otherwise apply to a sale-leaseback transaction.

30-2A-309. Lessor's and lessee's rights when goods become fixtures.

Official Comment

Source: Section 2A-309, U.C.C.

Uniform Statutory Source: Section 9-313[, U.C.C.].

Changes: Revised to reflect leasing terminology and to add new material.

Purposes: While Section 9-313 [30-9-313, now repealed, see 30-9A-334] provided a model for this section, certain provisions were substantially revised.

Section 2A-309(1)(c) [30-2A-309(1)(c)], which is new, defines purchase money lease to exclude leases where the lessee had possession or use of the goods or the right thereof before the lease agreement became enforceable. This term is used in subsection (4)(a) as one of the conditions that must be satisfied to obtain priority over the conflicting interest of an encumbrancer or owner of the real estate.

Section 2A-309(4) [30-2A-309(4)], which states one of several priority rules found in this section, deletes reference to office machines and the like (Section 9-313(4)(c) [30-9-313(4)(c), now repealed, see 30-9A-334]) as well as certain liens (Section 9-313(4)(d) [30-9-313(4)(d), now repealed, see 30-9A-334]). However, these items are included in subsection (5), another priority rule that is more permissive than the rule found in subsection (4) as it applies whether or not the interest of the lessor is perfected. In addition, subsection (5)(a) expands the scope of the provisions of Section 9-313(4)(c) [30-9-313(4)(c), now repealed, see 30-9A-334] to include readily removable equipment not primarily used or leased for use in the operation of real estate; the qualifier is intended to exclude from the expanded rule equipment integral to the operation of real estate, *e.g.*, heating and air conditioning equipment.

The rule stated in subsection (7) is more liberal than the rule stated in Section 9-313(7) [30-9-313(7), now repealed, see 30-9A-334] in that issues of priority not otherwise resolved in this subsection are left for resolution by the priority rules governing conflicting interests in real estate, as opposed to the Section 9-313(7) [30-9-313(7), now repealed, see 30-9A-334] automatic subordination of the security interest in fixtures.

The rule stated in subsection (8) is more liberal than the rule stated in Section 9-313(8) [30-9-313(8), now repealed, see 30-9A-604] in that the right of removal is extended to both the lessor and the lessee and the occasion for removal includes expiration, termination or cancellation of the lease agreement, and enforcement of rights and remedies under this Article, as well as default. The new language also provides that upon removal the goods are free and clear of conflicting interests of owners and encumbrancers of the real estate.

Finally, subsection (9) provides a mechanism for the lessor of fixtures to perfect its interest by filing a financing statement under the provisions of the Article on Secured Transactions (Article 9 [Title 30, chapter 9A]), even though the lease agreement does not create a security interest. Section 1-201(37) [30-1-201(37)]. The relevant provisions of Article 9 [Title 30, chapter 9A] must be interpreted permissively to give effect to this mechanism as it implicitly expands the scope, perfection and priority provisions of Article 9 [Title 30, chapter 9A] to govern transactions that create a lease of fixtures, even though the lease agreement does not create a security interest. This mechanism is similar to that provided in Section 2-326(3)(c) [30-2-326(3)(c)] for the seller of goods on consignment, even though the consignment is not "intended as security". Section 1-201(37) [30-1-201(37)]. Given the lack of litigation with respect to the mechanism created for consignment sales, this new mechanism should prove effective. Note, however, that this is a more pervasive change in Article 9 [Title 30, chapter 9A] than that wrought by expanding the filing system to accommodate permissive filing for leases. U.C.C. § 9-408 app. II (West 1983)(Reasons for 1972 Adoption of New Section).

Compiler's Comments

1999 Amendment: Chapter 305 at end of (1)(b) substituted "30-9-522(1) and (2)" (renumbered 30-9A-502(1) and (2)) for "30-9-402(5)". Amendment effective July 1, 2001.

30-2A-310. Lessor's and lessee's rights when goods become accessions.

Official Comment

Source: Section 2A-310, U.C.C.

Uniform Statutory Source: Section 9-314[, U.C.C.].

Changes: Revised to reflect leasing terminology and to add new material.

Purposes: Subsections (1) and (2) restate the provisions of subsection (1) of Section 9-314 [30-9-314(1), now repealed, see 30-9A-335] to clarify the definition of accession and to add leasing terminology to the priority rule that applies when the lease is entered into before the goods become accessions. Subsection (3) restates the provisions of subsection (2) of Section 9-314 [30-9-314(2), now repealed, see 30-9A-335] to add leasing terminology to the priority rule that applies when the lease is entered into on or after the goods become accessions. Unlike the rule with respect to security interests, the lease is merely subordinate, not invalid.

Subsection (4) creates two exceptions to the priority rules stated in subsections (2) and (3). Subsection (4) deletes the special priority rule found in the provisions of Section 9-314(3)(b) [30-9-314(3)(b), now repealed, see 30-9A-335] as the interests of the lessor and lessee are entitled to greater protection.

Finally, subsection (5) is modeled on the provisions of Section 9-314(4) [30-9-314(4), now repealed, see 30-9A-335] with respect to removal of accessions, restated to reflect the parallel changes in Section 2A-309(8) [30-2A-309(8)].

Neither this section nor Section 9-314 [30-9-314, now repealed, see 30-9A-335] governs where the accession to the goods is not subject to the interest of a lessor or a lessee under a lease contract and is not subject to the interest of a secured party under a security agreement. This issue is to be resolved by the courts, case by case.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

30-2A-311. Priority subject to subordination.

Official Comment

Source: Section 2A-311, U.C.C.

Uniform Statutory Source: Section 9-316[, U.C.C.].

Purposes: The several preceding sections deal with questions of priority. This section is inserted to make it entirely clear that a person entitled to priority may effectively agree to subordinate the claim. Only the person entitled to priority may make such an agreement: the rights of such a person cannot be adversely affected by an agreement to which that person is not a party.

Part 4

Performance of Lease Contract Repudiated, Substituted, and Excused

30-2A-401. Insecurity — adequate assurance of performance.

Official Comment

Source: Section 2A-401, U.C.C.

Uniform Statutory Source: Section 2-609[, U.C.C.].

Changes: Revised to reflect leasing practices and terminology. Note that in the analogue to subsection (3) (Section 2-609(4) [30-2-609(4)]), the adjective "justified" modifies demand. The adjective was deleted here as unnecessary, implying no substantive change.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

30-2A-402. Anticipatory repudiation.

Official Comment

Source: Section 2A-402, U.C.C.

Uniform Statutory Source: Section 2-610[, U.C.C.].

Changes: Revised to reflect leasing practices and terminology.

30-2A-403. Retraction of anticipatory repudiation.

Official Comment

Source: Section 2A-403, U.C.C.

Uniform Statutory Source: Section 2-611[, U.C.C.].

Changes: Revised to reflect leasing practices and terminology. Note that in the analogue to subsection (2) (Section 2-611(2) [30-2-611(2)]) the adjective "justifiably" modifies demanded. The adjective was deleted here (as it was in Section 2A-401 [30-2A-401]) as unnecessary, implying no substantive change.

30-2A-404. Substituted performance.

Official Comment

Source: Section 2A-404, U.C.C.

Uniform Statutory Source: Section 2-614[, U.C.C.].

Changes: Revised to reflect leasing practices and terminology.

30-2A-405. Excused performance.

Official Comment

Source: Section 2A-405, U.C.C.

Uniform Statutory Source: Section 2-615[, U.C.C.].

Changes: Revised to reflect leasing practices and terminology.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

30-2A-406. Procedure on excused performance.

Official Comment

Source: Section 2A-406, U.C.C.

Uniform Statutory Source: Section 2-616(1) and (2)[, U.C.C.].

Changes: Revised to reflect leasing practices and terminology. Note that subsection 1(a) allows the lessee under a lease, including a finance lease, the right to terminate the lease for excused performance (Sections 2A-404 and 2A-405 [30-2A-404 and 30-2A-405]). However, subsection 1(b), which allows the lessee the right to modify the lease for excused performance, excludes a finance lease that is not a consumer lease. This exclusion is compelled by the same policy that led to codification of provisions with respect to irrevocable promises. Section 2A-407 [30-2A-407].

30-2A-407. Irrevocable promises — finance leases.

Official Comment

Source: Section 2A-407, U.C.C.

Purposes: This section extends the benefits of the classic "hell or high water" clause to a finance lease that is not a consumer lease. This section is self-executing; no special provision need be added to the contract. This section makes covenants in a finance lease irrevocable and independent due to the function of the finance lessor in a three party relationship: the lessee is looking to the supplier to perform the essential covenants and warranties. Section 2A-209 [30-2A-209]. Thus, upon the lessee's acceptance of the goods the lessee's promises to the lessor under the lease contract become irrevocable and independent. The provisions of this section remain subject to the obligation of good faith (Sections 2A-103(4) and 1-203 [30-2A-103(4) and 30-1-203]), and the lessee's revocation of acceptance (Section 2A-517 [30-2A-517]).

The section requires the lessee to perform even if the lessor's performance after the lessee's acceptance is not in accordance with the lease contract; the lessee may, however, have and pursue a cause of action against the lessor, *e.g.*, breach of certain limited warranties (Sections 2A-210 and 211(1) [30-2A-210 and 30-2A-211(1)]). This is appropriate because the benefit of the supplier's promises and warranties to the lessor under the supply contract is extended to the lessee under the finance lease. Section 2A-209 [30-2A-209]. Despite this balance, this section excludes a finance lease that is a consumer lease. That a consumer be obligated to pay notwithstanding defective goods or the like is a principle that is not tenable under case law (Unico v. Owen, 50 N.J. 101, 232 A.2d 405 (1967)), state statute (Unif. Consumer Credit Code §§ 3.403-.405, 7A U.L.A. 126-31 (1974), or federal statute (15 U.S.C. § 1666i (1982)).

The relationship of the three parties to a transaction that qualifies as a finance lease is best demonstrated by a hypothetical. A, the potential lessor, has been contacted by B, the potential lessee, to discuss the lease of an expensive line of equipment that B has recently placed an order for with C, the manufacturer of such goods. The negotiation is completed and A, as lessor, and B, as lessee, sign a lease of the line of equipment for a 60-month term. B, as buyer, assigns the purchase order with C to A. If this transaction creates a lease (Section 2A-103(1)(j) [30-2A-103(1)(j)]), this transaction should qualify as a finance lease. Section 2A-103(1)(g) [30-2A-103(1)(g)].

The line of equipment is delivered by C to B's place of business. After installation by C and testing by B, B accepts the goods by signing a certificate of delivery and acceptance, a copy of which is sent by B to A and C. One year later the line of equipment malfunctions and B falls behind in its manufacturing schedule.

Under this Article, because the lease is a finance lease, no warranty of fitness or merchantability is extended by A to B. Sections 2A-212(1) and 2A-213 [30-2A-212(1) and 30-2A-213]. Absent an express provision in the lease agreement, application of Section 2A-210 [30-2A-210] or Section 2A-211(1) [30-2A-211(1)], or application of the principles of law and equity, including the law with respect to fraud, duress, or the like (Sections 2A-103(4) and 1-103 [30-2A-103(4) and 30-1-103]), B has no claim against A. B's obligation to pay rent to A continues as the obligation became irrevocable and independent when B accepted the line of equipment (Section 2A-407(1) [30-2A-407(1)]). B has no right of set-off with respect to any part of the rent still due under the lease. Section 2A-508(6) [30-2A-508(6)]. However, B may have another remedy. Despite the lack of privity between B and C (the purchase order with C having been assigned by B to A), B may have a claim against C. Section 2A-209(1) [30-2A-209(1)].

This section is silent as to whether a "hell or high water" clause, *i.e.*, a clause that is to the effect of this section, is enforceable if included in a finance lease that is a consumer lease or a lease that is not a finance lease. That issue will continue to be determined by the facts of each case. Sections 2A-104, 2A-103(4), 9-206 and 9-318 [30-2A-104, 30-2A-103(4), 30-9-206, now repealed, see 30-9A-403, and 30-9-318, now repealed, see 30-9A-404 through 30-9A-406]. However, with respect to finance leases that are not consumer leases courts have enforced "hell or high water" clauses. In re O.P.M. Leasing Servs., 21 Bankr. 993, 1006 (Bankr. S.D.N.Y. 1982).

Subsection (2) further provides that a promise that has become irrevocable and independent under subsection (1) is enforceable not only between the parties but also against third parties. Thus, the finance lease can be transferred or assigned without disturbing enforceability. Further, subsection (2) also provides that the promise cannot, among other things, be cancelled or terminated without the consent of the lessor.

Part 5
Default

30-2A-501. Default — procedure.

Official Comment

Source: Section 2A-501, U.C.C.

Uniform Statutory Source: Section 9-501[, U.C.C.].

Changes: Substantially revised.

Purposes: Subsection (1) is new and represents a departure from the Article on Secured Transactions (Article 9 [Title 30, chapter 9A]) as the subsection makes clear that whether a party to the lease agreement is in default is determined by the agreement as well as this Article. Sections 2A-508 and 2A-523 [30-2A-508 and 30-2A-523]. It further departs from Article 9 [Title 30, chapter 9A] in recognizing the potential default of either party, a function of the bilateral nature of the obligations between the parties to the lease contract.

Subsection (2) is a version of the first sentence of Section 9-501(1) [30-9-501(1), now repealed, see 30-9A-601], revised to reflect leasing terminology.

Subsection (3), an expansive version of the second sentence of Section 9-501(1) [30-9-501(1), now repealed, see 30-9A-601], lists the procedures that may be followed by the party seeking enforcement; in effect, the scope of the procedures listed in subsection (3) is consistent with the scope of the procedures available to the foreclosing secured party.

Subsection (4) establishes that the parties' rights and remedies are cumulative. DeKoven, *Leases of Equipment: Puritan Leasing Company v. August, A Dangerous Decision*, 12 U.S.F. L.Rev. 257, 276-80 (1978).

Section 9-501(3) [30-9-501(3), now repealed, see 30-9A-602 and 30-9A-603], which, among other things, states that certain rules, to the extent they give rights to the debtor and impose duties on the secured party, may not be waived or varied, was not incorporated in this Article. Given the significance of freedom of contract in the development of the common law as it applies to bailments for hire and the lessee's lack of an equity of redemption, there was no reason to impose that restraint.

30-2A-502. Notice after default.

Official Comment

Source: Section 2A-502, U.C.C.

Purposes: This section makes clear that absent agreement to the contrary or provision in this Article to the contrary, *e.g.*, Section 2A-516(3)(a) [30-2A-516(3)(a)], the party in default is not entitled to notice of default or enforcement. While a review of Part 5 of Article 9 [Title 30, chapter 9A] leads to the same conclusion with respect to giving notice of default to the debtor, it is never stated. Although Article 9 [Title 30, chapter 9A] requires notice of disposition and strict foreclosure, the different scheme of lessors' and lessees' rights and remedies developed under the common law, and codified by this Article, generally does not require notice of enforcement; furthermore, such notice is not mandated by due process requirements. However, certain sections of this Article do require notice. *E.g.*, Section 2A-517(2) [30-2A-517(2)].

30-2A-503. Modification or impairment of rights and remedies.

Official Comment

Source: Section 2A-503, U.C.C.

Uniform Statutory Source: Sections 2-719 and 2-701[, U.C.C.].

Changes: Rewritten to reflect lease terminology and to clarify the relationship between this section and Section 2A-504 [30-2A-504].

Purposes: A significant purpose of this Part is to provide rights and remedies for those parties to a lease who fail to provide them by agreement or whose rights and remedies fail of their essential purpose or are unenforceable. However, it is important to note that this implies no restriction on freedom to contract. Sections 2A-103(4) and 1-102(3) [30-2A-103(4) and 30-1-102(3)]. Thus, subsection (1), a revised version of the provisions of Section 2-719(1) [30-2-719(1)], allows the parties to the lease agreement freedom to provide for rights and remedies in addition to or in substitution for those provided in this Article and to alter or limit the measure of damages recoverable under this Article. Except to the extent otherwise provided in this Article (*e.g.*, Sections 2A-105, 106 and 108(1) and (2) [30-2A-105, 30-2A-106, and 30-2A-108(1) and (2)]), this Part shall be construed neither to restrict the parties' ability to provide for rights and remedies or to limit or alter the measure of damages by agreement, nor to imply disapproval of rights and remedy schemes other than those set forth in this Part.

Subsection (2) makes explicit with respect to this Article what is implicit in Section 2-719 [30-2-719] with respect to the Article on Sales (Article 2 [Title 30, chapter 2]): if an exclusive remedy is held to be unconscionable, remedies under this Article are available. Section 2-719 [30-2-719] official comment 1.

Subsection (3), a revision of Section 2-719(3) [30-2-719(3)], makes clear that consequential damages may also be liquidated. Section 2A-504(1) [30-2A-504(1)].

Subsection (4) is a revision of the provisions of Section 2-701 [30-2-701]. This subsection leaves the treatment of default with respect to obligations or promises collateral or ancillary to the lease contract to other law. Sections 2A-103(4) and 1-103 [30-2A-103(4) and 30-1-103]. An example of such an obligation would be that of the lessor to the secured creditor which has provided the funds to leverage the lessor's lease transaction; an example of such a promise would be that of the lessee, as seller, to the lessor, as buyer, in a sale-leaseback transaction.

30-2A-504. Liquidation of damages.

Official Comment

Source: Section 2A-504, U.C.C.

Uniform Statutory Source: Sections 2-718(1), (2), (3) and 2-719(2)[, U.C.C.].

Changes: Substantially rewritten.

Purposes: Many leasing transactions are predicated on the parties' ability to agree to an appropriate amount of damages or formula for damages in the event of default or other act or omission. The rule with respect to sales of goods (Section 2-718 [30-2-718]) may not be sufficiently flexible to accommodate this practice. Thus, consistent with the common law emphasis upon freedom to contract with respect to bailments for hire, this section has created a revised rule that allows greater flexibility with respect to leases of goods.

Subsection (1), a significantly modified version of the provisions of Section 2-718(1) [30-2-718(1)], provides for liquidation of damages in the lease agreement at an amount or by a formula. Section 2-718(1) [30-2-718(1)] does not by its express terms include liquidation by a formula; this change was compelled by modern leasing practice. Subsection (1), in a further expansion of Section 2-718(1) [30-2-718(1)], provides for liquidation of damages for default as well as any other act or omission.

A liquidated damages formula that is common in leasing practice provides that the sum of lease payments past due, accelerated future lease payments, and the lessor's estimated residual interest, less the net proceeds of disposition (whether by sale or re-lease) of the leased goods is the lessor's damages. Tax indemnities, costs, interest and attorney's fees are also added to determine the lessor's damages. Another common liquidated damages formula utilizes a periodic depreciation allocation as a credit to the aforesaid amount in mitigation of a lessor's damages. A third formula provides for a fixed number of periodic payments as a means of liquidating damages. Stipulated loss or stipulated damage schedules are also common. Whether these formulae are enforceable will be determined in the context of each case by applying a standard of reasonableness in light of the harm anticipated when the formula was agreed to. Whether the inclusion of these formulae will affect the classification of the transaction as a lease or a security interest is to be determined by the facts of each case. Section 1-201(37) [30-1-201(37)]. *E.g., In re Noack,* 44 Bankr. 172, 174-75 (Bankr. E.D.Wis. 1984).

This section does not incorporate two other tests that under sales law determine enforceability of liquidated damages, *i.e.,* difficulties of proof of loss and inconvenience or nonfeasibility of otherwise obtaining an adequate remedy. The ability to liquidate damages is critical to modern leasing practice; given the parties' freedom to contract at common law, the policy behind retaining these two additional requirements here was thought to be outweighed. Further, given the expansion of subsection (1) to enable the parties to liquidate the amount payable with respect to an indemnity for loss or diminution of anticipated tax benefits resulted in another change: the last sentence of Section 2-718(1) [30-2-718(1)], providing that a term fixing unreasonably large liquidated damages is void as a penalty, was also not incorporated. The impact of local, state and federal tax laws on a leasing transaction can result in an amount payable with respect to the tax indemnity many times greater than the original purchase price of the goods. By deleting the reference to unreasonably large liquidated damages the parties are free to negotiate a formula, restrained by the rule of reasonableness in this section. These changes should invite the parties to liquidate damages. Peters, *Remedies for Breach of Contracts Relating to the Sale of Goods Under the Uniform Commercial Code: A Roadmap for Article Two,* 73 Yale L.J. 199, 278 (1963).

Subsection (2), a revised version of Section 2-719(2) [30-2-719(2)], provides that if the liquidated damages provision is not enforceable or fails of its essential purpose, remedy may be had as provided in this Article.

Subsection (3)(b) of this section differs from subsection (2)(b) of Section 2-718 [30-2-718(2)(b)]; in the absence of a valid liquidated damages amount or formula the lessor is permitted to retain 20 percent of the present value of the total rent payable under the lease. The alternative limitation of $500 contained in Section 2-718 [30-2-718] is deleted as unrealistically low with respect to a lease other than a consumer lease.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

30-2A-505. Cancellation and termination — effect of cancellation, termination, rescission, or fraud on rights and remedies.

Official Comment

Source: Section 2A-505, U.C.C.

Uniform Statutory Source: Sections 2-106(3) and (4), 2-720 and 2-721[, U.C.C.].

Changes: Revised to reflect leasing practices and terminology.

30-2A-506. Statute of limitations.

Official Comment

Source: Section 2A-506, U.C.C.

Uniform Statutory Source: Section 2-725[, U.C.C.].

Changes: Substantially rewritten.

Purposes: Subsection (1) does not incorporate the limitation found in Section 2-725(1) [30-2-725(1)] prohibiting the parties from extending the period of limitation. Breach of warranty and indemnity claims often arise in a lease transaction; with the passage of time such claims often diminish or are eliminated. To encourage the parties to commence litigation under these circumstances makes little sense.

Subsection (2) states two rules for determining when a cause of action accrues. With respect to default, the rule of Section 2-725(2) [30-2-725(2)] is not incorporated in favor of a more liberal rule of the later of the date when the default occurs or when the act or omission on which it is based is or should have been discovered. With respect to indemnity, a similarly liberal rule is adopted.

30-2A-507. Proof of market rent — time and place.

Official Comment

Source: Section 2A-507, U.C.C.

Uniform Statutory Source: Sections 2-723 and 2-724[, U.C.C.].

Changes: Revised to reflect leasing practices and terminology. Section 2A-519(2) [30-2A-519(2)] provides an example of one of the several times this Article refers to a determination of market rent prevailing at a given time or place. Section 2A-507(2) [30-2A-507(2)].

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

30-2A-508. Lessee's remedies.

Official Comment

Source: Section 2A-508, U.C.C.

Uniform Statutory Source: Sections 2-711 and 2-717[, U.C.C.].

Changes: Substantially rewritten.

Purposes: This section is an index to Sections 2A-509 through 522 [30-2A-509 through 30-2A-522] and their effect on the lessee's rights and remedies after the lessor's default. The lessor and the lessee can otherwise agree; thus, the parties can, among other things, raise or lower the threshold of events that give rise to a lessor's default or create a new scheme of rights and remedies triggered by the occurrence of the default. Sections 2A-103(4) and 1-102(3) [30-2A-103(4) and 30-1-102(3)].

Subsection (1), a substantially rewritten version of the provisions of Section 2-711(1) [30-2-711(1)], lists three cumulative remedies of the lessee where the lessor has failed to deliver conforming goods or has repudiated the contract, or the lessee has rightfully rejected or justifiably revoked. Sections 2A-501(2) and (4) [30-2A-501(2) and (4)]. This Article rejects any doctrine of election of remedy. To determine if one remedy bars another in a particular case is a function of whether the lessee has been put in as good a position as if the lessor had fully performed the lease agreement. Sections 2A-103(4) and 1-106(1) [30-2A-103(4) and 30-1-106(1)]. Note that a special rule has been created regarding the lessee's recovery of rent and security that have been paid in the case of an installment lease—recovery is limited to that which is just under the circumstances. With the various different types of installment leases, no bright line can be created that would operate fairly in all cases; in addition, this provision should further encourage the parties to establish their own rules by agreement.

Subsection (2), a version of the provisions of Section 2-711(2) [30-2-711(2)] revised to reflect leasing terminology, lists two alternative remedies for the recovery of the goods by the lessee; however, each of these remedies is cumulative with respect to those listed in subsection (1).

Subsection (3) is new and allows the lessee access to the remedy scheme of this Article as well as the lease contract if the lessor is in default for reasons other than those stated in subsection (1). Note that the reference to this Article includes supplemental principles of law and equity. Sections 2A-103(4) and 1-103 [30-2A-103(4) and 30-1-103].

Subsection (4) is new and merely adds to the completeness of the index by including a reference to the lessee's recovery of damages upon the lessor's breach of warranty; such breach may not rise to the level of a default by the lessor (*e.g.* breach of an express warranty that the goods subject to the lease conform to description where the non-conformity is such that when measured by objective criteria it reflects a minimal deviation from description) unless the breach is material or unless so provided by the lease agreement.

Subsection (5), a revised version of the provisions of Section 2-711(3) [30-2-711(3)], recognizes, on rightful rejection or justifiable revocation, the lessee's security interest in goods in its possession and control. Section 9-113 [30-9-113, now repealed, see 30-9A-110], which recognized security interests arising under the Article on Sales (Article 2 [Title 30, chapter 2]), was amended with the adoption of this Article to reflect the security interests arising under this Article. Pursuant to Section 2A-511(4) [30-2A-511(4)], a purchaser who purchases goods from the lessee in good faith takes free of any rights of the lessor, or in the case of a finance lease the supplier. Such goods, however, must have been rightfully rejected and disposed of pursuant to Section 2A-511 or 2A-512 [30-2A-511 or 30-2A-512]. However, Section 2A-517(3) [30-2A-517(3)] provides that the lessee will have the same rights and duties with respect to goods where acceptance has been revoked as with respect to goods rejected. Thus, Section 2A-511(4) [30-2A-511(4)] will apply to the lessee's disposition of such goods.

Pursuant to Section 2A-527(5) [30-2A-527(5)], the lessee must account to the lessor for the excess proceeds of such disposition, after satisfaction of the claim secured by the lessee's security interest.

Subsection (6), a slightly revised version of the provisions of Section 2-717 [30-2-717], sanctions a right of set-off by the lessee, subject to the rule of Section 2A-407 [30-2A-407] with respect to irrevocable promises in a finance lease that is not a consumer lease, and further subject to an enforceable "hell or high water" clause in the lease agreement. Section 2A-407 [30-2A-407] official comment. No attempt is made to state how the set-off should occur; this is to be determined by the facts of each case.

There is no special treatment of the finance lease in this section. Absent supplemental principles of law and equity to the contrary, in the case of most finance leases, following the lessee's acceptance of the goods the lessee will have no rights or remedies against the lessor, because the lessor's obligations to the lessee are minimal. Sections 2A-210 and 2A-211(1) [30-2A-210 and 30-2A-211(1)]. Since the lessee will look to the supplier for performance, this is appropriate. Section 2A-209 [30-2A-209].

30-2A-509. Lessee's rights on improper delivery — rightful rejection.

Official Comment

Source: Section 2A-509, U.C.C.

Uniform Statutory Source: Sections 2-601 and 2-602(1)[, U.C.C.].

Changes: Revised to reflect leasing practices and terminology.

30-2A-510. Installment lease contracts — rejection and default.

Official Comment

Source: Section 2A-510, U.C.C.

Uniform Statutory Source: Section 2-612[, U.C.C.].

Changes: Revised to reflect leasing practices and terminology.

30-2A-511. Merchant lessee's duties as to rightfully rejected goods.

Official Comment

Source: Section 2A-511, U.C.C.

Uniform Statutory Source: Sections 2-603 and 2-706(5)[, U.C.C.].

Changes: Revised to reflect leasing practices and terminology. This section, by its terms, applies to merchants as well as others. Thus, in construing the section it is important to note that under this Act the term good faith is defined differently for merchants (Section 2-103(1)(b) [30-2-103(1)(b)]) than for others (Section 1-201(19) [30-1-201(19)]). Section 2A-103(3) and (4) [30-2A-103(3) and (4)].

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

30-2A-512. Lessee's duties as to rightfully rejected goods.

Official Comment

Source: Section 2A-512, U.C.C.

Uniform Statutory Source: Sections 2-602(2)(b) and (c) and 2-604[, U.C.C.].

Changes: Substantially rewritten.

Purposes: The introduction to subsection (1) references goods that threaten to decline in value speedily and not perishables, the reference in Section 2-604 [30-2-604], the statutory analogue. This is a change in style, not substance, as the first phrase includes the second. Subparagraphs (a) and (c) are revised versions of the provisions of Section 2-602(2)(b) and (c) [30-2-602(2)(b) and (2)(c)]. Subparagraph (a) states the rule with respect to the lessee's treatment of goods in its possession following rejection; subparagraph (b) states the rule regarding such goods if the lessor or supplier then fails to give instructions to the lessee. If the lessee performs in a fashion consistent with subparagraphs (a) and (b), subparagraph (c) exonerates the lessee.

30-2A-513. Cure by lessor of improper tender or delivery — replacement.

Official Comment

Source: Section 2A-513, U.C.C.

Uniform Statutory Source: Section 2-508[, U.C.C.].

Changes: Revised to reflect leasing practices and terminology.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

30-2A-514. Waiver of lessee's objections.

Official Comment

Source: Section 2A-514, U.C.C.

Uniform Statutory Source: Section 2-605[, U.C.C.].

Changes: Revised to reflect leasing practices and terminology.

Purposes: The principles applicable to the commercial practice of payment against documents (subsection 2) are explained in official comment 4 to Section 2-605 [30-2-605], the statutory analogue to this section.

Compiler's Comments

2005 Amendment: Chapter 575 in (2) at end substituted "in the documents" for "on the face of the documents". Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-2A-515. Acceptance of goods.

Official Comment

Source: Section 2A-515, U.C.C.

Uniform Statutory Source: Section 2-606[, U.C.C.].

Changes: The provisions of Section 2-606(1)(a) [30-2-606(1)(a)] were substantially rewritten to provide that the lessee's conduct may signify acceptance. Further, the provisions of Section 2-606(1)(c) [30-2-606(1)(c)] were not incorporated as irrelevant given the lessee's possession and use of the leased goods.

30-2A-516. Effect of acceptance of goods — notice of default — burden of establishing default after acceptance — notice of claim or litigation to person answerable over.

Official Comment

Source: Section 2A-516, U.C.C.

Uniform Statutory Source: Section 2-607[, U.C.C.].

Changes: Substantially revised.

Purposes: Subsection (2) creates a special rule for finance leases, precluding revocation if acceptance is made with knowledge of nonconformity with respect to the lease agreement, as opposed to the supply agreement; this is not inequitable as the lessee has a direct claim against the supplier. Section 2A-209(1) [30-2A-209(1)]. Revocation of acceptance of a finance lease is permitted if the lessee's acceptance was without discovery of the nonconformity (with respect to the lease agreement, not the supply agreement) and was reasonably induced by the lessor's assurances. Section 2A-517(1)(b) [30-2A-517(1)(b)]. Absent exclusion or modification, the lessor under a finance lease makes certain warranties to the lessee. Sections 2A-210 and 2A-211(1) [30-2A-210 and 30-2A-211(1)]. Revocation of acceptance is not prohibited even after the lessee's promise has become irrevocable and independent. Section 2A-407 [30-2A-407] official comment. Where the finance lease creates a security interest, the rule may be to the contrary. *General Elec. Credit Corp. of Tennessee v. Ger-Beck Mach. Co.*, 806 F.2d 1207 (3rd Cir. 1986).

Subsection (3)(a) requires the lessee to give notice of default, within a reasonable time after the lessee discovered or should have discovered the default. In all cases, notice of default must be given to the lessor. In the case of a finance lease, notice of default must be given to the lessor and the supplier. The definition of supplier is a person from whom a lessor buys or leases goods to be leased under a finance lease. Section 2A-103(1)(x) [30-2A-103(1)(x)]. Thus, not all sellers or lessors of goods to be leased are included within the set of persons to be given notice of default, as suppliers.

Subsection (3)(b) requires the lessee to give the lessor notice of litigation for infringement or the like. There is an exception created in the case of a consumer lease. While such an exception was considered for a finance lease, it was not created because it was not necessary—the lessor in a finance lease does not give a warranty against infringement. Section 2A-211(2) [30-2A-211(2)]. Even though not required under subsection (3)(b), the lessee who takes under a finance lease should consider giving notice of litigation for infringement or the like to the supplier, because the lessee obtains the benefit of the suppliers' promises subject to the suppliers' defenses or claims. Sections 2A-209(1) and 2-607(3)(b) [30-2A-209(1) and 30-2-607(3)(b)].

30-2A-517. Revocation of acceptance of goods.

Official Comment

Source: Section 2A-517, U.C.C.

Uniform Statutory Source: Section 2-608[, U.C.C.].

Changes: Revised to reflect leasing practices and terminology. Note that in the case of a finance lease the lessee retains a limited right to revoke acceptance. Sections 2A-517(1)(b) and 2A-516 [30-2A-517(1)(b) and 30-2A-516] official comment.

30-2A-518. Cover — substitute goods.

Official Comment

Source: Section 2A-518, U.C.C.

Uniform Statutory Source: Section 2-712[, U.C.C.].

Changes: Substantially revised.

Purposes: Subsection (1) allows the lessee to take action to fix its damages after default by the lessor. Such action may consist of the purchase or lease of goods. The decision to cover is a function of commercial judgment, not a statutory mandate replete with sanctions for failure to comply. *Cf.* Section 9-507 [30-9-507, now repealed, see 30-9A-625 and 30-9A-627].

Subsection (2) states a rule for determining the amount of lessee's damages provided that there is no agreement to the contrary. The lessee's damages will be established using the new lease agreement as a measure if the following three criteria are met: (i) the lessee's cover is by lease agreement, (ii) the lease agreement is substantially similar to the original lease agreement, and (iii) such cover was effected in good faith, and in a commercially reasonable manner. Thus, the lessee will be entitled to recover from the lessor the present value, as of the date of default, of the difference between the rent reserved under the new lease and the original lease, together with incidental or consequential damages less expenses saved in consequence of the lessor's default. Note that the reference in Section 2A-518(2)(a) [30-2A-518(2)(a)] is to the date of default not to the date of an event of default. An event of default under a lease agreement becomes a default under a lease agreement only after the expiration of any relevant period of grace and compliance with any notice requirements under this Article and the lease agreement. American Bar Foundation, *Commentaries on Indentures*, § 5-1, at 216-217 (1971). Section 2A-501(1) [30-2A-501(1)]. This conclusion is also a function of whether, as a matter of fact or law, the event of default has been waived, suspended or cured. Sections 2A-103(4) and 1-103 [30-2A-103(4) and 30-1-103, 2003 MCA; see 2005 amendment]. If the lessee's cover does not satisfy the criteria of subsection (2), Section 2A-519 [30-2A-519] governs.

Two of the three criteria to be met by the lessee are familiar, but the concept of the new lease agreement being substantially similar to the original lease agreement is not. Given the many variables facing a party who intends to lease goods and the rapidity of change in the market place, the policy decision was made not to draft with specificity. It was thought unwise to seek to establish certainty at the cost of fairness. Thus, the decision of whether the new lease agreement is substantially similar to the original will be determined case by case.

While the section does not draw a bright line, it is possible to describe some of the factors that should be considered in finding that a new lease agreement is substantially similar to the original. First, the goods subject to the new lease agreement should be examined. For example, in a lease of computer equipment the new lease might be for more modern equipment. However, it may be that at the time of the lessor's breach it was not possible to obtain the same type of goods in the market place. Because the lessee's remedy under Section 2A-519 [30-2A-519] is intended to place the lessee in essentially the same position as if he had covered, if goods similar to those to have been delivered under the original lease are not available, then the computer equipment in this hypothetical should qualify as a commercially reasonable substitute. *See* Section 2-712(1) [30-2-712(1)].

Second, the various elements of the new lease agreement should also be examined. Those elements include the term of the new lease (because the damages are calculated under subsection (2) as the difference between the total rent payable for the entire term of the new lease agreement and the remaining term of the original lease); the presence or absence of options to purchase or release; the lessor's representations, warranties and covenants to the lessee, as well as those to be provided by the lessee to the lessor; and the services, if any, to be provided by the lessor or by the lessee. All of these factors allocate cost and risk between the lessor and the lessee and thus affect the amount of rent to be paid.

Having examined the goods and the agreement, the test to be applied is whether, in light of these comparisons, the new lease agreement is substantially similar to the original lease agreement. These findings should not be made with scientific precision, as they are a function of economics, nor should they be made independently with respect to the goods and each element of the agreement, as it is important that a sense of commercial judgment pervade the finding. To establish the new lease as a proper measure of damage under subsection (2), these factors, taken as a whole, must result in a finding that the new lease agreement is substantially similar to the original.

Compiler's Comments

2005 Amendment: Chapter 575 in (2) in second parenthetical item deleted reference to 30-1-102(3). Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-2A-519. Lessee's damages for nondelivery, repudiation, default, and breach of warranty in regard to accepted goods.

Official Comment

Source: Section 2A-519, U.C.C.

Uniform Statutory Source: Sections 2-713 and 2-714[, U.C.C.].

Changes: Substantially revised.

Purposes: Subsection (1), a revised version of the provisions of Section 2-713(1) [30-2-713(1)], states the basic rule governing the measure of lessee's damages for non-delivery or repudiation by the lessor or for rightful rejection or revocation of acceptance by the lessee. This measure will apply, absent agreement to the contrary, if the lessee does not cover or if the cover does not qualify under Section 2A-518 [30-2A-518]. There is no sanction for cover that does not qualify.

The measure of damage is the present value, as of the date of default, of the difference between market rent and original rent for the remaining term of the lease, less expenses saved in consequence of the default. Note that the reference in Section 2A-519(1) [30-2A-519(1)] is to the date of default not to the date of an event of default. An event of default under a lease agreement becomes a default under a lease agreement only after the expiration of any relevant period of grace and compliance with any notice requirements under this Article and the lease agreement. American Bar Foundation, *Commentaries on Indentures*, § 5-1, at 216-217 (1971). Section 2A-501(1) [30-2A-501(1)]. This conclusion is also a function of whether, as a matter of fact or law, the event of default has been waived, suspended or cured. Sections 2A-103(4) and 1-103 [30-2A-103(4) and 30-1-103, 2003 MCA; see 2005 amendment].

Subsection (2), a revised version of the provisions of Section 2-713(2) [30-2-713(2)], states the rule with respect to determining market rent.

Subsection (3), a revised version of the provisions of Section 2-714(1) and (3) [30-2-714(1) and (3)], states the measure of damages where goods have been accepted and acceptance is not revoked. The measure in essence is the loss, in the ordinary course of events, flowing from the default.

Subsection (4), a revised version of the provisions of Section 2-714(2) [30-2-714(2)], states the measure of damages for breach of warranty. The measure in essence is the present value of the difference between the value of the goods accepted and of the goods if they had been as warranted.

Compiler's Comments

2005 Amendment: Chapter 575 in (1) in second parenthetical item deleted reference to 30-1-102(3). Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-2A-520. Lessee's incidental and consequential damages.

Official Comment

Source: Section 2A-520, U.C.C.

Uniform Statutory Source: Section 2-715[, U.C.C.].

Changes: Revised to reflect leasing terminology and practices.

Purposes: Subsection (1), a revised version of the provisions of Section 2-715(1) [30-2-715(1)], lists some examples of incidental damages resulting from a lessor's default; the list is not exhaustive. Subsection (1) makes clear that it applies not only to rightful rejection, but also to justifiable revocation.

Subsection (2), a revised version of the provisions of Section 2-715(2) [30-2-715(2)], lists some examples of consequential damages resulting from a lessor's default; the list is not exhaustive.

30-2A-521. Lessee's right to specific performance or replevin.

Official Comment

Source: Section 2A-521, U.C.C.

Uniform Statutory Source: Section 2-716[, U.C.C.].

Changes: Revised to reflect leasing practices and terminology, and to expand the reference to the right of replevin in subsection (3) to include other similar rights of the lessee.

30-2A-522. Lessee's right to goods on lessor's insolvency.

Official Comment

Source: Section 2A-522, U.C.C.

Uniform Statutory Source: Section 2-502[, U.C.C.].

Changes: Revised to reflect leasing practices and terminology.

30-2A-523. Lessor's remedies.

Official Comment

Source: Section 2A-523, U.C.C.

Uniform Statutory Source: Section 2-703[, U.C.C.].

Changes: Substantially revised.

Purposes: This section is an index to Sections 2A-524 through 2A-531 [30-2A-524 through 30-2A-531] and their effect on the lessor's rights and remedies upon the lessee's default.

The lessor and the lessee can agree otherwise; thus, the parties can, among other things, raise or lower the threshold that gives rise to lessee's default or create a new scheme of rights and remedies triggered by the occurrence of the default. Sections 2A-103(4) and 1-102(3) [30-2A-103(4) and 30-1-102(3)].

Subsection (1), a substantially rewritten version of Section 2-703 [30-2-703], lists various cumulative remedies of the lessor where the lessee wrongfully rejects or revokes acceptance, fails to make a payment when due, or repudiates. Section 2A-501(4) [30-2A-501(4)].

This Article rejects the doctrine of election of remedy. Whether, in a particular case, one remedy bars another, is a function of whether lessor has been put in as good a position as if the lessee had fully performed the lease contract. Sections 2A-103(4) and 1-106(1) [30-2A-103(4) and 30-1-106(1)].

Hypothetical: 1. To better understand the application of subparagraphs (a) through (e) [subsections (1)(a) through (1)(e) of this section], it is useful to review a hypothetical. Assume that A is a merchant in the business of selling and leasing new bicycles of various types. B is about to engage in the business of subleasing bicycles to summer residents of and visitors to an island resort. A, as lessor, has agreed to lease 60 bicycles to B. While there is one master lease, deliveries and terms are staggered. 20 bicycles are to be delivered by A to B's island location on June 1; the term of the lease of these bicycles is four months. 20 bicycles are to be delivered by A to B's island location on July 1; the term of the lease of these bicycles is three months. Finally, 20 bicycles are to be delivered by A to B's island location on August 1; the term of the lease of these bicycles is two months. B is obligated to pay rent to A on the 15th day of each month during the term for the lease. Rent is $50 per month, per bicycle. B has no option to purchase or release and must return the bicycles to A at the end of the term, in good condition, reasonable wear and tear excepted. Since the retail price of each bicycle is $400 and bicycles used in the retail rental business have a useful economic life of 36 months, this transaction creates a lease. Sections 2A-103(1)(j) and 1-201(37) [30-2A-103(1)(j) and 30-1-201(37)].

2. A's current inventory of bicycles is not large. Thus, upon signing the lease with B in February, A agreed to purchase 60 new bicycles from A's principal manufacturer, with special

instructions to drop ship the bicycles to B's island location in accordance with the delivery schedule set forth in the lease.

3. The first shipment of 20 bicycles was received by B on May 21. B inspected the bicycles, accepted the same as conforming to the lease and signed a receipt of delivery and acceptance. However, due to poor weather that summer, business was terrible and B was unable to pay the rent due on June 15. Pursuant to the lease A sent B notice of default and proceeded to enforce his rights and remedies against B.

4. A's counsel first advised A that under Section 2A-510(2) [30-2A-510(2)] and the terms of the lease B's failure to pay was a default with respect to the whole. Thus, to minimize A's continued exposure, A was advised to take possession of the bicycles. If A had possession of the goods A could refuse to deliver. Section 2A-525(1) [30-2A-525(1)]. However, the facts here are different. With respect to the bicycles in B's possession, A has the right to take possession of the bicycles, without breach of the peace. Section 2A-525(2) [30-2A-525(2)]. If B refuses to allow A access to the bicycles, A can proceed by action, including replevin or injunctive relief.

5. With respect to the 40 bicycles that have not been delivered, this Article provides various alternatives. First, assume that 20 of the remaining 40 bicycles have been manufactured and delivered by the manufacturer to a carrier for shipment to B. Given the size of the shipment, the carrier was using a small truck for the delivery and the truck had not yet reached the island ferry when the manufacturer (at the request of A) instructed the carrier to divert the shipment to A's place of business. A's right to stop delivery is recognized under these circumstances. Section 2A-526(1) [30-2A-526(1)]. Second, assume that the 20 remaining bicycles were in the process of manufacture when B defaulted. A retains the right (as between A as lessor and B as lessee) to exercise reasonable commercial judgment whether to complete manufacture or to dispose of the unfinished goods for scrap. Since A is not the manufacturer and A has a binding contract to buy the bicycles, A elected to allow the manufacturer to complete the manufacture of the bicycles, but instructed the manufacturer to deliver the completed bicycles to A's place of business. Section 2A-524(2) [30-2A-524(2)].

6. Thus, so far A has elected to exercise the remedies referred to in subparagraphs (b) through (d) in subsection (1). None of these remedies bars any of the others because A's election and enforcement merely resulted in A's possession of the bicycles. Had B performed A would have recovered possession of the bicycles. Thus A is in the process of obtaining the benefit of his bargain.

7. A's counsel next would determine what action, if any, should be taken with respect to the goods. As stated in subparagraph (e) [subsection (1)(e) of this section] and as discussed fully in Section 2A-527(1) [30-2A-527(1)] the lessor may, but has no obligation to, dispose of the goods by lease, sale or otherwise. In this case, since A is in the business of leasing and selling bicycles, A will probably inventory the 60 bicycles for its retail trade.

8. A's counsel then will determine which of the various, alternate means of ascertaining A's claim for damages against B will be computed. Subparagraph (e) [subsection (1)(e) of this section] catalogues each relevant section. First, under Section 2A-527(2) [30-2A-527(2)] the amount of A's claim will be computed by comparing the original lease between A and B with any subsequent lease of the bicycles but only if the subsequent lease is substantially similar to the lease contract. While the section does not define this term, the official comment does establish some parameters. If, however, A elects to lease the bicycles to his retail trade, it is unlikely that the resulting lease will be substantially similar to the original, as leases to retail customers are considerably different from leases to wholesale customers like B. If, however, the leases were substantially similar, the damage claim is for accrued and unpaid rent, the present value of the difference between the rent reserved under both leases for the balance of their terms, together with incidental damages less expenses saved in consequence of the lessee's default.

9. If the new lease is not substantially similar or if A elects to sell the bicycles or to hold the bicycles, damages are computed under Section 2A-528 or 2A-529 [30-2A-528 or 30-2A-529].

10. If A elects to pursue his claim under Section 2A-528(1) [30-2A-528(1)] the damage rule is the same as that stated in Section 2A-527(2) [30-2A-527(2)] except that the standard of comparison is not the rent reserved under a substantially similar lease entered into by the lessor but a market rent, as defined in Section 2A-507 [30-2A-507(2)]. Further, if the facts of this hypothetical were more elaborate A may be able to establish that the measure of damage under subsection (1) is inadequate to put him in the same position that B's performance would have, in which case A can claim his lost profits.

11. Yet another alternative for computing A's damage claim against B is prescribed by Section 2A-529 [30-2A-529]. However, to use this formula A must, among other things, hold

the bicycles identified in the lease contract for B. Since this would include all 60 bicycles and A is a merchant, it is unlikely to occur. Further, subsection (1)(a), which in essence allows A to receive the present value of the rent reserved under the lease, would in this case apply only to the 20 bicycles accepted by B in May. With respect to the remaining 40 bicycles, subsection 1(b) will apply only if A is unable to dispose of them, or circumstances indicate the effort will be unavailing, in which case the damage formula identical to the one set forth in (1)(a) will apply. At any time up to collection of a judgment by A against B, A may dispose of the bicycles. In such case A's claim for damages against B is governed by Section 2A-527 or 2A-528 [30-2A-527 or 30-2A-528]. Section 2A-529(3) [30-2A-529(3)]. The resulting recalculation of claim should reduce the amount recoverable by A against B. However, the nature of the post-judgment proceedings to resolve this issue, and the sanctions for abuse, if any, will be determined by other law.

12. Finally, if the lease agreement had provided, A's claim against B would not be determined under any of these statutory formulae, but pursuant to a liquidated damages clause. Section 2A-504(1) [30-2A-504(1)].

13. These various methods of computing A's damage claim against B are alternatives. However, the pursuit of any one of these alternatives is not a bar to, nor has it been barred by, A's earlier action to obtain possession of the 60 bicycles. These formulae, which vary as a function of an overt or implied mitigation of damage theory, focus on allowing A a recovery of the benefit of his bargain with B. Had B performed, A would have received the rent as well as the return of the 60 bicycles at the end of the term.

14. Finally, A's counsel should also advise A of his right to cancel the lease contract under subparagraph (a) [subsection (1) (a) of this section]. Section 2A-505(1) [30-2A-505(1)]. Cancellation will discharge all existing obligations but preserve A's rights and remedies.

15. Subsection (2) is new and allows the lessor access to the remedy scheme of this Article as well as that contained in the lease contract if the lessee is in default for reasons other than those stated in subsection (1). Note that the reference to this Article includes supplementary principles of law and equity, *e.g.*, fraud, misrepresentation and duress. Sections 2A-103(4) and 1-103 [30-2A-103(4) and 30-1-103].

16. There is no special treatment of the finance lease in this section. Absent supplementary principles of law to the contrary, in most cases the supplier will have no rights or remedies against the defaulting lessee. Section 2A-209(2)(b) [30-2A-209(2)(b)]. Given that the supplier will look to the lessor for payment, this is appropriate. However, there is a specific exception to this rule with respect to the right to identify goods to the lease contract. Section 2A-524(2) [30-2A-524(2)]. The parties are free to create a different result in a particular case. Sections 2A-103(4) and 1-102(3) [30-2A-103(4) and 30-1-102(3)].

30-2A-524. Lessor's right to identify goods to lease contract.

Official Comment

Source: Section 2A-524, U.C.C.

Uniform Statutory Source: Section 2-704[, U.C.C.].

Changes: Revised to reflect leasing practices and terminology.

30-2A-525. Lessor's right to possession of goods.

Official Comment

Source: Section 2A-525, U.C.C.

Uniform Statutory Source: Section 2-702(1) and 9-503[, U.C.C.].

Changes: Substantially revised.

Purposes: Subsection (1), a revised version of the provisions of Section 2-702(1) [30-2-702(1)], allows the lessor to refuse to deliver goods if the lessee is insolvent. Note that the provisions of Section 2-702(2) [30-2-702(2)], granting the unpaid seller certain rights of reclamation, were not incorporated in this section. Subsection (2) made this unnecessary.

Subsection (2), a revised version of the provisions of Section 9-503 [30-9-503, now repealed, see 30-9A-609], allows the lessor, on default by the lessee, the right to take possession of or reclaim the goods; since the lessee's insolvency is an event of default in a standard lease agreement, subsection (2) is the functional equivalent of Section 2-702(2) [30-2-702(2)]. Further, subsection (2) sanctions the classic crate and delivery clause obligating the lessee to assemble the goods and to make them available to the lessor. Finally, the lessor may leave the goods in place, render them unusable (if they are goods employed in trade or business), and dispose of them on the lessee's premises.

Subsection (3), a revised version of the provisions of Section 9-503 [30-9-503, now repealed, see 30-9A-609], allows the lessor to proceed under subsection (2) without judicial process, absent breach of the peace, or by action. Sections 2A-501(3), 2A-103(4) and 1-201(1) [30-2A-501(3), 30-2A-103(4), and 30-1-201(1)]. In the appropriate case action includes injunctive relief. *Clark Equip. Co. v. Armstrong Equip. Co.*, 431 F.2d 54 (5th Cir.1970), *cert. denied*, 402 U.S. 909 (1971). This Section, as well as a number of other Sections in this Part, are included in the Article to codify the lessor's common law right to protect the lessor's reversionary interest in the goods. Section 2A-103(1)(q) [30-2A-103(1)(q)]. These Sections are intended to supplement and not displace principles of law and equity with respect to the protection of such interest. Sections 2A-103(4) and 1-103 [30-2A-103(4) and 30-1-103]. Such principles apply in many instances, *e.g.*, loss or damage to goods if risk of loss passes to the lessee, failure of the lessee to return goods to the lessor in the condition stipulated in the lease, and refusal of the lessee to return goods to the lessor after termination or cancellation of the lease.

30-2A-526. Lessor's stoppage of delivery in transit or otherwise.

Official Comment

Source: Section 2A-526, U.C.C.

Uniform Statutory Source: Section 2-705[, U.C.C.].

Changes: Revised to reflect leasing practices and terminology.

Compiler's Comments

2005 Amendment: Chapter 575 in (2)(c) at end substituted "a warehouse" for "warehouseman". Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-2A-527. Lessor's rights to dispose of goods.

Official Comment

Source: Section 2A-527, U.C.C.

Uniform Statutory Source: Section 2-706(1), (5) and (6)[, U.C.C.].

Changes: Substantially revised.

Purposes: Subsection (1), a revised version of the first sentence of subsection 2-706(1) [30-2-706(1)], allows the lessor the right to dispose of goods after default by the lessee (even if the goods remain in the lessee's possession—Section 2A-525(2) [30-2A-525(2)]) or after the lessor refuses to deliver or takes possession of the goods. The lessor's decision to exercise this right is a function of a commercial judgment, not a statutory mandate replete with sanctions for failure to comply. *Cf.* Section 9-507 [30-9-507, now repealed, see 30-9A-625 and 30-9A-627]. As the owner of the goods, in the case of a lessor, or as the prime lessee of the goods, in the case of a sublessor, compulsory disposition of the goods is inconsistent with the nature of the interest held by the lessor or the sublessor and is not necessary because the interest held by the lessee or the sublessee is not protected by a right of redemption under the common law or this Article. Subsection 2A-527(5) [30-2A-527(5)].

The rule for determining the measure of damages recoverable by the lessor against the lessee is a function of several variables. If the lessor has elected to effect disposition under subsection (1) and such disposition is by lease that qualifies under subsection (2), the measure of damages set forth in subsection (2) will apply, absent agreement to the contrary. Sections 2A-504, 2A-103(4) and 1-102(3) [30-2A-504, 30-2A-103(4), and 30-1-102(3), 2003 MCA; see 2005 amendment].

The lessor's damages will be established using the new lease agreement as a measure if the following three criteria are satisfied: (i) the lessor disposed of the goods by lease, (ii) the lease agreement is substantially similar to the original lease agreement, and (iii) such disposition was in good faith, and in a commercially reasonable manner. Thus, the lessor will be entitled to recover from the lessee the accrued and unpaid rent as of the date of default, and the present value, as of the date of default, of the difference between the rent reserved under the new lease and the original lease, together with incidental damages less expenses saved in consequence of the lessee's default. If the lessor's disposition does not satisfy the criteria of subsection (2), the lessor may calculate its claim against the lessee pursuant to Section 2A-528 [30-2A-528]. Section 2A-523(1)(e) [30-2A-523(1)(e)]. Note that the reference in Section 2A-527(2)(a) and (b)

[30-2A-527(2)(a) and (2)(b)] is to the date of default not to the date of an event of default. An event of default under a lease agreement becomes a default under a lease agreement only after the expiration of any relevant period of grace and compliance with any notice requirements under this Article and the lease agreement. American Bar Foundation, *Commentaries on Indentures*, § 5-1, at 216-217 (1971). Section 2A-501(1) [30-2A-501(1)]. This conclusion is also a function of whether, as a matter of fact or law, the event of default has been waived, suspended or cured. Sections 2A-103(4) and 1-103 [30-2A-103(4) and 30-1-103].

Two of the three criteria to be met by the lessor are familiar, but the concept of the new lease agreement that is substantially similar to the original lease agreement is not. Given the many variables facing a party who intends to lease goods and the rapidity of change in the market place, the policy decision was made not to draft with specificity. It was thought unwise to seek to establish certainty at the cost of fairness. The decision of whether the new lease agreement is substantially similar to the original will be determined case by case.

While the section does not draw a bright line, it is possible to describe some of the factors that should be considered in a finding that a new lease agreement is substantially similar to the original. The various elements of the new lease agreement should be examined. Those elements include the term of the new lease (because the damages are calculated under subsection (2) as the difference between the total rent payable for the entire term of the new lease agreement and the remaining lease term of the original lease); the options to purchase or release; the lessor's representations, warranties and covenants to the lessee as well as those to be provided by the lessee to the lessor; and the services, if any, to be provided by the lessor or by the lessee. All of these factors allocate cost and risk between the lessor and the lessee and thus affect the amount of rent to be paid. These findings should not be made with scientific precision, as they are a function of economics, nor should they be made independently, as it is important that a sense of commercial judgment pervade the finding. *See* Section 2A-507(2) [30-2A-507(2)]. To establish the new lease as a proper measure of damage under subsection (2), these various factors, taken as a whole, must result in a finding that the new lease agreement is substantially similar to the original.

The following hypothetical illustrates the difficulty of providing a bright line. Assume that A buys a jumbo tractor for $1 million and then leases the tractor to B for a term of 36 months. The tractor is delivered to and is accepted by B on May 1. On June 1 B fails to pay the monthly rent to A. B returns the tractor to A, who immediately releases the tractor to C for a term identical to the term remaining under the lease between A and B. All terms and conditions under the lease between A and C are identical to those under the original lease between A and B, except that C does not provide any property damage or other insurance coverage, and B agreed to provide complete coverage. Coverage is expensive and difficult to obtain. The new lease should be viewed as not substantially similar to the original. However, if the lessor seeks a recovery under Section 2A-528 [30-2A-528] the new lease can be introduced into evidence to establish market rent (Section 2A-507 [30-2A-507]), with a proper allowance for the lessor's cost of replacing the lost insurance coverage.

Subsection (3), which is new, provides that if the lessor's disposition is by lease that does not qualify under subsection (2), or is by sale or otherwise, Section 2A-528 [30-2A-528] governs.

Subsection (4), a revised version of subsection 2-706(5) [30-2-706(5)], applies to protect a subsequent buyer or lessee who buys or leases from the lessor in good faith and for value, pursuant to a disposition under this section. Note that by its terms, the rule in subsection 2A-304(1) [30-2A-304(1)], which provides that the subsequent lessee takes subject to the original lease contract, is controlled by the rule stated in this subsection.

Subsection (5), a revised version of subsection 2-706(6) [30-2-706(6)], provides that the lessor is not accountable to the lessee for any profit made by the lessor on a disposition. This rule follows from the fundamental premise of the bailment for hire that the lessee under a lease of goods has no equity of redemption to protect.

Compiler's Comments

2005 Amendment: Chapter 575 in (2) in second parenthetical item deleted reference to 30-1-102(3). Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does

not apply to a right of action that has accrued before [the effective date of this act].” Effective October 1, 2005.

30-2A-528. Lessor’s damages for nonacceptance, failure to pay, repudiation, or other default.

Official Comment

Source: Section 2A-528, U.C.C.

Uniform Statutory Source: Section 2-708[, U.C.C.].

Changes: Substantially revised.

Purposes: Subsection (1), a substantially revised version of Section 2-708(1) [30-2-708(1)], states the basic rule governing the measure of lessor’s damages for non-acceptance or repudiation by the lessee; repudiation is defined (Section 2A-402 [30-2A-402]) to include the lessee’s post acceptance default for failure to pay rent and the like. Section 2A-523(1) [30-2A-523(1)]. This measure will apply if the lessor elects to retain the goods (whether undelivered, returned by the lessee, or repossessed by the lessor after acceptance and default by the lessee) or if the lessor’s disposition does not qualify under subsection 2A-527(2) [30-2A-527(2)]. Section 2A-527(3) [30-2A-527(3)]. Note that under some of these conditions, the lessor may recover damages from the lessee pursuant to the rule set forth in Section 2A-529 [30-2A-529]. There is no sanction for disposition that does not qualify under subsection 2A-527(2) [30-2A-527(2)]. Application of the rule set forth in this section is subject to agreement to the contrary. Sections 2A-504, 2A-103(4) and 1-102(3) [30-2A-504, 30-2A-103(4), and 30-1-102(3), 2003 MCA; see 2005 amendment].

The measure of damage is the accrued and unpaid rent as of the date of default together with the present value, as of the date of default, of the difference between market rent and the original rent for the remaining term of the lease, and incidental damages, less expenses saved in consequence of the default. Note that the reference in Section 2A-528(1)(a) and (b) [30-2A-528(1)(a) and (1)(b)] is to the date of default not to the date of an event of default. An event of default under a lease agreement becomes a default under a lease agreement only after the expiration of any relevant period of grace and compliance with any notice requirements under this Article and the lease agreement. American Bar Foundation, *Commentaries on Indentures*, § 5-1, at 216-217 (1971). Section 2A-501(1) [30-2A-501(1)]. This conclusion is also a function of whether, as a matter of fact or law, the event of default has been waived, suspended or cured. Sections 2A-103(4) and 1-103 [30-2A-103(4) and 30-1-103].

Market rent will be computed pursuant to Section 2A-507 [30-2A-507]. In the case of a default by the lessee, the time for tender should be interpreted as the date of the default. If, as of the date of default, the lessor has attempted and failed to obtain possession of the goods, the lessor has, among various additional rights and remedies, a cause of action against the lessee for damages due to loss of use of possession of the goods between the date of default and the date the lessor obtains possession of the goods. Sections 2A-525(3), 2A-103(4), 1-201(1) [30-2A-525(3),

30-2A-103(4), and 30-1-201(1)]. *See also* Section 2A-530 [30-2A-530]. This conclusion is critical to an important policy decision to protect the lessor’s residual interest in the goods. Section 2A-103(1)(q) [30-2A-103(1)(q)].

Subsection (2), a somewhat revised version of the provisions of subsection 2-708(2) [30-2-708(2)], states a measure of damages which applies in each case that subsection (1) applies but the measure of damages in subsection (1) is inadequate to put the lessor in as good a position as performance would have. The measure of damage is the lessor’s profit, including overhead, together with incidental damages, with allowance for costs reasonably incurred and credit for payments or proceeds of disposition. In determining the amount of due credit with respect to proceeds of disposition a proper value should be attributed to the lessor’s residual interest in the goods. Sections 2A-103(1)(q) and 2A-507(4) [30-2A-103(1)(q) and 30-2A-507(4)].

In calculating profit, a court should include any expected appreciation of the goods, *e.g.* the foal of a leased brood mare. Because this subsection is intended to give the lessor the benefit of the bargain, a court should consider any reasonable benefit or profit expected by the lessor from the performance of the lease agreement. *See Honeywell, Inc. v. Lithonia Lighting, Inc.*, 317 F.Supp. 406, 413 (N.D.Ga.1970); *Locks v. Wade*, 36 N.J.Super. 128, 131, 114 A.2d 875, 877 (Super.Ct.App.Div.1955). Further, in calculating profit the concept of present value should be given effect. *Taylor v. Commercial Credit Equip. Corp.*, 170 Ga.App. 322, 316 S.E.2d 788 (Ct. App.1984). *See generally* Section 2A-103(1)(u) [30-2A-103(1)(u)].

Compiler’s Comments

2005 Amendment: Chapter 575 in (1) in second parenthetical item deleted reference to 30-1-102(3). Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-2A-529. Lessor's action for rent.

Official Comment

Source: Section 2A-529, U.C.C.

Uniform Statutory Source: Section 2-709[, U.C.C.].

Changes: Substantially revised.

Purposes: Subsection (1) provides another method of determining the measure of lessor's damages after default by the lessee. Absent agreement to the contrary (Section 2A-504 [30-2A-504]), this Article provides the lessor, in this section and the two preceding sections, three alternate methods of computing damages recoverable from the defaulting lessee (Section 2A-523(1)(e) [30-2A-523(1)(e)]). This section, as well as the two preceding sections, applies to goods subject to the lease, even if such goods have been repossessed from the lessee or otherwise (Section 2A-525(2) [30-2A-525(2)]). This is a departure from Section 2-709 [30-2-709], the statutory analogue. The departure is not surprising given the essential difference between a sale and a lease.

Absent the right to repossess the goods, the recovery stated in subsection (1)(a) would not compensate the lessor for his or her loss. Consider a lease of a carpet cleaner by A to B, for a term of two days. A purchased the carpet cleaner for $500.00. The rent for the two day term is $75.00. If B defaulted by not paying the rent and refusing to return the carpet cleaner and A was not allowed to repossess the carpet cleaner, the measure of damage stated in this section would allow a recovery of not more than $75.00, together with incidental damages. The rule stated in this Article, which allows the lessor the right to repossess the goods from the lessee and to recover damages, is consistent with the lessor's ownership of the goods. DeKoven, Proceedings After Default by the Lessee Under a True Lease of Equipment, in 1C P. Coogan, W. Hogan, D. Vagts, *Secured Transactions Under the Uniform Commercial Code*, § 29B.06[4] (1986). The statutory analogue, Section 2-709 [30-2-709], only provides an action for the price of the goods sold, which is consistent with the seller's agreement to dispose of all of his or her right, title and interest in the goods to the buyer. That measure of damage would not have been appropriate here as the lessor's agreement is to dispose of possession and use of the goods for a term; the bargain includes the return of the goods at the end of the term. It would be anomalous to allow the lessee to improve on the bargain, i.e. retain the goods, solely by virtue of his or her default, even if that had been balanced by allowing the lessor to sue to recover the price or value of the goods.

The measure of the lessor's damages under this section is a function of a two-part rule. First, subparagraph (1)(a) establishes a rule of recovery with respect to goods accepted by the lessee (even if repossessed by the lessor) and with respect to conforming goods lost or damaged within a commercially reasonable time after risk of loss passed to the lessee. Thus, reading subsections (1), (2) and (3) together, if accepted goods are repossessed by the lessor and the lessor holds the goods for the lessee for the balance of the term, lessor's damages will be calculated pursuant to subsection (1)(a); if the lessor leases, sells or otherwise disposes of the goods, subsection (1)(a) is inapplicable and the lessor's damages will be calculated pursuant to Section 2A-528 [30-2A-528], unless the lessor's disposition was by a substantially similar lease, in which case Section 2A-527(2) [30-2A-527(2)] applies. Second, subparagraph (1)(b) establishes a rule of recovery with respect to goods identified to the lease contract (but not accepted by the lessee—*see* subparagraph (1)(a)) only if the lessor is unable, after reasonable effort, to dispose of them at a reasonable price, or if circumstances indicate the effort would be unavailing.

As a condition to the lessor's election to employ the method to measure the lessor's claim against the lessee set forth in subsection (1), the lessor must comply with subsection (2), which provides that, with one exception, goods identified to the lease contract and in the lessor's control (whether as a result of repossession or otherwise) must be held for the lessee for the balance of the lease term. This eliminates the possibility of a double recovery by the lessor and preserves the value of the leasehold estate to the lessee.

Subsection (3) creates an exception to the requirement set forth as a condition to subsection (1), that goods identified to the contract and in the lessor's control be held by the lessor. (Section 2A-529(2) [30-2A-529(2)]). If the lessor disposes of those goods prior to collection of the judgment (whether as a matter of law or agreement), the lessor's recovery is governed by the measure of damages in Section 2A-527 [30-2A-527] if the disposition is by lease that is substantially similar to the original lease, or otherwise by the measure of damages in Section 2A-528 [30-2A-528]. Section 2A-523 [30-2A-523] official comment Number 11.

The relationship between subsections (2) and (3) is best stated by examining a hypothetical. Assume the lease is for a term of two years and after default by the lessee the lessor recovers the goods from the lessee and obtains judgment against the lessee for damages pursuant to subsection (1). If the lessor holds the goods so recovered until the end of the two year term, any subsequent disposition will have no effect on the lessor's judgment. If, however, the lessor determines that the lessee is judgment proof, the lessor might be wise to dispose of the goods before the end of the remaining lease term, even though the amount that the lessor then will be allowed to recover from the lessee, as determined by the provisions of Section 2A-527 or 2A-528 [30-2A-527 or 30-2A-528], is less than the judgment. Subsection (3) allows the lessor to make this election at any time before collection of the judgment.

Subsection (4), which is new, further reinforces the requisites of Subsection (2). In the event the judgment for damages obtained by the lessor against the lessee pursuant to subsection (1) is satisfied, the lessee regains the right to use and possession of the remaining goods for the balance of the original lease term; a partial satisfaction of the judgment creates no right in the lessee to use and possession of the goods.

The relationship between subsections (2) and (4) is important to understand. Subsection (2) requires the lessor to hold for the lessee identified goods in the lessor's possession. Absent agreement to the contrary, whether in the lease or otherwise, under most circumstances the requirement that the lessor hold the goods for the lessee for the term will mean that the lessor is not allowed to use them. Sections 2A-103(4) and 1-203 [30-2A-103(4) and 30-1-203]. Further, the lessor's use of the goods could be viewed as a disposition of the goods that would bar the lessor from recovery under this section, remitting the lessor to the two preceding sections for a determination of the lessor's claim for damages against the lessee.

Subsection (5), the analogue of subsection 2-709(3) [30-2-709(3)], further reinforces the thrust of subsection (3) by stating that a lessor who is held not entitled to rent under this section has not elected a remedy; the lessor must be awarded damages under Sections 2A-527 and 2A-528 [30-2A-527 and 30-2A-528]. This is a function of two significant policies of this Article—that resort to a remedy is optional, unless expressly agreed to be exclusive (Section 2A-503(2) [30-2A-503(2)]) and that rights and remedies provided in this Article are cumulative. (Section 2A-501(2) and (4) [30-2A-501(2) and (4)]).

30-2A-530. Lessor's incidental damages.

Official Comment

Source: Section 2A-530, U.C.C.

Uniform Statutory Source: Section 2-710[, U.C.C.].

Changes: Revised to reflect leasing practices and terminology.

30-2A-531. Standing to sue third parties for injury to goods.

Official Comment

Source: Section 2A-531, U.C.C.

Uniform Statutory Source: Section 2-722[, U.C.C.].

Changes: Revised to reflect leasing practices and terminology.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

30-2A-532. Lessor's rights to residual interest.

Official Comment

Source: Section 2A-532, U.C.C.

Purposes: This section recognizes the right of the lessor to recover under this Article (as well as under other law) from the lessee for failure to comply with the lease obligations as to the condition of leased goods when returned to the lessor, for failure to return the goods at the end of the lease, or for any other default which causes loss or injury to the lessor's residual interest in the goods.

CHAPTER 3
UNIFORM COMMERCIAL CODE
NEGOTIABLE INSTRUMENTS

Chapter Compiler's Comments

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Section Not Codified: Section 87A-10-101, R.C.M. 1947, an effective date, was not codified in the MCA. This clause has not been repealed and is still valid law. Citation may be made to sec. 10-101, Ch. 264, L. 1963.

Chapter Case Notes

DECISIONS UNDER U.C.C. AFTER 1991 REVISION

Superior Rights as Between Holder of Perfected Security Interest in Collateral and Purchaser of Collateral: Equipment owned by Gauvin and used to secure a promissory note with American Federal Savings and Loan Association (American) was sold to Madison Valley Properties, Inc. (Madison). Upon receipt of the proceeds, Gauvin's girlfriend contacted American for a payoff amount on the promissory note. Gauvin then took a cashier's check from the sale proceeds and converted it to another cashier's check at Valley Bank of Helena (Valley) made out to American for the payoff amount. The check was delivered to American, but later that same day, Valley informed American that the cashier's check had been purchased with stolen funds and was void. American returned the check to Valley, and as a result, the loan was not paid or the lien on the equipment released. American sued Gauvin to recover on the note and sued Madison to recover the equipment. Madison counterclaimed, seeking to quiet title. Summary judgment was granted Madison under the rationale that Madison had superior rights in the collateral equipment. Although American initially received the Valley check in good faith and without notice of the underlying theft, once it was advised of the theft, American could not go forward in good faith and without notice of an adverse claim and Valley's defenses. At the time that it received notice, American still had time and was able to reverse the administrative steps that it had taken to process the loan payment. Notice of the theft could not simply be ignored; therefore, American was required to suspend performance. If it had proceeded in the face of the notice, American could not have claimed holder-in-due-course status. The District Court erred by not first determining whether American was a holder in due course of the cashier's check. Under 30-3-301(1)(a) or (1)(c), American was not a holder in due course because American did not give value. Thus, the Supreme Court reversed the summary judgment award of superior rights in the collateral to Madison. Am. Fed. S&L Ass'n v. Madison Valley Properties, Inc., 1998 MT 93, 288 M 365, 958 P2d 57, 55 St. Rep. 366 (1998).

DECISIONS UNDER U.C.C. PRIOR TO 1991 REVISION

Proof of Validity of Debt — Court Discretion to Post Security: Former 30-3-804 (repealed 1991) authorized but did not compel a court to require security indemnifying an obligor against loss by reason of further claims on a lost, destroyed, or stolen instrument. Therefore, the District Court did not abuse its discretion in refusing to order plaintiff to post security when the note was not endorsed. In this case, proof of ownership and of the terms of the note was supplied in the parties' security agreement, which was attached to the complaint. Plaintiff supplied a photocopy of the original note. Having met the burden of proof as to the validity of the debt, plaintiff was entitled to judgment as a matter of law. Owen v. Ostrum, 259 M 249, 855 P2d 1015, 50 St. Rep. 779 (1993).

Interest in Negotiable Instruments Not Joint Tenancy Interest: To create a joint tenancy interest in a negotiable instrument, there must be an express declaration in the instrument declaring the ownership to be a joint tenancy in order to comply with 70-1-307. In this case, the Supreme Court affirmed a District Court decision, on remand, that the Uniform Commercial Code (Title 30, chapters 1 through 9A) does not provide for joint tenancy interests in negotiable instruments made payable to more than one person and that the use of the term "joint payee" does not create a joint tenancy interest. Stapleton v. First Sec. Bank, 219 M 323, 711 P2d 1364, 42 St. Rep. 2056 (1985), modifying Stapleton v. First Sec. Bank, 207 M 248, 675 P2d 83, 40 St. Rep. 2015 (1983).

Action on Promissory Notes Held in Trust — Real Party in Interest: The plaintiff bank filed an action to collect payment on four promissory notes, and the defendant contended that the bank was not a real party in interest to the case. The Supreme Court found that the District Court's finding that the plaintiff was the holder of legal title to each of the promissory notes and that it was therefore a real party in interest was supported by substantial evidence in both the transcripts and exhibits. First Nat'l Bank & Trust of Wibaux v. Sec. Bank, 199 M 168, 648 P2d 1166, 39 St. Rep. 1270 (1982).

Failure to Timely Pay Draft — Cancellation of Oil and Gas Lease: Failure of lessee to timely pay a draft executed at the same time as an oil and gas lease was sufficient justification for cancellation of the lease. Clawson v. Berklund, 188 M 48, 610 P2d 1168 (1980).

DECISIONS UNDER UNIFORM NEGOTIABLE INSTRUMENTS LAW

Scope of Law:

The Uniform Negotiable Instruments Law deals with negotiable instruments only so long as they are in the hands of holders in due course; if in other hands, they are subject to the same defenses as if nonnegotiable. Merchants' Nat'l Bank of Billings v. Smith, 59 M 280, 196 P 523, 15 ALR 430 (1921).

The provisions of the Negotiable Instruments Law deal with negotiable instruments, and not with instruments nonnegotiable in character. U.S. Nat'l Bank of Red Lodge v. Shupak, 54 M 542, 172 P 324 (1918).

Insofar as the provisions of the Negotiable Instruments Law are clear and unambiguous, they are controlling in the determination of rights of the parties to negotiable paper. Brophy Groc. Co. v. Wilson, 45 M 489, 124 P 510 (1912).

Part 1

Short Title, Form, and Interpretation

30-3-101. Short title.

Official Comment

Source: Section 3-101, U.C.C.

Compiler's Comments

1991 Amendment: At end substituted "Negotiable Instruments" for "Commercial Paper".

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

30-3-102. Definitions.

Official Comment

Source: Section 3-103, U.C.C.

Prior Uniform Statutory Provision: Sections 1(5), 128 and 191, Uniform Negotiable Instruments Law.

Official Comment to 1991 Amendment:

1. Subsection (a) [subsection (1) of this section] defines some common terms used throughout the Article that are not defined by present Article 3 [Title 30, chapter 3, prior to 1991 revision] and adds the definitions of "order" and "promise" found in present Section 3-102(1)(b) and (c) [30-3-102(1)(b) and (1)(c) prior to 1991 revision, now 30-3-102(1)(f) and (1)(i)].

2. The definition of "order" includes an instruction given by the signer to itself. The most common example of this kind of order is a cashier's check which is a draft with respect to which the drawer and drawee are the same bank or branches of the same bank. Present Section 3-118(a) [30-3-118, now repealed] treats a cashier's check as a note. It states "a draft drawn on the drawer is effective as a note." Although it is technically more correct to treat a cashier's check as a promise by the issuing bank to pay rather than an order to pay, a cashier's check is in the form of a check and it is normally referred to as a check. Thus, proposed Article 3 [Title 30, chapter 3] follows banking practice in treating a cashier's check as both a draft and a check rather than a note. Some insurance companies also follow the practice of issuing drafts in which the drawer draws on itself and make [sic] the draft payable at or through a bank. These instruments are treated as drafts.

An order may be addressed to more than one person as drawee either jointly or in the alternative. The authorization of alternative drawees follows present Section 3-102(1)(b) [30-3-102(1)(b) prior to 1991 revision, now 30-3-102(1)(f)] and recognizes the practice of drawers, such as corporations issuing dividend checks, who for commercial convenience name a number of drawees, usually in different parts of the country. Section 3-501(b)(1) [30-3-504(2)(a)] provides that presentment may be made to any one of multiple drawees. Drawees in succession are not permitted because the holder should not be required to make more than one presentment. Dishonor by any drawee named in the draft entitles the holder to rights of recourse against the drawer or indorsers.

3. The last sentence of subsection (a)(9) [subsection (1)(i) of this section] is intended to make it clear that an I.O.U. or other written acknowledgement of indebtedness is not a note unless there is also an undertaking to pay the obligation.

4. Subsection (a)(4) [subsection (1)(d) of this section] introduces a definition of good faith to apply to Article 3 [Title 30, chapter 3]. Present Article 3 [Title 30, chapter 3, prior to 1991 revision] uses the definition in Section 1-201(19) [30-1-201(19)]. The definition in subsection (a)(4) [subsection (1)(d) of this section] is consistent with the definitions of good faith applicable to Articles 2, 2A, 4, and 4A [Title 30, chapters 2, 2A, 4, and 4A].

5. In subsection (c) [subsection (3) of this section] reference is made to a new definition of "bank" in amended Article 4 [Title 30, chapter 4].

Compiler's Comments

2005 Amendment: Chapter 575 in definition of prove substituted "30-1-201(2)(i)" for "30-1-201(8)". Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

1991 Amendment: In (1) inserted definitions of acceptor, drawee, drawer, good faith, maker, ordinary care, party, prove, and remitter; deleted definition of issue that read: ""Issue" means the first delivery of an instrument to a holder or a remitter"; deleted definition of secondary party that read: ""Secondary party" means a drawer or endorser"; deleted definition of instrument that read: ""Instrument" means a negotiable instrument"; substituted definition of order for former definition that read: "An "order" is a direction to pay and must be more than an authorization or request. It must identify the person to pay with reasonable certainty. It may be addressed to one or more such persons jointly or in the alternative but not in succession"; substituted definition of promise for former definition that read: "A "promise" is an undertaking to pay and must be more than an acknowledgement of an obligation"; in (2) inserted references to accommodated party, anomalous indorsement, blank indorsement, cashier's check, certified check, consideration, fiduciary, incomplete instrument, indorsement, indorser, instrument, issue, issuer, negotiable instrument, payable at a definite time, payable on demand, payable to bearer, payable to order, payment, person entitled to enforce, reacquisition, represented person, special indorsement, teller's check, transfer of instrument, traveler's check, and value and deleted ""Certification". 30-3-411", ""Definite time". 30-3-109", ""Dishonor". 30-3-507", ""Notice of dishonor". 30-3-508", ""On demand". 30-3-108", ""Protest". 30-3-509", ""Restrictive endorsement". 30-3-205", and ""Signature". 30-3-401"; in (3) inserted references to bank and suspends payments and deleted ""Account". 30-4-104" and ""Midnight deadline". 30-4-104"; and made minor changes in style.

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

Bank to Exercise Ordinary Care in Settling Checks — Common Law That Bank Exercise Ordinary Care in Processing Checks Preempted by Uniform Commercial Code: Hughes brought common-law claims against a bank for failing to exercise ordinary care in processing checks and for communications that the bank made regarding check processing. A bank that receives a check from a depositor must use ordinary care, as defined in the Uniform Commercial Code (U.C.C.), in settling those checks. However, when a check is processed by automated means, reasonable commercial standards do not require the bank to examine the check, subject to certain exceptions. To the extent that common-law claims relate to processing checks, the specific provisions of the U.C.C. prevail, so Hughes' claims regarding the propriety of the bank's check processing were preempted. However, because the U.C.C. does not address misrepresentation in communications, Hughes' common-law and equitable claims for negligence were not preempted by the U.C.C., and the District Court committed reversible error by failing to consider whether common-law and equitable principles supplement the U.C.C.-defined duty of ordinary care with respect to the bank's representations about the check settlement process. Valley Bank of Ronan v. Hughes, 2006 MT 285, 334 M 335, 147 P3d 185 (2006).

Disqualification of Expert Witness for Lack of Knowledge of Uniform Commercial Code Standard of Ordinary Care: This section defines a bank's duty of ordinary care with respect to the community in which the bank is situated. Defendant's expert witness was well qualified by education, special training, and experience in banking policies and procedures, but had no knowledge of the commercial standards prevailing in the area where plaintiff bank was located, so the District Court did not err in disqualifying the expert for lack of knowledge of the Uniform Commercial Code standard of ordinary care. Valley Bank of Ronan v. Hughes, 2006 MT 285, 334 M 335, 147 P3d 185 (2006), distinguishing Burlingham v. Mintz, 270 M 277, 891 P2d 527 (1995).

Withdrawal Slip Not Considered Check or Order: On appeal from a conviction of issuing a bad check for writing savings withdrawal forms as checks, the Supreme Court found that withdrawal slips negotiated through deception did not meet the definition of check found in 30-3-104 or the definition of order found in this section. Conviction under 45-6-316 was reversed because defendant should properly have been charged with theft. St. v. Taylor, 229 M 138, 745 P2d 337, 44 St. Rep. 1843 (1987).

30-3-104. Negotiable instrument.

Official Comment

Source: Section 3-104, U.C.C.

Prior Uniform Statutory Provision: Sections 1, 5, 10, 126, 184 and 185, Uniform Negotiable Instruments Law.

Official Comment to 1991 Amendment:

1. The definition of "negotiable instrument" defines the scope of Article 3 [Title 30, chapter 3] since Section 3-102 [30-3-124] states: "This Article applies to negotiable instruments." The definition in Section 3-104(a) [30-3-104(1)] incorporates other definitions in Article 3 [Title 30, chapter 3]. An instrument is either a "promise," defined in Section 3-103(a)(9) [30-3-102(1)(i)], or "order," defined in Section 3-103(a)(6) [30-3-102(1)(f)]. A promise is a written undertaking to pay money signed by the person undertaking to pay. An order is a written instruction to pay money signed by the person giving the instruction. Thus, the term "negotiable instrument" is limited to a signed writing that orders or promises payment of money. "Money" is defined in Section 1-201(24) [30-1-201(24)], and it includes foreign money as well as United States dollars. Five other requirements are stated in Section 3-104(a) [30-3-104(1)]: First, the promise or order must be "unconditional." The quoted term is explained in Section 3-106 [30-3-105]. Second, the amount of money must be "a fixed amount . . . with or without interest or other charges described in the promise or order." Section 3-112(b) [30-3-128(2)] relates to "interest." Third, the promise or order must be "payable to bearer or to order." The quoted phrase is explained in Section 3-109 [30-3-111]. An exception to this requirement is stated in subsection (c) [subsection (3) of this section]. Fourth, the promise or order must be payable "on demand or at a definite time." The quoted phrase is explained in Section 3-108 [30-3-108 and 30-3-109]. Fifth, the promise or order may not state "any other undertaking or instruction by the person promising or ordering payment to do any act in addition to the payment of money" with three exceptions. The quoted phrase is based on the first sentence of N.I.L. Section 5 which is the precursor of "no other promise, order, obligation or power given by the maker or drawer" appearing in present Section 3-104(1)(b) [30-3-104(1)(b) prior to 1991 revision]. The words "instruction" and "undertaking" are used instead of "order" and "promise" that are used in the N.I.L. formulation because the latter words are defined terms that include only orders or promises to pay money. The three exceptions stated in proposed Section 3-104(a)(3) [30-3-104(1)(c)] are based on present Section 3-112(1)(b), (c), (d), and (e) [30-3-112, now repealed], as well as N.I.L. Section 5(1), (2), and (3). Subsection (b) [30-3-104(2)] states that "instrument" means "negotiable instrument." This follows present Section 3-102(1)(e) [30-3-102(1)(e) prior to 1991 revision] which treats the two terms as synonymous.

2. Unless subsection (c) [subsection (3) of this section] applies, the effect of subsection (a)(1) [subsection (1)(a) of this section] and Section 3-102 [30-3-124] is to exclude from Article 3 [Title 30, chapter 3] any promise or order that is not payable to bearer or to order. There is no provision in proposed Article 3 [Title 30, chapter 3] that is comparable to present Section 3-805 [30-3-805, now repealed]. The comment to present Section 3-805 [30-3-805, now repealed] states that the typical example of a writing covered by Section 3-805 [30-3-805, now repealed] is a check reading "Pay John Doe." Such a check is governed by present Article 3 [Title 30, chapter 3] but there can not be a holder in due course of the check. Under proposed Section 3-104(c) [30-3-104(3)] such a check is governed by Article 3 [Title 30, chapter 3] and there can be a holder in due course of the check. But subsection (c) [subsection (3) of this section] applies only to checks. The comment to present Section 3-805 [30-3-805, now repealed] does not state any example other than the check to illustrate that section. Subsection (c) [subsection (3) of this section] is based on the belief that it

is good policy to treat checks, that are payment instruments, as negotiable instruments whether or not they contain the words "to the order of'. These words are almost always pre-printed on the check form. Occasionally the drawer of a check may strike out these words before issuing the check. In the past some credit unions used check forms that did not contain the quoted words. Such check forms may still be in use but they are no longer common. Absence of the quoted words can easily be overlooked and should not affect the rights of holders who may pay money or give credit for a check without being aware that it is not in the conventional form.

Total exclusion from Article 3 [Title 30, chapter 3] of other promises or orders that are not payable to bearer or to order serves a useful purpose. It provides a simple device to exclude a writing that does not fit the pattern of typical negotiable instruments and which is not intended to be a negotiable instrument. If a writing could be an instrument despite the absence of "to order" or "to bearer" language, when a dispute arises with respect to the writing, it might be argued that the writing is a negotiable instrument because the other requirements of subsection (a) [subsection (1) of this section] are somehow met. Even if the argument is eventually found to be without merit it can be used as a litigation ploy. Words making a promise or order payable to bearer or to order are the most distinguishing feature of a negotiable instrument and such words are frequently referred to as "words of negotiability." Article 3 [Title 30, chapter 3] is not meant to apply to contracts for the sale of goods or services or the sale or lease of real property or similar writings that may contain a promise to pay money. The use of words of negotiability in such contracts would be an aberration. Absence of the words precludes any argument that such contracts might be negotiable instruments.

An order or promise which is excluded from Article 3 [Title 30, chapter 3] because of the requirements of Section 3-104(a) [30-3-104(1)] may nevertheless be similar to a negotiable instrument in many respects. Although such a writing cannot be made a negotiable instrument within Article 3 [Title 30, chapter 3] by contract or conduct of its parties, nothing in Section 3-104 [30-3-104] or in Section 3-102 [30-3-124] is intended to mean that in a particular case involving such a writing a court could not arrive at a result similar to the result that would follow if the writing were a negotiable instrument. For example, a court might find that the obligor with respect to a promise that does not fall within Section 3-104(a) [30-3-104(1)] is precluded from asserting a defense against a bona fide purchaser. The preclusion could be based on estoppel or ordinary principles of contract. It does not depend upon the law of negotiable instruments. An example is stated in the paragraph following Case #2 in Comment 4 to Section 3-302 [30-3-302].

Moreover, consistent with the principle stated in Section 1-102(2)(b) [30-1-102(2)(b)], the immediate parties to an order or promise that is not an instrument may provide by agreement that one or more of the provisions of Article 3 [Title 30, chapter 3] determine their rights and obligations under the writing. Upholding the parties' choice is not inconsistent with Article 3 [Title 30, chapter 3]. Such an agreement may bind a transferee of the writing if the transferee has notice of it or the agreement arises from usage of trade and the agreement does not violate other law or public policy. An example of such an agreement is a provision that a transferee of the writing has the rights of a holder in due course stated in Article 3 [Title 30, chapter 3] if the transferee took rights under the writing in good faith, for value, and without notice of a claim or defense.

Even without an agreement of the parties to an order or promise that is not an instrument, it may be appropriate, consistent with the principles stated in Section 1-102(2) [30-1-102(2)], for a court to apply one or more provisions of Article 3 [Title 30, chapter 3] to the writing by analogy, taking into account the expectations of the parties and the differences between the writing and an instrument governed by Article 3 [Title 30, chapter 3]. Whether such application is appropriate depends upon the facts of each case.

3. There is no concept of a "nonnegotiable instrument" in proposed Article 3 [Title 30, chapter 3]. That term is not used because the term is ambiguous and in practice is used with quite different meanings. The term is often used to refer to an order or promise with respect to which there cannot be a holder in due course but which is transferable by indorsement. For example, that term can refer to an order or promise that would be an instrument except for the fact that "to order or to bearer" is not used. Under present Article 3 [Title 30, chapter 3, prior to 1991 revision] the order or promise is an instrument covered by Article 3 [Title 30, chapter 3] but there can't be a holder in due course. Present Section 3-805 [30-3-805, now repealed]. That term has also been used to refer to promissory notes with a variable interest rate. Such a note is not covered by present Article 3 [Title 30, chapter 3, prior to 1991 revision] at all. Another meaning of "nonnegotiable instrument" refers to an order or promise to pay money that is transferable by indorsement and delivery and which is enforced by the special rules of Article 3 [Title 30, chapter

3] whether or not the holder-in-due-course doctrine applies. This describes many notes under present law which meet the requirements of Article 3 [Title 30, chapter 3], but with respect to which case law or statute abolishes the holder-in-due-course doctrine to protect a particular class of issuers of instruments such as notes given in consumer transactions. Sometimes the word "nonnegotiable" stamped across what appears to be a check or note is meant to indicate that the writing is only a copy of an instrument or is only a specimen that is not meant to represent any legal rights. Proposed Article 3 [Title 30, chapter 3] thus avoids this ambiguous term altogether and does not take any position with respect to the effect of a statement in an instrument that it is nonnegotiable.

4. Subsection (d) [subsection (4) of this section] provides a device that can be used to exclude from Article 3 [Title 30, chapter 3] a writing that would otherwise be an instrument under subsection (a) [subsection (1) of this section]. The effect under subsection (d) [subsection (4) of this section] is not only to negate the possibility of a holder in due course, but to prevent the writing from being a negotiable instrument for any purpose. Subsection (d) [subsection (4) of this section] does not, however, apply to a check.

5. Instruments are divided into two general categories: drafts and notes. A draft is an instrument that is an order. A note is an instrument that is a promise. Section 3-104(e) [30-3-104(5)]. Subsections (f) through (j) [subsections (6) through (10) of this section] define particular instruments that fall within the categories of draft and note. The term "draft," defined in subsection (e) [subsection (5) of this section], includes a "check" which is defined in subsection (f) [subsection (6) of this section]. "Check" includes a share draft drawn on a credit union payable through a bank because the definition of bank (Section 4-104 [30-4-104]) includes credit unions. However, a draft drawn on an insurance company payable through a bank is not a check because it is not drawn on a bank. The definition of "check" in Article 3 [Title 30, chapter 3] is different from the definition of "check" in Regulation CC Section 229.2. "Teller's check" is separately defined in subsection (h) [subsection (8) of this section]. A teller's check is always drawn by a bank and is usually drawn on another bank. In some cases a teller's check is drawn on a nonbank but is made payable at or through a bank. Article 3 [Title 30, chapter 3] treats both types of teller's check identically, and both are included in the definition of "check." A cashier's check, defined in subsection (g) [subsection (7) of this section], is also included in the definition of "check." The term "bill of exchange" is not used in proposed Article 3 [Title 30, chapter 3]. It is generally understood to be a synonym for the term "draft." Certificates of deposit are treated in present Article 3 [Title 30, chapter 3, prior to 1991 revision] as a separate type of instrument. Proposed Section 3-104(j) [30-3-104(10)] treats them as notes.

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "Form of negotiable instruments — "draft" — "check" — "certificate of deposit" — "note". (1) Any writing to be a negotiable instrument within this chapter must:

(a) be signed by the maker or drawer; and

(b) contain an unconditional promise or order to pay a sum certain in money and no other promise, order, obligation or power given by the maker or drawer except as authorized by this chapter; and

(c) be payable on demand or at a definite time; and

(d) be payable to order or to bearer.

(2) A writing which complies with the requirements of this section is:

(a) a "draft" ("bill of exchange") if it is an order;

(b) a "check" if it is a draft drawn on a bank and payable on demand;

(c) a "certificate of deposit" if it is an acknowledgment by a bank of receipt of money with an engagement to repay it;

(d) a "note" if it is a promise other than a certificate of deposit.

(3) As used in other chapters of this code, and as the context may require, the terms "draft", "check", "certificate of deposit" and "note" may refer to instruments which are not negotiable within this chapter as well as to instruments which are so negotiable."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

DECISIONS UNDER U.C.C. AFTER 1991 REVISION

Summary Judgment Improper — Genuine Issue of Material Fact Surrounding Payment: The District Court's grant of summary judgment, which was based in part on the plaintiff's failure to timely remit payment to the defendant insurance company, was erroneous when the District

Court excluded admissible party-opponent statements regarding the nature of the plaintiff's payment. In addition, the District Court erred in granting summary judgment on the alternate ground that the plaintiff's money order was an invalid method of payment. Although the money order was not signed by the plaintiff, summary judgment was not appropriate because a genuine issue of material fact existed regarding whether the money order would have been honored had it been presented to the bank. Smith v. Farmers Union Mut. Ins. Co., 2011 MT 216, 361 Mont. 516, 260 P.3d 163.

Elements of Issuing Bad Checks Supportive of Information: The County Attorney filed an information against McWilliams for issuing bad checks in connection with a construction business. McWilliams asserted that the information should be dismissed because the series of transactions involving the checks were an illegal series of deferred deposit loans, so McWilliams could not be criminally prosecuted. However, 31-1-723, which prohibits deferred deposit loans, applies only to licensees under Title 31, ch. 1, part 7. None of the parties involved were licensees, so the statute did not apply. McWilliams also contended that the checks did not meet the definition of negotiable instruments in 30-3-104 because they were not payable on demand, but rather were in the nature of a future promise. However, the checks contained no restrictive endorsement, and although the parties to whom the checks were written agreed to refrain from cashing them immediately, the checks were in fact payable on demand and met the statutory definition. McWilliams also cited 45-2-211 in arguing a consent defense because the parties consented to take the checks and hold them, but that argument also failed because even though the parties agreed to hold the checks, they did not consent to nonpayment or to having McWilliams stop payment altogether. McWilliams next asserted that under St. v. Patterson, 75 M 315, 243 P 355 (1926), the information was defective because it contained no assertion of an intent to defraud. The statutory language under which Patterson was charged in 1926 required a showing of intent to defraud, but the current statute, 45-6-316, contains no intent to defraud element, so the information was not defective in that regard. There was sufficient evidence to charge McWilliams with issuing bad checks, and the District Court did not err in denying McWilliams' pretrial motion to dismiss the information. St. v. McWilliams, 2008 MT 59, 341 M 517, 178 P3d 121 (2008).

DECISIONS UNDER U.C.C. PRIOR TO 1991 REVISION

Withdrawal Slip Not Considered Check or Order: On appeal from a conviction of issuing a bad check for writing savings withdrawal forms as checks, the Supreme Court found that withdrawal slips negotiated through deception did not meet the definition of check found in this section or the definition of order found in 30-3-102. Conviction under 45-6-316 was reversed because defendant should properly have been charged with theft. St. v. Taylor, 229 M 138, 745 P2d 337, 44 St. Rep. 1843 (1987).

Partial Enforcement of Promissory Note: Respondent signed a promissory note to her former husband in the amount of $2,000. She did not make any payments on the note. At trial, she testified that the only consideration she had received for the note was $1,000 and the use of a pickup. Thus, the lower court's decision to enforce the note only partially was not clearly erroneous. In re Marriage of Jones, 218 M 441, 709 P2d 158, 42 St. Rep. 1722 (1985).

Statutory Elements Required: At the time Croft and Starhaven Ranch, Ltd., entered a ranch purchase agreement, David Erickson signed an itemized list of personal property setting an evaluation of the items listed on behalf of Starhaven. Croft assigned his interest in the list to defendant. After default, defendant brought a foreclosure action and contended the list was a promissory note. The list contained no promise to pay, no date for payment, and was not made payable to order or bearer. The document was not a promissory note and could not support a judgment against either Erickson or Starhaven. On rehearing, the court rejected the bank's contention that, even if not a promissory note, the list is an enforceable contract. Erickson v. First Nat'l Bank, 215 M 350, 697 P2d 1332, 42 St. Rep. 423 (1985).

DECISIONS UNDER UNIFORM NEGOTIABLE INSTRUMENTS LAW

Determination of Negotiability — Check Torn and Repaired: Tearing of check and its repair did not constitute a "spoliation" which would render it nonnegotiable, and the fact that it was so torn before being cashed by defendant afforded no ground for relieving him from liability for grand larceny and subsequently for forgery in endorsing it. St. v. Romero, 146 M 77, 404 P2d 500 (1965).

Determinable Time for Payment: A chattel mortgage, which provided that balance should become due without notice if customer defaulted on any obligation under the mortgage or if the holder should consider the indebtedness or the car insecure, was not a negotiable instrument as it was not payable at a determinable future time. Sonnek v. Universal C. I. T. Credit Corp., 140 M 503, 374 P2d 105 (1962).

Proof of Negotiability: Where in an action on a trade acceptance the instrument contained all the elements necessary under section 55-201, R.C.M. 1947 (now repealed), to constitute it a negotiable one and was introduced in evidence, it spoke for itself and proof of its negotiability was unnecessary. Best v. Boyer, 98 M 40, 37 P2d 331 (1934).

Effect of Clause Providing Interest After Due Date: Inclusion in a promissory note of the clause "Interest or principal not paid when due, to draw interest thereafter at ten per cent per annum until paid", did not destroy its negotiability. Lister v. Donlan, 85 M 571, 281 P 348, 72 ALR 1 (1929).

Cashiers Check — No Trust Relationship: A cashier's check is a draft or bill of exchange drawn by a bank upon itself or some other bank in which funds of the former are deposited; it represents credit which the purchaser of such a check buys. The money paid the issuing bank becomes the bank's money, the transaction being one of purchase and sale, and no trust relationship is thereby established. Mont.-Wyo. Ass'n of Credit Men v. Commercial Nat'l Bank, 80 M 174, 259 P 1060 (1927).

Federal, State, or Municipal Corporation Bonds: Coupon liberty bonds are negotiable instruments within the Uniform Negotiable Instruments Act, but registered bonds are not. Grosfield v. First Nat'l Bank of Miles City, 73 M 219, 236 P 250 (1925).

Provision for Costs in Note — "Attorney's Fee" and "Costs of Collection" Interchangeable: A promissory note containing a provision for the payment of an attorney's fee and costs of collection, instead of the statutory phrase "with costs of collection or an attorney's fee", was not thereby rendered nonnegotiable. The words "attorney's fee" and "costs of collection" in this connection mean the same thing, so that the use of both of them in the conjunctive imposed no greater burden upon the maker than their use in the disjunctive would have done. Wood v. Ferguson, 71 M 540, 230 P 592 (1924).

Time of Payment Uncertain: A 6-months' promissory note containing an accelerating clause to the effect that "in the event of insolvency of either maker or endorsers, the institution of suit or attachment against them or either of them, or the mortgaging of any property by the makers or endorsers", the note might be declared immediately due and payable was nonnegotiable in that it left the time when payable uncertain and indefinite. Great Falls Nat'l Bank v. Young, 67 M 328, 215 P 651 (1923).

Payment in Money: A promissory note legally imports a promise to pay in money and nothing else. First St. Bank of Hilger v. Lang, 55 M 146, 174 P 597, 9 ALR 1139 (1918).

Requirements for Negotiability: To constitute an instrument a negotiable one, it must, under section 55-1701, R.C.M. 1947 (now repealed), be in writing, signed by the maker, contain an unconditional promise to pay a certain sum in money, and be payable on demand or at a fixed or determinable future time, to order or bearer. First Nat'l Bank of Miles City v. Barrett, 52 M 359, 157 P 951 (1916).

Description of Nonnegotiable Note as Negotiable: A provision in a note that it is negotiable at a particular bank is not a waiver of the effect of a stipulation for payment of attorney's fees in case of suit, which, under other statutory provisions, renders the note nonnegotiable. Stadler v. First Nat'l Bank, 22 M 190, 56 P 111 (1898), explained in Bullard v. Smith, 28 M 387, 72 P 761 (1903) and Cornish v. Woolverton, 32 M 456, 81 P 4 (1905).

Attorney General's Opinions

Delinquency Charges on Overdue Payments: The Department of Agriculture can assess delinquency charges on overdue monthly installment payments as provided in notes evidencing loans taken by that Department. 37 A.G. Op. 50 (1977).

30-3-105. Unconditional promise or order.

Official Comment

Source: Section 3-106, U.C.C.

Prior Uniform Statutory Provision: Section 3, Uniform Negotiable Instruments Law.

Official Comment to 1991 Amendment:

1. This provision replaces present Section 3-105 [30-3-105]. Its purpose is to define when a promise or order fulfills the requirement in Section 3-104(a) [30-3-104(1)] that it be an "unconditional" promise or order to pay. Under Section 3-106(a) [30-3-106, now repealed] a promise or order is deemed to be unconditional unless one of the two tests of the subsection make the promise or order conditional. If the promise or order states an express condition to payment, the promise or order is not an instrument. For example, a promise states, "I promise

to pay $100,000 to the order of John Doe if he conveys title to Blackacre to me." The promise is not an instrument because there is an express condition to payment. However, suppose a promise states, "In consideration of John Doe's promise to convey title to Blackacre I promise to pay $100,000 to the order of John Doe." That promise can be an instrument if Section 3-104 [30-3-104] is otherwise satisfied. Although the recital of the executory promise of Doe to convey Blackacre might be read as an implied condition that the promise be performed, the condition is not an express condition as required by Section 3-106(a)(i) [30-3-106, now repealed]. This result is consistent with present Section 3-105(1)(a) and (b) [30-3-105(1)(a) and (1)(b) prior to 1991 revision]. Present Section 3-105(1)(b) [30-3-105(1)(b) prior to 1991 revision] is not repeated in Section 3-106 [30-3-105] because it is not necessary. It is an example of an implied condition. The first clause of present Section 3-105(1)(c) [30-3-105(1)(c) prior to 1991 revision] and present Section 3-105(1)(d), (e), and (f) [30-3-105(1)(d) through (1)(f) prior to 1991 revision] are other examples of implied conditions. They are not repeated in Section 3-106 [30-3-105] because they are not necessary. The law is not changed.

Section 3-106(a)(ii) [30-3-105(1)(a)(ii)] is a restatement of present Section 3-105(2)(a) [30-3-105(2)(a) prior to 1991 revision]. The only change is the use of "writing" instead of "agreement" and a broadening of the language that can result in conditionality. For example, a promissory note is not an instrument defined by Section 3-104 [30-3-104] if it contains any of the following statements: 1. "This note is subject to a contract of sale dated April 1, 1990 between the payee and maker of this note." 2. "This note is subject to a loan and security agreement dated April 1, 1990 between the payee and maker of this note." 3. ["]Rights and obligations of the parties with respect to this note are stated in an agreement dated April 1, 1990 between the payee and maker of this note." It is not relevant whether any condition to payment is or is not stated in the writing to which reference is made. The rationale is that the holder of a negotiable instrument should not be required to examine another document to determine rights with respect to payment. But subsection (b)(i) [subsection (2)(a) of this section] permits reference to a separate writing for information with respect to collateral, prepayment, or acceleration.

Many notes issued in commercial transactions are secured by collateral, are subject to acceleration in the event of default, or are subject to prepayment. A statement of rights and obligations concerning collateral, prepayment, or acceleration does not prevent the note from being an instrument if the statement is in the note itself. See Section 3-104(a)(3) [30-3-104(1)(c)] and Section 3-108(b) [30-3-109(1)]. In some cases it may be convenient not to include a statement concerning collateral, prepayment, or acceleration in the note, but rather to refer to an accompanying loan agreement, security agreement or mortgage for that statement. Subsection (b)(i) [subsection (2)(a) of this section] allows a reference to the appropriate writing for a statement of these rights. For example, a note would not be made conditional by the following statement: "This note is secured by a security interest in collateral described in a security agreement dated April 1, 1990 between the payee and maker of this note. Rights and obligations with respect to the collateral are [stated in] [governed by] the security agreement." The bracketed words are alternatives, either of which complies.

Subsection (b)(ii) [subsection (2)(b) of this section] addresses the issues covered by present Section 3-105(1)(f), (g), and (h) [30-3-105(1)(f) through (1)(h) prior to 1991 revision] and Section 3-105(2)(b) [30-3-105(2)(b)]. Under Section 3-106(a) [30-3-105(1)] a promise or order is not made conditional because payment is limited to payment from a particular source or fund. This reverses the result of present Section 3-105(2)(b) [30-3-105(2)(b)]. There is no cogent reason why the general credit of a legal entity must be pledged to have a negotiable instrument. Market forces determine the marketability of instruments of this kind. If potential buyers don't want promises or orders that are payable only from a particular source or fund, they won't take them, but Article 3 [Title 30, chapter 3] should apply.

2. Subsection (c) [subsection (3) of this section] applies to traveler's checks or other instruments that may require a countersignature. Although the requirement of a countersignature is a condition to payment, traveler's checks are treated in the commercial world as money substitutes and therefore should be governed by Article 3 [Title 30, chapter 3]. The first sentence of subsection (c) [subsection (3) of this section] allows a traveler's check to meet the definition of instrument by stating that the countersignature condition does not make it conditional for the purposes of Section 3-104 [30-3-104]. The second sentence states the effect of a failure to meet the condition. Suppose a thief steals a traveler's check and cashes it by skillfully imitating the specimen signature so that the countersignature appears to be authentic. The countersignature is for the purpose of identification. It is not treated as an indorsement. Subsection (c) [subsection (3) of this section] provides that the failure of the owner to countersign does not prevent a

transferee from becoming a holder. Thus, the merchant or bank that cashed the traveler's check becomes a holder when the traveler's check is taken. The forged countersignature is a defense to the obligation of the issuer to pay the instrument, and is included in defenses under Section 3-305(a)(2) [30-3-305(1)(b)]. These defenses may not be asserted against a holder in due course. Whether a holder has notice of the defense is a factual question. If the countersignature is a very bad forgery, there may be notice. But if the merchant or bank cashed a traveler's check for a skilled forger there might not be notice that the countersignature was forged. Thus, the merchant or bank could be a holder in due course.

3. Subsection (d) [subsection (4) of this section] concerns the effect of a statement to the effect that the rights of a holder or transferee are subject to claims and defenses that the issuer could assert against the original payee. The subsection applies only if the statement is required by statutory or administrative law. The prime example is the Federal Trade Commission Rule (16 C.F.R. Part 433) preserving consumers' claims and defenses in consumer credit sales. The intent of the FTC rule is to make it impossible for there to be a holder in due course of a note bearing the FTC legend and undoubtedly that is the result. But the legend may also have the unintended effect of making the note conditional, thus excluding the note from present Article 3 [Title 30, chapter 3, prior to 1991 revision] altogether. Subsection (d) [subsection (4) of this section] is designed to make it possible to preclude the possibility of a holder in due course without excluding the instrument from Article 3 [Title 30, chapter 3]. Most of the provisions of Article 3 [Title 30, chapter 3] are not affected by the holder-in-due-course doctrine and there is no reason why Article 3 [Title 30, chapter 3] should not apply to a note bearing the FTC legend if holder-in-due-course rights are not involved. Under subsection (d) [subsection (4) of this section] the statement does not make the note conditional. If the note otherwise meets the requirements of Section 3-104(a) [30-3-104(1)] it is a negotiable instrument under Article 3 [Title 30, chapter 3] for all purposes except that there cannot be a holder in due course of the note. No particular form of legend or statement is required by subsection (d) [subsection (4) of this section] so long as the statement conveys the substance of what is stated in the statute, that "the rights of a holder or transferee are subject to claims or defenses that the issuer could assert against the original payee." For example, the FTC legend required in a note taken by the seller in a consumer sale of goods or services is tailored to that particular transaction and therefore uses language that is somewhat different from that stated in subsection (d) [subsection (4) of this section], but the difference in expression does not affect the essential similarity of the message conveyed. The effect of the FTC legend is to make the rights of a holder or transferee subject to claims or defenses that the issuer could assert against the original payee of the note.

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "When promise or order unconditional. (1) A promise or order otherwise unconditional is not made conditional by the fact that the instrument:

(a) is subject to implied or constructive conditions; or

(b) states its consideration, whether performed or promised, or the transaction which gave rise to the instrument, or that the promise or order is made or the instrument matures in accordance with or "as per" such transaction; or

(c) refers to or states that it arises out of a separate agreement or refers to a separate agreement for rights as to prepayment or acceleration; or

(d) states that it is drawn under a letter of credit; or

(e) states that it is secured, whether by mortgage, reservation of title or otherwise; or

(f) indicates a particular account to be debited or any other fund or source from which reimbursement is expected; or

(g) is limited to payment out of a particular fund or the proceeds of a particular source, if the instrument is issued by a government or governmental agency or unit; or

(h) is limited to payment out of the entire assets of a partnership, unincorporated association, trust or estate by or on behalf of which the instrument is issued.

(2) A promise or order is not unconditional if the instrument:

(a) states that it is subject to or governed by any other agreement; or

(b) states that it is to be paid only out of a particular fund or source except as provided in this section."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

DECISIONS UNDER UNIFORM NEGOTIABLE INSTRUMENTS LAW

Contract Made Part of Instrument: An order for goods embodying a promissory note in such form that if the note is detached there is no longer an order is not within section 55-203, R.C.M. 1947 (now repealed). St. v. Mitton, 37 M 366, 96 P 926, 127 Am. St. Rep. 732 (1908).

30-3-107. Instrument payable in foreign money.

Official Comment

Source: Section 3-107, U.C.C.

Prior Uniform Statutory Provision: Section 6(5), Uniform Negotiable Instruments Law.

Official Comment to 1991 Amendment:

The definition of instrument in proposed Section 3-104 [30-3-104] requires that the promise or order be payable in "money." That term is defined in Section 1-201(24) [30-1-201(24)] as "a medium of exchange authorized by a domestic or foreign government as part of its currency." Proposed Section 3-107 [30-3-107] states than an instrument payable in foreign money may be paid in dollars if the instrument does not prohibit it. The reference in present Section 3-107(1) [30-3-107(1) prior to 1991 revision] to instruments payable in "currency" or "current funds" has been dropped as superfluous.

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "Money. (1) An instrument is payable in money if the medium of exchange in which it is payable is money at the time the instrument is made. An instrument payable in "currency" or "current funds" is payable in money.

(2) A promise or order to pay a sum stated in a foreign currency is for a sum certain in money and, unless a different medium of payment is specified in the instrument, may be satisfied by payment of that number of dollars which the stated foreign currency will purchase at the buying sight rate for that currency on the day on which the instrument is payable or, if payable on demand, on the day of demand. If such an instrument specifies a foreign currency as the medium of payment the instrument is payable in that currency."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

30-3-108. Payable on demand.

Official Comment

Source: Section 3-108, U.C.C.

Prior Uniform Statutory Provision: Section 7, Uniform Negotiable Instruments Law.

Official Comment: See official comment to 30-3-109.

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "Instruments payable on demand include those payable at sight or on presentation and those in which no time for payment is stated."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

DECISIONS UNDER U.C.C. PRIOR TO 1991 REVISION

Time of Repayment Specified in Note — Not Considered Demand Note: As a general rule, notes payable on demand are due and payable immediately upon execution, and no further demand is necessary to mature them. However, an exception applies when the terms of the instrument disclose an intention by the parties that the note is not due and payable immediately after delivery. In that case, an actual demand is necessary to mature the note. Therefore, language in a note stating that "[i] no demand is made, Borrower shall pay 120 days after the date of this note" took the note out of the category of a demand note, and an actual demand was necessary to mature the note prior to the date set. Bottrell v. Am. Bank, 237 M 1, 773 P2d 694, 46 St. Rep. 561 (1989).

DECISIONS UNDER UNIFORM NEGOTIABLE INSTRUMENTS LAW

Formal Demand: Demand upon maker of a note for payment before an action is instituted is unnecessary. Barrett v. Morton, 137 M 190, 351 P2d 601 (1960).

30-3-109. Definite time.

Official Comment

Source: Section 3-108, U.C.C.

Prior Uniform Statutory Provision: Sections 4 and 17(3), Uniform Negotiable Instruments Law.

Official Comment to 1991 Amendment:

This section [in part] is a restatement of present Section 3-108 [30-3-108 prior to 1991 revision] and Section 3-109 [30-3-109 prior to 1991 revision]. Subsection (b) [subsection (1) of this section] broadens present Section 3-109 [30-3-109 prior to 1991 revision] somewhat by providing that a definite time includes a time readily ascertainable at the time the promise or order is issued. Subsection (b)(iii) and (iv) [subsections (1)(c) and (1)(d) of this section] restates present Section 3-109(1)(d) [30-3-109(1)(d) prior to 1991 revision]. It adopts the generally accepted rule that a clause providing for extension at the option of the holder, even without a time limit, does not affect negotiability since the holder is given only a right which the holder would have without the clause. If the extension is to be at the option of the maker or acceptor or is to be automatic, a definite time limit must be stated or the time of payment remains uncertain and the order or promise is not a negotiable instrument. If a definite time limit is stated, the effect upon certainty of time of payment is the same as if the instrument were made payable at the ultimate date with a term providing for acceleration.

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "(1) An instrument is payable at a definite time if by its terms it is payable:

(a) on or before a stated date or at a fixed period after a stated date; or

(b) at a fixed period after sight; or

(c) at a definite time subject to any acceleration; or

(d) at a definite time subject to extension at the option of the holder, or to extension to a further definite time at the option of the maker or acceptor or automatically upon or after a specified act or event.

(2) An instrument which by its terms is otherwise payable only upon an act or event uncertain as to time of occurrence is not payable at a definite time even though the act or event has occurred."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

DECISIONS UNDER U.C.C. PRIOR TO 1991 REVISION

Time of Repayment Specified in Note — Not Considered Demand Note: As a general rule, notes payable on demand are due and payable immediately upon execution, and no further demand is necessary to mature them. However, an exception applies when the terms of the instrument disclose an intention by the parties that the note is not due and payable immediately after delivery. In that case, an actual demand is necessary to mature the note. Therefore, language in a note stating that "[i] no demand is made, Borrower shall pay 120 days after the date of this note" took the note out of the category of a demand note, and an actual demand was necessary to mature the note prior to the date set. Bottrell v. Am. Bank, 237 M 1, 773 P2d 694, 46 St. Rep. 561 (1989).

Supply of Presentment Date by Holder: The holder of a 160-day sight draft may supply a date of presentment when the drawee fails to provide his written acceptance or date thereof. Thus, the holder of the draft could in good faith treat the date on which the collecting bank acknowledged receipt of the draft as the date of acceptance and could properly treat the draft as dishonored when payment was received 162 days after the date the draft was received from the bank. Clawson v. Berklund, 188 M 48, 610 P2d 1168 (1980).

DECISIONS UNDER UNIFORM NEGOTIABLE INSTRUMENTS LAW

Contingency Maturity: A chattel mortgage that provided that the balance should become due without notice if the customer defaulted on any obligation under the mortgage or if the holder should consider the indebtedness or the car insecure was not a negotiable instrument within the meaning of section 55-204, R.C.M. 1947 (now repealed). Sonnek v. Univ. C. I. T. Credit Corp., 140 M 503, 374 P2d 105 (1962).

Note Due on Insolvency: A provision that the holder may declare a note due immediately on the insolvency of the maker renders it nonnegotiable. Erlandson v. Erskine, 76 M 537, 248 P 209 (1926). See also Anderson v. Border, 87 M 4, 285 P 174 (1930).

Acceleration Clause: A 6-months' promissory note containing an accelerating clause to the effect that in the event of insolvency of either maker or endorsers or the institution of suit or attachment against them or either of them, or the mortgaging of any property by the makers or endorsers, the note might be declared immediately due and payable, was nonnegotiable in that it left the time when payable uncertain and indefinite. Great Falls Nat'l Bank v. Young, 67 M 328, 215 P 651 (1923).

30-3-111. Payable to bearer or to order.

Official Comment

Source: Section 3-109, U.C.C.

Prior Uniform Statutory Provision: Section 9, Uniform Negotiable Instruments Law.

Official Comment to 1991 Amendment:

1. Under Section 3-104(a) [30-3-104(1)], a promise or order cannot be an instrument unless the instrument is payable to bearer or to order when it is issued or unless Section 3-104(c) [30-3-104(3)] applies. The terms "payable to bearer" and "payable to order" are defined in Section 3-109 [30-3-111]. The quoted terms are also relevant in determining how an instrument is negotiated. If the instrument is payable to bearer it can be negotiated by delivery alone. Section 3-201(b) [30-3-202(2)]. An instrument that is payable to an identified person cannot be negotiated without the indorsement of the identified person. Section 3-201(b) [30-3-202(2)]. An instrument payable to order is payable to an identified person. Section 3-109(b) [30-3-111(2)]. Thus, an instrument payable to order requires the indorsement of the person to whose order the instrument is payable.

2. Subsection (a) [subsection (1) of this section] states when an instrument is payable to bearer. An instrument is payable to bearer if it states that it is payable to bearer, but some instruments use ambiguous terms. For example, check forms usually have the words "to the order of" printed at the beginning of the line to be filled in for the name of the payee. If the drawer writes in the word "bearer" or "cash," the check reads "to the order of bearer" or "to the order of cash." In each case the check is payable to bearer. Sometimes the drawer will write the name of the payee "John Doe" but will add the words "or bearer." In that case the check is payable to bearer. Subsection (a) [subsection (1) of this section]. Under subsection (b) [subsection (2) of this section], if an instrument is payable to bearer it can't be payable to order. This is different from present Section 3-110(3) [30-3-110, now repealed]. An instrument that purports to be payable both to order and bearer states contradictory terms. A transferee of the instrument should be able to rely on the bearer term and acquire rights as a holder without obtaining the indorsement of the identified payee. An instrument is also payable to bearer if it does not state a payee. Instruments that do not state a payee are in most cases incomplete instruments. In some cases the drawer of a check may deliver or mail it to the person to be paid without filling in the line for the name of the payee. Under subsection (a) [subsection (1) of this section] the check is payable to bearer when it is sent or delivered. It is also an incomplete instrument. This case is discussed in Comment 2 to Section 3-115 [30-3-115]. Subsection (a) [subsection (1) of this section] contains the words "otherwise indicates that it is not payable to an identified person." The quoted words are meant to cover uncommon cases in which an instrument indicates that it is not meant to be payable to a specific person. Such an instrument is treated like a check payable to "cash." The quoted words are not meant to apply to an instrument stating that it is payable to an identified person such as "ABC Corporation" if ABC Corporation is a nonexistent company. Although the holder of the check cannot be the nonexistent company, the instrument is not payable to bearer. Negotiation of such an instrument is governed by Section 3-404(b) [30-3-405(2)].

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "Payable to bearer. An instrument is payable to bearer when by its terms it is payable to:

(a) bearer or the order of bearer; or
(b) a specified person or bearer; or
(c) "cash" or the order of "cash", or any other indication which does not purport to designate a specific payee."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

30-3-114. Date of instrument.

Official Comment

Source: Section 3-113, U.C.C.

Prior Uniform Statutory Provision: Sections 6(1), 11, 12 and 17(3), Uniform Negotiable Instruments Law.

Official Comment to 1991 Amendment:

This section replaces present Section 3-114 [30-3-114 prior to 1991 revision]. Subsections (1) and (3) of present Section 3-114 [30-3-114(1) and (3) prior to 1991 revision] are deleted as unnecessary. Proposed Section 3-113(a) [30-3-114(1)] is based on subsection (2) of present Section 3-114 [30-3-114(2) prior to 1991 revision], except for the reference to Section 4-401 [30-4-401] which prescribes the procedure for notifying the payor bank of a postdated check. With respect to an undated instrument, the date is the date of issue.

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "Date, antedating, postdating. (1) The negotiability of an instrument is not affected by the fact that it is undated, antedated or postdated.

(2) Where an instrument is antedated or postdated the time when it is payable is determined by the stated date if the instrument is payable on demand or at a fixed period after date.

(3) Where the instrument or any signature thereon is dated, the date is presumed to be correct."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

DECISIONS UNDER UNIFORM NEGOTIABLE INSTRUMENTS LAW

Erroneous Date: Evidence is admissible that the maker of an instrument inadvertently wrote the date "1904" instead of "1905" because at the beginning of the new year he had not yet become accustomed to writing the new date. McDonald v. Klenze, 52 M 142, 157 P 175 (1916).

30-3-115. Incomplete instrument.

Official Comment

Source: Section 3-115, U.C.C.

Prior Uniform Statutory Provision: Sections 13, 14 and 15, Uniform Negotiable Instruments Law.

Official Comment to 1991 Amendment:

1. This section generally carries forward the rules set out in present Section 3-115 [30-3-115 prior to 1991 revision]. The term "incomplete instrument" applies both to an "instrument," i.e. a writing meeting all the requirements of proposed Section 3-104 [30-3-104], and to a writing intended to be an instrument that is signed but lacks some element of an instrument. The test in both cases is whether the contents show that it is incomplete and that the signer intended that additional words or numbers be added.

2. If an incomplete instrument meets the requirements of Section 3-104 [30-3-104] and is not completed it may be enforced in accordance with its terms. Suppose a note delivered to the payee is incomplete solely because a space on the pre-printed note form for the due date is not filled in.

Case #1. If the incomplete instrument is never completed, the note is payable on demand. Section 3-108(a) [30-3-108(1)]. However, if the payee and the maker agreed to a due date, the maker may have a defense under Section 3-117 [30-3-119].

Case #2. If the payee completes the note by stating a due date, the note is payable on the due date stated. However, if the due date filled in was not the date agreed to by the parties there is an alteration of the note. Section 3-407 [30-3-407] governs the case.

Suppose Debtor pays Creditor by giving Creditor a check on which the space for the name of the payee is left blank. The check is an instrument but it is incomplete. The check is enforceable in its incomplete form and it is payable to bearer because it does not state a payee. Section 3-109(a)(2) [30-3-311(1)(b)]. Thus, Creditor is a holder of the check. Normally in this kind of case Creditor would simply fill in the space with Creditor's name. When that occurs the check becomes payable to the Creditor.

3. In some cases the incomplete instrument does not meet the requirements of Section 3-104 [30-3-104]. An example is a check with the amount not filled in. The check cannot be enforced until the amount is filled in. If the payee fills in an amount authorized by the drawer there is no problem. If the payee fills in an unauthorized amount there is an alteration of the check and Section 3-407 [30-3-407] applies.

4. Section 3-302(a)(1) [30-3-302(1)(a)] also bears on the problem of incomplete instruments. Under that section one cannot be a holder in due course if the instrument is so incomplete as to call into question its validity. Subsection (d) of Section 3-115 [30-3-115(4)] is based on the last clause in subsection (2) of present Section 3-115 [30-3-115 prior to 1991 revision].

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "Incomplete instruments. (1) When a paper whose contents at the time of signing show that it is intended to become an instrument is signed while still incomplete in any necessary respect it cannot be enforced until completed, but when it is completed in accordance with authority given it is effective as completed.

(2) If the completion is unauthorized the rules as to material alteration apply (30-3-407), even though the paper was not delivered by the maker or drawer; but the burden of establishing that any completion is unauthorized is on the party so asserting."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

DECISIONS UNDER UNIFORM NEGOTIABLE INSTRUMENTS LAW

Time of Payment of Interest: Where four of the notes held by plaintiff were silent as to the time interest should be paid, plaintiff could have filled in the blanks but there was no obligation to do so, and effect of the contract was the same as if the blanks had been filled in and annual payment of interest specifically stipulated. Mercer v. Mercer, 120 M 132, 180 P2d 248 (1947).

Interest Rate Not Stated: A promissory note payable with interest without specifying the rate of interest carries interest at the legal rate. Burnett v. Burnett, 68 M 546, 219 P 831 (1923).

Forgery Prosecution: In a prosecution for forgery, the rule that the delivery of a writing containing blanks evidently intended to be filled creates an implied authority in the person who receives it to complete the instrument by filling the blanks has no application where the defendant had himself testified that the blanks in the note which he was charged with uttering, while knowing it to be spurious, had all been filled before it was signed. St. v. Mitton, 37 M 366, 96 P 926 (1908). See First Nat'l Bank of Miles City v. Barrett, 52 M 359, 157 P 951 (1916).

30-3-119. Other agreements affecting instrument.

Official Comment

Source: Section 3-117, U.C.C.

Official Comment to 1991 Amendment:

1. The separate agreement might be a security agreement or mortgage or it might be an agreement that contradicts the terms of the instrument. For example, a person may be induced to sign an instrument under an agreement that the signer will not be liable on the instrument unless certain conditions are met. Suppose X requested credit from Creditor who is willing to give the credit only if an acceptable accommodation party will sign the note of X as co-maker. Y agrees to sign as co-maker on the condition that Creditor also obtain the signature of Z as co-maker. Creditor agrees and Y signs as co-maker with X. Creditor fails to obtain the signature of Z on the note. Under Sections 3-412 [30-3-413] and 3-419(b) [30-3-415(2)], Y is obliged to pay the note, but Section 3-117 [30-3-119] applies. In this case, the agreement contradicts the terms of the note and nullifies the obligation of Y. This case is essentially similar to a case in which a maker of a note is induced to sign the note by fraud of the holder. Although the agreement that Y not be liable on the note unless Z also signs may not have been fraudulently made, a subsequent attempt by Creditor to require Y to pay the note in violation of the agreement is a bad faith act. Section 3-117 [30-3-119], in treating the agreement as a defense, allows Y to assert the agreement against Creditor, but the defense would not be good against a subsequent holder in due course of the note that took it without notice of the agreement. If there cannot be a holder in due course because of Section 3-106(d) [30-3-105(4)], a subsequent holder that took the note in good faith, for value and without knowledge of the agreement would not be able to enforce the liability of Y. This result is consistent with the risk that a holder not in due course takes with respect to fraud in inducing issuance of an instrument.

2. The effect of merger or integration clauses to the effect that a writing is intended to be the complete and exclusive statement of the terms of the agreement is left to the supplementary law of the jurisdiction pursuant to Section 1-103 [30-1-103].

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "Other writings affecting instrument. (1) As between the obligor and his immediate obligee or any transferee the terms of an instrument may be modified or affected by any other written agreement executed as a part of the same transaction, except that a holder in due course is not affected by any limitation of his rights arising out of the separate written agreement if he had no notice of the limitation when he took the instrument.

(2) A separate agreement does not affect the negotiability of an instrument."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

30-3-122. Statute of limitations.

Official Comment

Source: Section 3-118, U.C.C.

Official Comment to 1991 Amendment:

1. Proposed Section 3-118 [30-3-122] differs from present Section 3-122 [30-3-122 prior to 1991 revision], which states when a cause of action accrues on an instrument. Section 3-118 [30-3-122] does not define when a cause of action accrues. Accrual of a cause of action is stated in other sections of Article 3 [Title 30, chapter 3] such as those that state the various obligations of parties to an instrument. The only purpose of Section 3-118 [30-3-122] is to define the time within which an action to enforce an obligation, duty, or right arising under Article 3 [Title 30, chapter 3] must be commenced. Section 3-118 [30-3-122] does not attempt to state all rules with respect to a statute of limitations. For example, the circumstances under which the running of a limitations period may be tolled is left to other law pursuant to Section 1-103 [30-3-103].

2. The first six subsections apply to actions to enforce an obligation of any party to an instrument to pay the instrument. This changes present law in that indorsers who may become liable on an instrument after issue are subject to a period of limitations running from the same date as that of the maker or drawer. Subsections (a) and (b) [subsections (1) and (2) of this section] apply to notes. If the note is payable at a definite time, a six-year limitations period starts at the due date of the note, subject to prior acceleration. If the note is payable on demand, there are two limitations periods. Although a note payable on demand could theoretically be called a day after it was issued, the normal expectation of the parties is that the note will remain outstanding until there is some reason to call it. If the law provides that the limitations period does not start until demand is made, the cause of action to enforce it may never be barred. On the other hand, if the limitations period starts when demand for payment may be made, i.e. at any time after the note was issued, the payee of a note on which interest or portions of principal are being paid could lose the right to enforce the note even though it was treated as a continuing obligation by the parties. Some demand notes are not enforced because the payee has forgiven the debt. This is particularly true in family and other noncommercial transactions. A demand note found after the death of the payee may be presented for payment many years after it was issued. The maker may be a relative and it may be difficult to determine whether the note represents a real or a forgiven debt. Subsection (b) [subsection (2) of this section] is designed to bar notes that no longer represent a claim to payment and to require reasonably prompt action to enforce notes on which there is default. If a demand for payment is made to the maker, a six-year limitations period starts to run when demand is made. The second sentence of subsection (b) [subsection (2) of this section] bars an action to enforce a demand note if no demand has been made on the note and no payment of interest or principal has been made for a continuous period of 10 years. This covers the case of a note that does not bear interest or a case in which interest due on the note has not been paid. This kind of case is likely to be a family transaction in which a failure to demand payment may indicate that the holder did not intend to enforce the obligation but neglected to destroy the note. A limitations period that bars stale claims in this kind of case is appropriate if the period is relatively long.

3. Subsection (c) [subsection (3) of this section] applies primarily to personal uncertified checks. Checks are payment instruments rather than credit instruments. The limitations period expires six years after the date of dishonor or 10 years after the date of the check, whichever is earlier. Teller's checks, cashier's checks, certified checks, and traveler's checks are treated differently under subsection (d) [subsection (4) of this section] because they are commonly treated as cash equivalents. A great delay in presenting a cashier's check for payment in most cases will occur because the check was mislaid during that period. The person to whom traveler's checks are issued may hold them indefinitely as a safe form of cash for use in an emergency. There is no compelling reason for barring the claim of the owner of the cashier's check or traveler's check. Under subsection (d) [subsection (4) of this section] the claim is never barred because the six-year limitations period does not start to run until demand for payment is made. The limitations period in subsection (d) [subsection (4) of this section] in effect applies only to cases in which there is a dispute about the legitimacy of the claim of the person demanding payment.

4. Subsection (e) [subsection (5) of this section] covers certificates of deposit. The limitations period doesn't start to run until the depositor demands payment. Most certificates of deposit are payable on demand even if they state a maturity date. The effect of a demand for payment

before maturity is usually that the bank will pay, but that a penalty will be assessed against the depositor in the form of a reduction in the amount of interest that is paid. Subsection (e) [subsection (5) of this section] also provides for cases in which the bank has no obligation to pay until the maturity date. In that case the limitations period doesn't start to run until there is a demand for payment in effect and the maturity date has passed.

5. Subsection (f) [subsection (6) of this section] applies to accepted drafts other than certified checks. When a draft is accepted it is in effect turned into a note of the acceptor. In almost all cases the acceptor will agree to pay at a definite time. Subsection (f) [subsection (6) of this section] states that in that case the six-year limitations period starts to run on the payment date. In the rare case in which the obligation of the acceptor is payable on demand, the six-year limitations period starts to run at the date of the acceptance.

6. Subsection (g) [subsection (7) of this section] covers warranty and conversion cases and other actions to enforce obligations or rights arising under Article 3 [Title 30, chapter 3]. A three-year period is stated and it follows traditional law in stating that the period runs from the time the cause of action accrues.

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "Accrual of cause of action. (1) A cause of action against a maker or an acceptor accrues:

(a) in the case of a time instrument on the day after maturity;

(b) in the case of a demand instrument upon its date or, if no date is stated, on the date of issue.

(2) A cause of action against the obligor of a demand or time certificate of deposit accrues upon demand, but demand on a time certificate may not be made until on or after the date of maturity.

(3) A cause of action against a drawer of a draft or an endorser of any instrument accrues upon demand following dishonor of the instrument. Notice of dishonor is a demand.

(4) Unless an instrument provides otherwise, interest runs at the rate provided by law for a judgment:

(a) in the case of a maker, acceptor or other primary obligor of a demand instrument, from the date of demand;

(b) in all other cases from the date of accrual of the cause of action."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

Specific State Law on Statute of Limitations for Debts Applies to UCC Promissory Notes: The defendant argued that the language of 27-2-409 providing that partial payments on a debt result in the relevant statute of limitations starting to run anew did not apply to promissory notes created under the provisions of the Uniform Commercial Code. The Supreme Court affirmed the District Court's ruling that the statute applies to all debts, including those created under the UCC. Hughes v. Hughes, 2013 MT 176, 370 Mont. 499, 305 P.3d 772.

"Savings Clause" Preserves Existing Statute of Limitations for Debt Collection: After borrowing $25,000 from a Billings bank in the form of a demand note with a March 1, 1991, maturity date, plaintiff Fisher defaulted on the note. The bank attempted to collect the delinquent note, notifying Fisher that the 8-year statute of limitations had not run. Fisher subsequently filed a complaint against the bank, alleging that in conjunction with other modifications to Montana's commercial code, an amendment by the 1991 Legislature, which became effective more than 6 months after his loan default, had shortened the statute of limitations to 6 years. As a result, Fisher argued that the new statute of limitations applied to remove his liability to pay the note. The District Court did not concur with Fisher's assessment, ruling that the applicable statute was the 8-year statute of limitations in effect at the time of default. On appeal, the dispute centered solely around which statute of limitations applied. The Supreme Court affirmed the District Court decision, ruling that the savings clause included in the amendments by the 1991 Legislature preserved the 8-year statute of limitations in effect as of the maturity date of the note. Fisher v. First Citizens Bank, 2000 MT 314, 302 M 473, 14 P3d 1228, 57 St. Rep. 1331 (2000).

30-3-124. Subject matter.

Official Comment

Source: Section 3-102, U.C.C.

Official Comment:

1. Present Article 3 [Title 30, chapter 3, prior to 1991 revision] has no provision affirmatively stating its scope. Present Section 3-103 [30-3-103, now repealed] is a limitation on scope. Proposed Section 3-102 [30-3-124] states that Article 3 [Title 30, chapter 3] applies to "negotiable instruments," defined in Section 3-104 [30-3-104]. Section 3-104(b) [30-3-104(2)] also defines the term "instrument" as a synonym for "negotiable instrument." In most places Article 3 [Title 30, chapter 3] uses the shorter term "instrument." This follows the convention used in present Article 3 [Title 30, chapter 3, prior to 1991 revision].

2. The reference in present Section 3-103(1) [30-3-103, now repealed] to "documents of title" is omitted as superfluous because these documents contain no promise to pay money. Some investment securities also meet the definition of instrument. Present Article 8 [Title 30, chapter 8, prior to 1991 revision] states in Section 8-102(1)(c) [30-8-102(1)(c), substance now in 30-8-112] that "A writing that is a certificated security is governed by this Article and not by Article 3 [Title 30, chapter 3], even though it also meets the requirements of that Article." To conform Article 8 [Title 30, chapter 8] to proposed Section 3-102(a) [30-3-124(1)] the quoted language in Article 8 [Title 30, chapter 8] will have to be amended. The definition of "payment order" in Article 4A [Title 30, chapter 4A] excludes drafts which are governed by Article 3 [Title 30, chapter 3]. Proposed Section 3-102(a) [30-3-124(1)] makes clear that a payment order governed by Article 4A [Title 30, chapter 4A] is not governed by Article 3 [Title 30, chapter 3]. Thus, Article 3 [Title 30, chapter 3] and Article 4A [Title 30, chapter 4A] are mutually exclusive.

3. Although the terms of Article 3 [Title 30, chapter 3] apply to transactions by Federal Reserve Banks, federal preemption would make ineffective any Article 3 [Title 30, chapter 3] provision that conflicts with federal law. The activities of the Federal Reserve Banks are governed by regulations of the Federal Reserve Board and by operating circulars issued by the Reserve Banks themselves. In some instances, the operating circulars are issued pursuant to a Federal Reserve Board regulation. In other cases, the Reserve Bank issues the operating circular under its own authority under the Federal Reserve Act, subject to review by the Federal Reserve Board. Section 3-102(c) [30-3-124(3)] states that Federal Reserve Board regulations and operating circulars of the Federal Reserve Banks supersede any inconsistent provision of Article 3 [Title 30, chapter 3] to the extent of the inconsistency. Federal Reserve Board regulations, being valid exercises of regulatory authority pursuant to a federal statute, take precedence over state law if there is an inconsistency. Childs v. Federal Reserve Bank of Dallas, 719 F.2d 812 (5th Cir. 1983), reh. den. 724 F.2d 127 (5th Cir. 1984). Section 3-102(c) [30-3-124(3)] treats operating circulars as having the same effect whether issued under the Reserve Bank's own authority or under a Federal Reserve Board regulation. Federal statutes may also preempt Article 3 [Title 30, chapter 3]. For example, the Expedited Funds Availability Act, 12 U.S.C. Section 4001 et seq., provides that the Act and the regulations issued pursuant to the Act supersede any inconsistent provisions of the UCC. 12 U.S.C. Section 4007(b).

4. In Clearfield Trust Co. v. United States, 318 U.S. 363 (1943), the Court held that if the United States is a party to an instrument, its rights and duties are governed by federal common law in the absence of a specific federal statute or regulation. In United States v. Kimbell Foods, Inc., 440 U.S. 715 (1979), the Court stated a three-pronged test to ascertain whether the federal common-law rule should follow the state rule. In most instances courts under the Kimbell test have shown a willingness to adopt UCC rules in formulating federal common law on the subject. In Kimbell the Court adopted the priorities rules of Article 9 [Title 30, chapter 9A].

Compiler's Comments

1997 Amendment: Chapter 536 in (1), in second sentence, substituted "30-8-112(1)(d)" for "30-8-102(1)(a)".

30-3-125. Issue of instrument.

Official Comment

Source: Section 3-105, U.C.C.

Official Comment:

1. Under present Section 3-102(1)(a) [30-3-102(1)(a) prior to 1991 revision] "issue" is the first delivery to a "holder or a remitter" but the term "remitter" is neither defined nor otherwise used. Subsection (a) of proposed Section 3-105 [30-3-125(1)] defines "issue" more broadly to include the first delivery to anyone by the drawer or maker made for the purpose of giving rights to anyone on the instrument. "Delivery" with respect to instruments is defined in Section 1-201(14) [30-1-201(14)] as meaning "voluntary transfer of possession."

2. Subsection (b) [subsection (2) of this section] continues the rule that nonissuance, conditional issuance or issuance for a special purpose is a defense of the maker or drawer of an instrument. Thus, the defense can be asserted against a person other than a holder in due course. The same rule applies to nonissuance of an incomplete instrument later completed.

3. Subsection (c) [subsection (3) of this section] defines "issuer" to include the signer of an unissued instrument for convenience of reference in the statute.

30-3-126. Identification of person to whom instrument is payable.

Official Comment

Source: Section 3-110, U.C.C.

Official Comment:

1. Section 3-110 [30-3-126] states rules for determining the identity of the person to whom an instrument is payable if the instrument is payable to an identified person. This issue usually arises in a dispute over the validity of an indorsement in the name of the payee. Subsection (a) [subsection (1) of this section] states the general rule that the person to whom an instrument is payable is determined by the intent of "the person, whether or not authorized, signing as, or in the name or behalf of, the marker or drawer." If X signs a check as drawer of a check on X's account, the intent of X controls. If X, as President of Corporation, signs a check as President in behalf of Corporation as drawer, the intent of X controls. If X forges Y's signature as drawer of a check, the intent of X controls. In the case of a check payable to "John Smith," since there are many people in the world named "John Smith" it is not possible to identify the payee of the check unless there is some further identification or the intention of the drawer is determined. Name alone is sufficient under subsection (a) [subsection (1) of this section], but the intention of the drawer determines which John Smith is the person to whom the check is payable. The same issue is presented in cases of misdescriptions of the payee. The drawer intends to pay a person known to the drawer as John Smith. In fact that person's name is James Smith or John Jones or some other entirely different name. If the check identifies the payee as John Smith, it is nevertheless payable to the person intended by the drawer. That person may indorse the check in either the name John Smith or the person's correct name or in both names. Section 3-204(c) [30-3-203(3)]. The intent of the drawer is also controlling in fictitious payee cases. Section 3-404(b) [30-3-405(2)]. The last sentence of subsection (a) [subsection (1) of this section] refers to rare cases in which the signature of an organization requires more than one signature and the persons signing on behalf of the organization do not all intend the same person as payee. Any person intended by a signer for the organization is the payee and an indorsement by that person is an effective indorsement.

Subsection (b) [subsection (2) of this section] recognizes the fact that in a large number of cases there is no human signer of an instrument because the instrument, usually a check, is produced by automated means such as a check-writing machine. In that case, the relevant intent is that of the person who supplied the name of the payee. In most cases that person is an employee of the drawer, but in some cases the person could be an outsider who is committing a fraud by introducing names of payees of checks into the system that produces the checks. A check-writing machine is likely to be operated by means of a computer in which is stored information as to name and address of the payee and the amount of the check. Access to the computer may allow production of fraudulent checks without knowledge of the organization that is the issuer of the check. Section 3-404(b) [30-3-405(2)] is also concerned with this issue. See Case #4 in Comment 2 to Section 3-404 [30-3-405].

2. Subsection (c) [subsection (3) of this section] allows the payee to be identified in any way including the various ways stated. Subsection (c)(1) [subsection (3)(a) of this section] relates to instruments payable to bank accounts. In some cases the account might be identified by name and number, and the name and number might refer to different persons. For example, a check is payable to "X Corporation Account No. 12345 in Bank of Podunk." Under the last sentence of subsection (c)(1) [subsection (3)(a) of this section], this check is payable to X Corporation and can be negotiated by X Corporation even if Account No. 12345 is some other person's account or the check is not deposited in that account. In other cases the payee is identified by an account number and the name of the owner of the account is not stated. For example, Debtor pays Creditor by issuing a check drawn on Payor Bank. The check is payable to a bank account owned by Creditor but identified only by number. Under the first sentence of subsection (c)(1) [subsection (3)(a) of this section] the check is payable to Creditor and, under Section 1-201(20) [30-1-201(20)], Creditor becomes the holder when the check is delivered. Under Section 3-201(b) [30-3-201(2)], further negotiation of the check requires the indorsement of Creditor. But under Section 4-205 [30-4-205], if the check is taken by a depositary bank for collection, the bank may become a holder

without the indorsement. Under Section 3-102(b) [30-3-124(2)], provisions of Article 4 [Title 30, chapter 4] prevail over those of Article 3 [Title 30, chapter 3]. The depositary bank warrants that the amount of the check was credited to the payee's account.

3. Subsection (c)(2) [subsection (3)(b) of this section] replaces present Section 3-117 [30-3-117, now repealed] and subsection (1)(e), (f), and (g) of present Section 3-110 [30-3-110, now repealed]. This provision merely determines who can deal with an instrument as a holder. It does not determine ownership of the instrument or its proceeds. Subsection (c)(2)(i) [subsection (3)(b)(i) of this section] covers trusts and estates. If the instrument is payable to the trust or estate or to the trustee or representative of the trust or estate, the instrument is payable to the trustee or representative or any successor. Under subsection (c)(2)(ii) [subsection (3)(b)(ii) of this section], if the instrument states that it is payable to Doe, President of X Corporation, either Doe or X Corporation can be holder of the instrument. Subsection (c)(2)(iii) [subsection (3)(b)(iii) of this section] concerns informal organizations that are not legal entities such as unincorporated clubs and the like. Any representative of the members of the organization can act as holder. Subsection (c)(2)(iv) [subsection (3)(b)(iv) of this section] applies principally to instruments payable to public offices such as a check payable to County Tax Collector.

4. Subsection (d) [subsection (4) of this section] replaces present Section 3-116 [30-3-116, now repealed]. An instrument payable to A and B is governed by the first sentence of subsection (d) [subsection (4) of this section]. An instrument payable to A or B is governed by the second sentence of subsection (d) [subsection (4) of this section]. The third sentence is added to address the problem arising when it is not clear whether an instrument is payable to multiple payees alternatively. In the case of ambiguity persons dealing with the instrument should be able to rely on the indorsement of a single payee. For example, an instrument payable to A and/or B is treated like an instrument payable to A or B.

Case Notes

DECISIONS UNDER U.C.C. PRIOR TO 1991 REVISION

Plaintiff Estopped From Denying Ownership of Account: There was substantial evidence to support the District Court's conclusion that plaintiff was equitably estopped from denying his joint and beneficial ownership of a checking account by virtue of his acknowledgment and use of the account and the defendant-bank's reliance thereon in crediting a check to that account. The plaintiff could not complain that he lacked authority to draw checks on the account when he could have remedied that situation simply by signing the signature card. Beyer v. First Nat'l Bank of Dillon, 188 M 208, 612 P2d 1285, 37 St. Rep. 1035 (1980).

Check Payable to Husband and Wife: Normally, when a check is made payable to husband and wife, it is considered to be payable to them jointly and the check must be endorsed by both of them. Beyer v. First Nat'l Bank of Dillon, 188 M 208, 612 P2d 1285, 37 St. Rep. 1035 (1980).

30-3-127. Place of payment.

Official Comment

Source: Section 3-111, U.C.C.

Official Comment:

This is a new section. If an instrument is payable at a bank in the United States, Section 3-501(b)(1) [30-3-504(1)] states that presentment must be made at the place of payment, i.e. the bank.

30-3-128. Interest.

Official Comment

Source: Section 3-112, U.C.C.

Official Comment:

Under Section 3-104(a) [30-3-104(1)] the requirement of a "fixed amount" applies only to principal. The amount of interest payable is that described in the instrument. But if the description of interest in the instrument does not allow for the amount of interest payable to be ascertained, interest is to be payable at the judgment rate. Hence, if an instrument calls for interest, the amount of interest will always be determinable. If a variable rate of interest is prescribed, the amount of interest is ascertainable by reference to the formula or index described or referred to in the instrument. The last sentence of subsection (b) [subsection (2) of this section] replaces subsection (4) of present Section 3-118 [30-3-118, now repealed].

30-3-129. Contradictory terms of instrument.

Official Comment

Source: Section 3-114, U.C.C.

Official Comment:

Section 3-114 [30-3-129] replaces subsections (b) and (c) of present Section 3-118 [30-3-118, now repealed].

30-3-130. Joint and several liability — contribution.

Official Comment

Source: Section 3-116, U.C.C.

Official Comment:

1. Subsection (a) [subsection (1) of this section] replaces subsection (5) of present Section 3-118 [30-3-118, now repealed]. Subsection (b) [subsection (2) of this section] states contribution rights of parties with joint and several liability by referring to applicable law. But subsection (b) [subsection (2) of this section] is subject to Section 3-419(e) [30-3-415(5)]. If one of the parties with joint and several liability is an accommodation party and the other is the accommodated party, Section 3-419(e) [30-3-415(5)] applies. Subsection (c) [subsection (3) of this section] deals with discharge. The discharge of a jointly and severally liable obligor does not affect the right of other obligors to seek contribution from the discharged obligor.

2. Indorsers normally do not have joint and several liability. Rather, an earlier indorser has liability to a later indorser. But indorsers can have joint and several liability in two cases. If an instrument is payable to two payees jointly, both payees must indorse. The indorsement is a joint indorsement and the indorsers have joint and several liability and subsection (b) [subsection (2) of this section] applies. The other case is that of two or more anomalous indorsers. The term is defined in Section 3-205(d) [30-3-204(4)]. An anomalous indorsement normally indicates that the indorser signed as an accommodation party. If more than one accommodation party indorses the instrument the indorsers have joint and several liability and subsection (b) [subsection (2) of this section] applies.

30-3-131. Notice of right to defend action.

Official Comment

Source: Section 3-119, U.C.C.

Official Comment:

This section is a restatement of present Section 3-803 [30-3-803 prior to 1991 revision].

Part 2
Transfer and Negotiation

30-3-202. Negotiation.

Official Comment

Source: Section 3-201, U.C.C.

Prior Uniform Statutory Provision: Sections 30, 31 and 32, Uniform Negotiable Instruments Law.

Official Comment to 1991 Amendment:

1. Subsections (a) and (b) [subsections (1) and (2) of this section] are based in part on subsection (1) of present Section 3-202 [30-3-202(1)]. A person can become holder of an instrument when the instrument is issued to that person, or the status of holder can arise as the result of an event that occurs after issuance. "Negotiation" is the term used in Article 3 [Title 30, chapter 3] to describe this post-issuance event. Normally, negotiation occurs as the result of a voluntary transfer of possession of an instrument by a holder to another person who becomes the holder as a result of the transfer. Negotiation always requires a change in possession of the instrument because nobody can be a holder without possessing the instrument, either directly or through an agent. But in some cases the transfer of possession is involuntary and in some cases the person transferring possession is not a holder. In defining "negotiation" present Section 3-202(1) [30-3-202(1) prior to 1991 revision] uses the word "transfer," an undefined term, and "delivery," defined in Section 1-201(14) [30-1-201(14)] to mean voluntary change of possession. Instead, proposed subsections (a) and (b) [subsections (1) and (2) of this section] use the term "transfer of possession" and, subsection (b) [subsection (2) of this section] states that negotiation can occur by an involuntary transfer of possession. For example, if an instrument is payable to bearer and it is stolen by Thief or is found by Finder, Thief or Finder becomes the holder of the instrument when

possession is obtained. In this case there is an involuntary transfer of possession that results in negotiation to Thief or Finder.

2. In most cases negotiation occurs by a transfer of possession by a holder or remitter. Remitter transactions usually involve a cashier's or teller's check. For example, Buyer buys goods from Seller and pays for them with a cashier's check of Bank that Buyer buys from Bank. The check is issued by Bank when it is delivered to Buyer, regardless of whether the check is payable to Buyer or to Seller. Section 3-105(a) [30-3-125(1)]. If the check is payable to Buyer, negotiation to Seller is done by delivery of the check to Seller after it is indorsed by Buyer. It is more common, however, that the check when issued will be payable to Seller. In that case Buyer is referred to as the "remitter." Section 3-103(a)(11) [30-3-102(1)(k)]. The remitter, although not a party to the check, is the owner of the check until ownership is transferred to Seller by delivery. This transfer is a negotiation because Seller becomes the holder of the check when Seller obtains possession. In some cases Seller may have acted fraudulently in obtaining possession of the check. In those cases Buyer may be entitled to rescind the transfer to Seller because of the fraud and assert a claim of ownership to the check under Section 3-306 [30-3-306] against Seller or a subsequent transferee of the check. Section 3-202(b) [30-3-209(2)] provides for rescission of negotiation, and that provision applies to rescission by a remitter as well as by a holder.

3. Other sections of Article 3 [Title 30, chapter 3] may modify the rule stated in the first sentence of subsection (b) [subsection (2) of this section]. See for example, Sections 3-404 [30-3-404], 3-405 [30-3-405], and 3-406 [30-3-406].

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "Negotiation. (1) Negotiation is the transfer of an instrument in such form that the transferee becomes a holder. If the instrument is payable to order it is negotiated by delivery with any necessary endorsement; if payable to bearer it is negotiated by delivery.

(2) An endorsement must be written by or on behalf of the holder and on the instrument or on a paper so firmly affixed thereto as to become a part thereof.

(3) An endorsement is effective for negotiation only when it conveys the entire instrument or any unpaid residue. If it purports to be of less it operates only as a partial assignment.

(4) Words of assignment, condition, waiver, guaranty, limitation or disclaimer of liability and the like accompanying an endorsement do not affect its character as an endorsement."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

DECISIONS UNDER UNIFORM NEGOTIABLE INSTRUMENTS LAW

Cancellation of Old Note and Mortgage for Execution of New Ones: There is an absence or want of consideration where the party surrendering an old note and mortgage for execution of new ones doesn't own the old ones in the first instance. If plaintiff was not the owner of the original note and mortgage, she was in no position to perform her promise to cancel and surrender the original note and mortgage. Sommer v. Wigen, 103 M 327, 62 P2d 333 (1936).

Instrument Payable to Bearer:

An instrument payable to bearer is negotiated by delivery without endorsement. J. K. & C. S. Mullen Benev. Corp. v. School District, 99 M 388, 43 P2d 902 (1935).

Title to interest coupons which are payable to bearer and possess all the qualities and incidents of commercial paper passes by delivery. J. K. & C. S. Mullen Benev. Corp. v. School District, 99 M 388, 43 P2d 902 (1935).

"Negotiation" Generally: The definition of negotiation contained in this section is complete in itself and expresses the meaning of the term "negotiated" as it was used in the law merchant. Merchants' Nat'l Bank of Billings v. Smith, 59 M 280, 196 P 523, 15 ALR 430 (1921).

Exclusiveness of Method: The method of negotiation prescribed by section 55-404, R.C.M. 1947 (now repealed), is not exclusive. Merchants' Nat'l Bank of Billings v. Smith, 59 M 280, 196 P 523, 15 ALR 430 (1921).

Negotiation of Bearer Note: A note made payable to a named person, with the words "or bearer" added, passes from hand to hand by mere delivery and on becoming due may be enforced by the person holding it. J. I. Case Threshing Mach. Co. v. Simpson, 54 M 316, 170 P 12 (1918).

Payee as Holder in Due Course: The payee of a negotiable promissory note in possession of it is a prima facie holder in due course within the meaning of the Uniform Negotiable Instruments Act, negotiation by endorsement and delivery not being necessary to constitute one a holder in due course. J. I. Case Threshing Mach. Co. v. Simpson, 54 M 316, 170 P 12 (1918).

30-3-203. Indorsement.

Official Comment

Source: Section 3-204, U.C.C.

Prior Uniform Statutory Provision: Section 43, Uniform Negotiable Instruments Law.

Official Comment to 1991 Amendment:

1. Subsection (a) [subsection (1) of this section] is a definition of "indorsement," a term which was not defined in present Article 3 [Title 30, chapter 3, prior to 1991 revision]. Indorsement is defined in terms of the purpose of the signature. If a blank or special indorsement is made to give rights as a holder to a transferee the indorsement is made for the purpose of negotiating the instrument. Subsection (a)(i) [subsection (1)(a) of this section]. If the holder of a check has an account in the drawee bank and wants to be sure that payment of the check will be made by credit to the holder's account, the holder can indorse the check by signing the holder's name with the accompanying words "for deposit only" before presenting the check for payment to the drawee bank. In that case the purpose of the quoted words is to restrict payment of the instrument. Subsection (a)(ii) [subsection (1)(b) of this section]. If X wants to guarantee payment of a note signed by Y as maker, X can do so by signing X's name to the back of the note as an indorser. This indorsement is known as an anomalous indorsement (Section 3-205(d) [30-3-204(4)]) and is made for the purpose of incurring indorser's liability on the note. Subsection (a)(iii) [subsection (1)(c) of this section]. In some cases an indorsement may serve more than one purpose. For example, if the holder of a check deposits it to the holder's account in a depositary bank for collection and indorses the check by signing the holder's name with the accompanying words "for deposit only" the purpose of the indorsement is both to negotiate the check to the depositary bank and to restrict payment of the check.

The but clause of the first sentence of subsection (a) [subsection (1) of this section] elaborates on present Section 3-402 [30-3-402, now repealed]. In some cases it may not be clear whether a signature was meant to be that of an indorser, a party to the instrument in some other capacity such as drawer, maker or acceptor, or a person who was not signing as a party. The general rule is that a signature is an indorsement if the instrument does not indicate an unambiguous intent of the signer not to sign as an indorser. Intent may be determined by words accompanying the signature, the place of signature, or other circumstances. For example, suppose a depositary bank gives cash for a check properly indorsed by the payee. The bank requires the payee's employee to sign the back of the check. If the signature consists only of the initials of the employee it is not reasonable to assume that it was meant to be an indorsement. If there was a full signature but accompanying words indicated that it was meant as a receipt for the cash proceeds of the check, it is not an indorsement. If the signature is not qualified in any way and appears in the place normally used for indorsements, it may be an indorsement even though the signer intended the signature to be a receipt. To take another example, suppose the drawee of a draft signs the draft on the back in the space usually used for indorsements. No words accompany the signature. Since the drawee has no reason to sign a draft unless the intent is to accept the draft, the signature is effective as an acceptance. Custom and usage may be used to determine intent. For example, by long established custom and usage, a signature in the lower right hand corner of an instrument indicates an intent to sign as the maker of a note or the drawer of a draft. Any similar clear indication of an intent to sign in some other capacity may be enough to establish that a signature is not an indorsement.

The last sentence of subsection (a) [subsection (1) of this section] is based on subsection (2) of present Section 3-202 [30-3-202(2) prior to 1991 revision]. An indorsement on an allonge is valid even though there is sufficient space on the instrument for an indorsement.

2. Assume that Payee indorses a note to Creditor as security for a debt. Under subsection (b) of Section 3-203 [30-3-210(2)] Creditor takes Payee's rights to enforce or transfer the instrument subject to the limitations imposed by Article 9 [Title 30, chapter 9A]. Subsection (c) of Section 3-204 [30-3-203(3)] makes clear that Payee's indorsement to Creditor, even though it mentions creation of a security interest, is an unqualified indorsement that gives to Creditor the right to enforce the note as its holder.

3. Subsection (d) [subsection (4) of this section] is a restatement of present Section 3-203 [30-3-203 prior to 1991 revision]. Section 3-110(a) [30-3-126(1)] states that an instrument is payable to the person intended by the person signing as or in the name or behalf of the maker or drawer even if that person is identified by a name that is not the true name of the person. In some cases the name used in the instrument is a misspelling of the correct name and in some cases the two names may be entirely different. The payee may indorse in the name used in the instrument, in the payee's correct name, or in both. In each case the indorsement is effective. But because an

indorsement in a name different from that used in the instrument may raise a question about its validity and an indorsement in a name that is not the correct name of the payee may raise a problem of identifying the indorser, the accepted commercial practice is to indorse in both names. Subsection (d) [subsection (4) of this section] allows a person paying or taking the instrument for value or collection to require indorsement in both names.

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "Wrong or misspelled name. Where an instrument is made payable to a person under a misspelled name or one other than his own he may endorse in that name or his own or both; but signature in both names may be required by a person paying or giving value for the instrument."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

30-3-204. Special indorsement — blank indorsement — anomalous indorsement.

Official Comment

Source: Section 3-205, U.C.C.

Prior Uniform Statutory Provision: Sections 9(5), 33, 34, 35, 36, and 40, Uniform Negotiable Instruments Law.

Official Comment to 1991 Amendment:

1. Subsection (a) [subsection (1) of this section] is based on subsection (1) of present Section 3-204 [30-3-204(1) prior to 1991 revision]. It states the test of a special indorsement to be whether the indorsement identifies a person to whom the instrument is payable. Section 3-110 [30-3-126] states rules for identifying the payee of an instrument. Section 3-205(a) [30-3-204(1)] incorporates the principles stated in Section 3-110 [30-3-126] in identifying an indorsee. The language of Section 3-110 [30-3-126] refers to language used by the drawer or maker. When that section is used with respect to an indorsement, Section 3-110 [30-3-126] must be read as referring to the language used by the indorser.

2. Subsection (b) [subsection (2) of this section] is based on subsection (2) of present Section 3-204 [30-3-204(2) prior to 1991 revision]. An indorsement made by the holder is either a special or blank indorsement. If the indorsement is made by a holder and is not a special indorsement, it is a blank indorsement. A blank indorsement is usually the signature of the indorser on the back of the instrument without other words. Subsection (c) [subsection (3) of this section] is based on subsection (3) of present Section 3-204 [30-3-204(3) prior to 1991 revision]. A "restrictive indorsement" described in Section 3-206 [30-3-205] can be either a blank indorsement or a special indorsement. "Pay to T, in trust for B" is a restrictive indorsement. It is also a special indorsement because it identifies T as the person to whom the instrument is payable. "For deposit only" followed by the signature of the payee of a check is a restrictive indorsement. It is also a blank indorsement because it does not identify the person to whom the instrument is payable.

3. The only effect of an "anomalous indorsement," defined in subsection (d) [subsection (4) of this section], is to make the signer liable on the instrument as an indorser. Such an indorsement is normally made by an accommodation party. Section 3-419 [30-3-415].

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "Special endorsement — blank endorsement. (1) A special endorsement specifies the person to whom or to whose order it makes the instrument payable. Any instrument specially endorsed becomes payable to the order of the special endorsee and may be further negotiated only by his endorsement.

(2) An endorsement in blank specifies no particular endorsee and may consist of a mere signature. An instrument payable to order and endorsed in blank becomes payable to bearer and may be negotiated by delivery alone until specially endorsed.

(3) The holder may convert a blank endorsement into a special endorsement by writing over the signature of the endorser in blank any contract consistent with the character of the endorsement."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

30-3-205. Restrictive indorsement.

Official Comment

Source: Section 3-206, U.C.C.

Prior Uniform Statutory Provision: Sections 36 and 39, Uniform Negotiable Instruments Law.

Official Comment to 1991 Amendment:

1. This section replaces present Sections 3-205 [30-3-205 prior to 1991 revision] and 3-206 [30-3-206, now repealed] and attempts to clarify the law of restrictive indorsements.

2. Subsection (a) [subsection (1) of this section] provides that an indorsement that purports to limit further transfer or negotiation is ineffective to prevent further transfer or negotiation. If a payee indorses "Pay A only," A may negotiate the instrument to subsequent holders who may ignore the restriction on the indorsement. Subsection (b) [subsection (2) of this section] provides that an indorsement that states a condition to the right of a holder to receive payment is ineffective to condition payment. Thus if a payee indorses "Pay A if A ships goods complying with our contract," the right of A to enforce the instrument is not affected by the condition. In the case of a note, the obligation of the maker to pay A is not affected by the indorsement. In the case of a check, the drawee can pay A without regard to the condition, and if the check is dishonored the drawer is liable to pay A. If the check was negotiated by the payee to A in return for a promise to perform a contract and the promise was not kept, the payee would have a defense or counterclaim against A if the check were dishonored and A sued the payee as indorser, but the payee would have that defense or counterclaim whether or not the condition to the right of A was expressed in the indorsement. Present Section 3-206 [30-3-206, now repealed] treats a conditional indorsement like indorsements for deposit or collection. Proposed subsection (b) [subsection (2) of this section] rejects that approach and makes the conditional indorsement ineffective with respect to parties other than the indorser and indorsee. Since the indorsements referred to in subsections (a) and (b) [subsections (1) and (2) of this section] are not effective as restrictive indorsements, they are no longer described as restrictive indorsements.

3. The great majority of restrictive indorsements are those that fall within subsection (c) [subsection (3) of this section] which continues present law. The depositary bank or the payor bank, if it takes the check for immediate payment over the counter, must act consistently with the indorsement, but an intermediary bank or payor bank that takes the check from a collecting bank is not affected by the indorsement. Any other person is also bound by the indorsement. For example, a check is payable to X, who indorses in blank but writes above the signature the words "For deposit only." The check is stolen and is cashed at a grocery store by the thief. The grocery store indorses the check and deposits it in Depositary Bank. The account of the grocery store is credited and the check is forwarded to Payor Bank which pays the check. Under subsection (c) [subsection (3) of this section], the grocery store and Depositary Bank are converters of the check because X did not receive the proceeds of the check. Payor Bank and any intermediary bank in the collection process are not liable to X.

4. Subsection (d) [subsection (4) of this section] is based on subsection (4) of present Section 3-206 [30-3-206, now repealed]. Payee indorses a check "Pay to T in trust for B." T indorses in blank and delivers it to (a) Holder for value; (b) Depositary Bank for collection; or (c) Payor Bank for payment. In each case these takers can safely pay T so long as they have no notice under proposed Section 3-307 [30-3-308] of any breach of trust that T may be committing. For example, under subsection (a) of proposed Section 3-307 [30-3-308(1)] these takers have notice of a breach of trust if the check was taken in any transaction known by the taker to be for T's personal benefit. Subsequent transferees of the check from Holder or Depositary Bank are not affected by the restriction unless they have knowledge that T dealt with the check in breach of trust.

5. Subsection (f) [subsection (6) of this section] allows a restrictive indorsement to be used as a defense by a person obliged to pay the instrument if that person would be liable for paying in violation of the indorsement.

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "Restrictive endorsements. An endorsement is restrictive which either:

(a) is conditional; or

(b) purports to prohibit further transfer of the instrument; or

(c) includes the words "for collection", "for deposit", "pay any bank", or like terms signifying a purpose of deposit or collection; or

(d) otherwise states that it is for the benefit or use of the endorser or of another person."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

Existence of Fiduciary Duty Considered Question of Law, Not Fact — Summary Judgment on Question Proper if No Genuine Issue of Material Fact Exists: To resolve several inconsistent prior opinions, the Supreme Court held that the issue of whether a fiduciary duty exists between two parties is a question of law, not fact, and thus may be resolved on summary judgment if no genuine issues of material fact exist. Similarly, the issue of whether a special relationship exists between two parties that would give rise to a fiduciary relationship is also a question of law, not fact. In order to determine whether a special relationship exists in cases in which it does not normally exist, such as between a bank and a customer, a court may be required to make a fact-intensive inquiry. The circumstances of a particular relationship are factual, so disputes over material facts will preclude summary judgment, but the conclusion drawn by a court from undisputed facts is one of law, not of fact. Gliko v. Permann, 2006 MT 30, 331 M 112, 130 P3d 155 (2006), overruling Davis v. Church of Jesus Christ of Latter Day Saints, 258 M 286, 852 P2d 640 (1993), and Kondelik v. First Fidelity Bank of Glendive, 259 M 446, 857 P2d 687 (1993).

30-3-208. Reacquisition.

Official Comment

Source: Section 3-207, U.C.C.

Prior Uniform Statutory Provision: Sections 48, 50 and 121, Uniform Negotiable Instruments Law.

Official Comment to 1991 Amendment:

Section 3-207 [30-3-208] restates present Section 3-208 [30-3-208 prior to 1991 revision]. Reacquisition refers to cases in which a former holder reacquires the instrument either by negotiation from the present holder or by a transfer other than negotiation. If the reacquisition is by negotiation, the former holder reacquires the status of holder. Although Section 3-207 [30-3-208] allows the holder to cancel all indorsements made after the holder first acquired holder status, cancellation is not necessary. Status of holder is not affected whether or not cancellation is made. But if the reacquisition is not the result of negotiation the former holder can obtain holder status only by striking the former holder's indorsement and any subsequent indorsements. The latter case is an exception to the general rule that if an instrument is payable to an identified person, the indorsement of that person is necessary to allow a subsequent transferee to obtain the status of holder. Reacquisition without indorsement by the person to whom the instrument is payable is illustrated by two examples:

Case #1. X, a former holder, buys the instrument from Y, the present holder. Y delivers the instrument to X but fails to indorse it. Negotiation does not occur because the transfer of possession did not result in X's becoming holder. Section 3-201(a) [30-3-202(1)]. The instrument by its terms is payable to Y, not to X. But X can obtain the status of holder by striking X's indorsement and all subsequent indorsements. When these indorsements are struck, the instrument by its terms is payable either to X or to bearer, depending upon how X originally became holder. In either case X becomes holder. Section 1-201(20) [30-1-201(20)].

Case #2. X, the holder of an instrument payable to X, negotiates it to Y by special indorsement. The negotiation is part of an underlying transaction between X and Y. The underlying transaction is rescinded by agreement of X and Y, and Y returns the instrument without Y's indorsement. The analysis is the same as that in Case #1. X can obtain holder status by cancelling X's indorsement to Y. In Case #1 and Case #2, X acquired ownership of the instrument after reacquisition, but X's title was clouded because the instrument by its terms was not payable to X. Normally, X can remedy the problem by obtaining Y's indorsement, but in some cases X may not be able to conveniently obtain that indorsement. Section 3-208 [30-3-208] is a rule of convenience which relieves X of the burden of obtaining an indorsement that serves no substantive purpose. The effect of cancellation of any indorsement under Section 3-208 [30-3-208] is to nullify it. Thus, the person whose indorsement is canceled is relieved of indorser's liability. Since cancellation is notice of discharge, discharge is effective even with respect to the rights of a holder in due course. Sections 3-601 [30-3-601] and 3-604 [30-3-605].

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "Where an instrument is returned to or reacquired by a prior party he may cancel any endorsement which is not necessary to his title and reissue or further negotiate the instrument, but any intervening party is discharged as against the reacquiring party and subsequent holders not in due course and if his endorsement has been canceled is discharged as against subsequent holders in due course as well."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

30-3-209. Negotiation subject to rescission.

Official Comment

Source: Section 3-202, U.C.C.

Official Comment:

1. This section is based on present Section 3-207 [30-3-207, now repealed]. Subsection (2) of present Section 3-207 [30-3-207, now repealed] prohibits the rescinding of a negotiation against holders in due course. Subsection (b) of proposed Section 3-202 [30-3-209(2)] extends this protection to payor banks.

2. Subsection (a) [subsection (1) of this section] applies even though the lack of capacity or the illegality, is of a character which goes to the essence of the transaction and makes it entirely void. It is inherent in the character of negotiable instruments that any person in possession of an instrument which by its terms is payable to that person or to bearer is a holder and may be dealt with by anyone as a holder. The principle finds its most extreme application in the well settled rule that a holder in due course may take the instrument even from a thief and be protected against the claim of the rightful owner. The policy of subsection (a) [subsection (1) of this section] is that any person to whom an instrument is negotiated is a holder until the instrument has been recovered from that person's possession. The remedy of a person with a claim to an instrument is to recover the instrument by replevin or otherwise; to impound it or to enjoin its enforcement, collection or negotiation; to recover its proceeds from the holder; or to intervene in any action brought by the holder against the obligor. As provided in Section 3-305(c) [30-3-305(3)], the claim of the claimant is not a defense to the obligor unless the claimant defends the action.

3. There can be no rescission or other remedy against a holder in due course even though the prior negotiation may have been fraudulent or illegal in its essence and entirely void. As against any other party the claimant may have any remedy permitted by law. This section is not intended to specify what that remedy may be, or to prevent any court from imposing conditions or limitations such as prompt action or return of the consideration received. All such questions are left to the law of the particular jurisdiction. Section 3-202 [30-3-209] gives no right that would not otherwise exist. The section is intended to mean that any remedies afforded by other law are cut off only by a holder in due course.

Case Notes

DECISIONS UNDER UNIFORM NEGOTIABLE INSTRUMENTS LAW

Assignee of Holder: Where payee negotiated check to supplier and payee's father purchased check stamped "payment stopped" from supplier for value, payee's father took check by assignment and not by negotiation and acquired whatever rights supplier enjoyed under the instrument. Tesdahl v. Hiebert, 148 M 241, 419 P2d 298 (1966).

30-3-210. Rights acquired by transfer.

Official Comment

Source: Section 3-203, U.C.C.

Official Comment:

1. Section 3-203 [30-3-210] is based on present Section 3-201 [30-3-201, now repealed] which states that a transferee receives such rights as the transferor has. The present section is confusing because some rights of the transferor are not vested in the transferee unless the transfer is a negotiation. For example, a transferee that does not become the holder can not negotiate the instrument, a right that the transferor had. Present Section 3-201 [30-3-201, now repealed] does not define "transfer." Subsection (a) [subsection (1) of this section] defines transfer by limiting it to cases in which possession of the instrument is delivered. It excludes cases in which the owner of an instrument may attempt to give ownership rights to someone else without delivering the instrument. For example, X is the owner and holder of an instrument payable to X. X sells the instrument to Y but is unable to deliver immediate possession to Y. Instead, Y signs a document transferring all of X's right, title, and interest in the instrument to Y. Although the document may be effective to give Y a claim to ownership of the instrument, Y is not a person entitled to enforce the instrument under Section 3-301 [30-3-301] until Y obtains possession of the instrument. That kind of transaction is not covered by Section 3-203(a) [30-3-210(1)]. The instrument is not transferred until it is delivered. An instrument is a reified right to payment. The right is represented by the instrument itself. The right to payment is transferred by delivery of possession of the instrument "by a person other than its issuer for the purpose of giving to the person receiving delivery the right to enforce the instrument." The quoted phrase excludes issue of an instrument, defined in Section 3-105 [30-3-125], and cases in which a transfer of possession

is for some other purpose than transfer of the right to enforce. Subsection (a) [subsection (1) of this section] is designed to clarify present law rather than to change it.

2. Subsection (b) [subsection (2) of this section] states that transfer vests in the transferee any right of the transferor to enforce the instrument "including any right as a holder in due course." If the transferee is not a holder because the transferor did not indorse, the transferee is nevertheless a person entitled to enforce the instrument under Section 3-301 [30-3-301] if the transferor was a holder at the time of transfer. Although the transferee is not a holder, under subsection (b) [subsection (2) of this section] the transferee obtained the rights of the transferor as holder. Because the transferee's rights are derivative of the transferor's rights, those rights must be proved. Because the transferee is not a holder, there is no presumption under Section 3-308 [30-3-307] that the transferee, by producing the instrument, is entitled to payment. The instrument, by its terms, is not payable to the transferee and the transferee must account for possession of the unindorsed instrument by proving the transaction through which the transferee acquired it. Proof of a transfer to the transferee by a holder is proof that the transferee has acquired the rights of a holder. At that point the transferee is entitled to the presumption under Section 3-308 [30-3-307].

Under subsection (b) [subsection (2) of this section] a holder in due course that transfers an instrument transfers those rights as a holder in due course to the purchaser. The policy is to assure the holder in due course a free market for the instrument. There is one exception to this rule stated in the concluding clause of subsection (b) [subsection (2) of this section]. A person who is party to fraud or illegality affecting the instrument is not permitted to wash the instrument clean by passing it into the hands of a holder in due course and then repurchasing it.

3. Subsection (c) [subsection (3) of this section] applies only to a transfer for value. It applies only if the instrument is payable to order or specially indorsed to the transferor. The transferee acquires, in the absence of a contrary agreement, the specifically enforceable right to the indorsement of the transferor. Unless otherwise agreed, it is a right to the general indorsement of the transferor with full liability as indorser, rather than to an indorsement without recourse. The question may arise if the transferee has paid in advance and the indorsement is omitted fraudulently or through oversight. A transferor who is willing to indorse only without recourse or unwilling to indorse at all should make those intentions clear before transfer. The agreement of the transferee to take less than an unqualified indorsement need not be an express one, and the understanding may be implied from conduct, from past practice, or from the circumstances of the transaction. Subsection (c) [subsection (3) of this section] provides that there is no negotiation of the instrument until the indorsement by the transferor is made. Until that time the transferee does not become a holder, and if earlier notice of a defense or claim is received, the transferee does not qualify as a holder in due course under Section 3-302 [30-3-302].

4. The operation of Section 3-203 [30-3-210] is illustrated by the following cases. In each case Payee, by fraud, induced Maker to issue a note to Payee. The fraud is a defense to the obligation of Maker to pay the note under Section 3-305(a)(2) [30-3-305(1)(b)].

Case #1. Payee negotiated the note to X who took as a holder in due course. After the instrument became overdue X negotiated the note to Y who had notice of the fraud. Y succeeds to X's rights as a holder in due course and takes free of Maker's defense of fraud.

Case #2. Payee negotiated the note to X who took as a holder in due course. Payee then repurchased the note from X. Payee does not succeed to X's rights as a holder in due course and is subject to Maker's defense of fraud.

Case #3. Payee negotiated the note to X who took as a holder in due course. X sold the note to Purchaser who received possession. The note, however, was indorsed to X and X failed to indorse it. Purchaser is a person entitled to enforce the instrument under Section 3-301 [30-3-301] and succeeds to the rights of X as holder in due course. Purchaser is not a holder, however, and under Section 3-308 [30-3-307] Purchaser will have to prove the transaction with X under which the rights of X as holder in due course were acquired.

Case #4. Payee sold the note to Purchaser who took for value, in good faith and without notice of the defense of Maker. Purchaser received possession of the note but Payee neglected to indorse it. Purchaser became a person entitled to enforce the instrument but did not become holder because of the missing indorsement. If Purchaser received notice of the defense of Maker before obtaining the indorsement of Payee, Purchaser cannot become a holder in due course because at the time notice was received the note had not been negotiated to Purchaser. If indorsement by Payee was made after Purchaser received notice, Purchaser had notice of the defense when it became holder.

5. Subsection (d) [subsection (4) of this section] restates present Section 3-202(3) [30-3-202(3) prior to 1991 revision]. The cause of action on an instrument cannot be split. Any indorsement which purports to convey to any party less than the entire amount of the instrument is not effective for negotiation. This is true of either "Pay A one-half," or "Pay A two-thirds and B one-third." Neither A nor B becomes a holder. On the other hand an indorsement reading merely "Pay A and B" is effective, since it transfers the entire cause of action to A and B as tenants in common.

The partial indorsement does, however, operate as a partial assignment of the cause of action. Subsection (d) [subsection (4) of this section] makes no attempt to state the legal effect of such an assignment, which is left to other law. A partial assignee of an instrument has rights only to the extent the applicable law gives rights, either at law or in equity, to a partial assignee.

Case Notes

DECISIONS UNDER U.C.C. PRIOR TO 1991 REVISION

Payee-Assignor's Right to Attorney Fees Provided for by Note: Maker gave payee a promissory note which provided that maker would pay reasonable attorney fees incurred in collection of the note. Payee assigned it to corporation which sued maker on the note, maker in turn filing a third-party complaint against payee-assignor for fraudulent inducement for the note, wrongful assignment of it, and lack of consideration for it. Payee-assignor had no right to attorney fees as against maker, either under the note or under 28-3-704, which provides that when a contract grants the right to recover attorney fees to one party to the contract, then all parties to the contract have that right in any action on the contract. He had assigned all his rights under the note, and the complaint against him was not a collection action under the note. Sliter's v. Lee, 197 M 182, 641 P2d 475, 39 St. Rep. 453 (1982).

DECISIONS UNDER UNIFORM NEGOTIABLE INSTRUMENTS LAW

Ownership of Unendorsed Note: Upon transfer of a mortgage note payable to order without endorsement, title vested in the transferee; hence where the fact that the plaintiff assignee in his action to foreclose the mortgage bought the note from the mortgagee was uncontradicted and he produced it at the trial, a finding that he had failed to produce competent evidence of its ownership was error. Leffek v. Luedeman, 95 M 457, 27 P2d 511, 91 ALR 286 (1933).

Negotiability — Effect of Transfer Without Endorsement: The transfer of a negotiable instrument without endorsement destroys its negotiability. Mills v. Pope, 90 M 569, 4 P2d 485 (1931).

Delivery Without Endorsement: It has been said in a number of cases that delivery without endorsement transfers the title of the transferor. J. I. Case Threshing Mach. Co. v. Simpson, 54 M 316, 170 P 12 (1918).

Part 3
Rights of a Holder

30-3-301. Person entitled to enforce instrument.

Official Comment

Source: Section 3-301, U.C.C.

Prior Uniform Statutory Provision: Section 51, Uniform Negotiable Instruments Law.

Official Comment to 1991 Amendment:

This section replaces present Section 3-301 [30-3-301], which states the rights of a holder. It is not necessary to state the rights of a holder. Other sections of proposed Article 3 [Title 30, chapter 3] make clear how an instrument is negotiated and how discharge is made. Instead this section defines "person entitled to enforce" an instrument. The definition recognizes that enforcement is not limited to holders. The quoted phrase includes a person enforcing a lost or stolen instrument. Section 3-309 [30-3-309]. It also includes a person in possession of an instrument who is not a holder. A nonholder in possession of an instrument includes a person that acquired rights of a holder by subrogation or under Section 3-203(a) [30-3-210(a)]. It also includes any other person who under applicable law is a successor to the holder or otherwise acquires the holder's rights.

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "Rights of a holder. The holder of an instrument whether or not he is the owner may transfer or negotiate it and, except as otherwise provided in 30-3-603 on payment or satisfaction, discharge it or enforce payment in his own name."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

DECISIONS UNDER U.C.C. PRIOR TO 1991 REVISION

Out-of-State Bank Not Party to Be Joined: Interest in loans transferred to out-of-state bank under participation agreement between lending Montana bank and out-of-state bank prior to commencement of action does not make out-of-state bank true party in interest or person to be joined if feasible when borrower sued on loan agreement and notes payable to lending Montana bank because loan agreement only establishes rights and liabilities between lending Montana bank and borrower, while participation agreement only establishes rights and liabilities between lending Montana bank and out-of-state bank. Neither establishes any contractual relationship, rights or liabilities between borrower and out-of-state bank. Additionally lending Montana bank is owner and sole payee on notes and as holder of notes is entitled to sue in its own name. State ex rel. Drum v. District Court, 169 M 494, 548 P2d 1377 (1976).

DECISIONS UNDER UNIFORM NEGOTIABLE INSTRUMENTS LAW

Law Governing: Where a contract for the repair of drawer's tractor by payee was entered into and performed in State of Washington, and payee negotiated check to Washington supplier, and assignment of check by supplier to creditor occurred in Washington, Washington law was applied in creditor's suit on check against drawer. Tesdahl v. Hiebert, 148 M 241, 419 P2d 298 (1966).

Bona Fide Purchaser: Where payee negotiated check to supplier for face amount of check and supplier lacked notice, either actual or constructive, of any defect in instrument, supplier was "holder in due course" and took instrument free from any defenses existing between drawer and payee. Tesdahl v. Hiebert, 148 M 241, 419 P2d 298 (1966).

Affirmative Defense: Where territorial rights for sales of packaged hosiery were given to defendants in return for $10,000 which was represented by a note made payable to plaintiff, the affirmative defense, in action for $6,000 unpaid on note, that plaintiff had breached agreement by doing business in restricted territory was not a complete and valid defense but was an offset to be determined by testimony in mitigation of unpaid balance on note. Leiman-Scott, Inc. v. Holmes, 142 M 58, 381 P2d 489 (1963).

When Entitled to Position of Holder: In action on a check, plaintiff is not entitled to position of a holder in due course unless check was regular upon its face, plaintiff had no notice of any infirmity therein, and plaintiff took it in good faith. Miles City Bank v. Askin, 119 M 581, 179 P2d 750, 171 ALR 790 (1947).

Action by Administrator: The mere possession of a promissory note by a foreign administrator, made payable to the order of and transferred to his intestate but never endorsed, does not constitute him a holder thereof within the meaning of the Negotiable Instruments Law, and he is therefore not entitled to maintain an action thereon in his individual capacity but may maintain it only in his representative capacity after taking out ancillary letters. Parcells v. Price, 110 M 537, 104 P2d 12 (1940); State ex rel. Freebourn v. Merchants' Credit Serv., Inc., 104 M 76, 66 P2d 337 (1937), overruled on other grounds, Rae v. Cameron, 112 M 159, 114 P2d 1060 (1941); Lefebure v. Baker, 69 M 193, 220 P 1111 (1923), distinguished in In re Livingston's Estate, 91 M 584, 9 P2d 159 (1932).

Estoppel to Assert: One reaping benefit of his note to county for balance due him on depository bond by reduction of legal interest rate, release of bond obligation, and extension of time for payment thereof, during which Statute of Limitations ran against action on bond, and recognizing validity of note by making some payments thereon, will not be permitted to say that it is invalid and unenforceable as postponing obligation or liability in violation of Constitution. Fergus County v. Osweiler, 107 M 466, 86 P2d 410, 120 ALR 1457 (1938).

Plea of Undue Influence: In action on note, answer showing that defendant, plaintiff's brother, suffered from paresis which had weakened his mind, that he reposed special confidence in plaintiff, and that plaintiff, taking advantage of confidence, unduly influenced defendant to make the note, was sufficient as a plea of undue influence. Stagg v. Stagg, 96 M 573, 32 P2d 856 (1934).

Allegation of Ownership Not Required: A holder of a note may maintain an action for its collection; it is not required that the plaintiff in such an action allege in his complaint that he is owner at the time. J. I. Case Threshing Mach. Co. v. Simpson, 54 M 316, 170 P 12 (1918), distinguished in Cont. Supply Co. v. White, 92 M 254, 12 P2d 569 (1932), explained in Woody v. Sec. St. Bank, 67 M 109, 214 P 1096 (1923).

Complaint — Allegation as to Ownership: In action on note plaintiff must allege that he is the holder or owner of the note. Young v. Bray, 54 M 415, 170 P 1044 (1918). See also Matteson v. Trask, 63 M 160, 206 P 428 (1922).

30-3-302. Holder in due course.

Official Comment

Source: Section 3-302, U.C.C.

Prior Uniform Statutory Provision: Section 52, Uniform Negotiable Instruments Law.

Official Comment to 1991 Amendment:

1. Subsection (a)(1) [subsection (1)(a) of this section] is a return to the N.I.L. rule that the taker of an irregular or incomplete instrument is not a person the law should protect against defenses of the obligor or claims of prior owners. This reflects a policy choice against extending the harsh holder in due course doctrine to an instrument that is so incomplete or irregular "as to call into question its authenticity." The term "authenticity" is used to make it clear that the irregularity or incompleteness must indicate that the instrument may not be what it purports to be. Persons who purchase or pay such instruments should do so at their own risk. Under subsection (1) of present Section 3-304 [30-3-304(1) prior to 1991 revision], irregularity or incompleteness gives a purchaser notice of a claim or defense. But it is not clear from that provision whether the claim or defense must be related to the irregularity or incomplete aspect of the instrument. This ambiguity is not present in proposed subsection (a)(1) [subsection (1)(a) of this section].

2. Subsection (a)(2) [subsection (1)(b) of this section] restates subsection (1) of present Section 3-302 [30-3-302(1) prior to 1991 revision]. Section 3-305(a) [30-3-305(1)] makes a distinction between defenses to the obligation to pay an instrument and claims in recoupment by the maker or drawer that may be asserted to reduce the amount payable on the instrument. Because of this change to Section 3-305 [30-3-305], the reference in subsection (a)(2)(vi) [subsection (1)(b)(vi) of this section] is to both a defense and a claim in recoupment. Notice of forgery or alteration is stated separately because forgery and alteration are not technically defenses under subsection (a) of Section 3-305 [30-3-305(1)].

3. Discharge is also separately treated in the first sentence of subsection (b) [subsection (2) of this section]. Except for discharge in an insolvency proceeding, which is specifically stated to be a real defense in Section 3-305(a)(1) [30-3-305(1)(a)], discharge is not expressed in Article 3 [Title 30, chapter 3] as a defense and is not included in Section 3-305(a)(2) [30-3-305(1)(b)]. Discharge is effective against anybody except a person having rights of a holder in due course who took the instrument without notice of the discharge. Notice of discharge does not disqualify a person from becoming a holder in due course. For example, a check certified after it is negotiated by the payee may subsequently be negotiated to a holder. If the holder had notice that the certification occurred after negotiation by the payee, the holder necessarily had notice of the discharge of the payee as indorser. Section 3-415(d) [30-3-414(4)]. Notice of that discharge does not prevent the holder from becoming a holder in due course, but the discharge is effective against the holder. Section 3-601(b) [30-3-601(2)]. Notice of a defense under Section 3-305(a)(1) [30-3-305(1)(a)] of a maker, drawer or acceptor based on a bankruptcy discharge is different. There is no reason to give holder in due course status to a person with notice of that defense. The second sentence of subsection (b) [subsection (2) of this section] is from present Section 3-304(5) [30-3-304(5) prior to 1991 revision].

4. Professor Britton in his treatise Bills and Notes 309 (1961) stated: "A substantial number of decisions before the [N.I.L.] indicates that at common law there was nothing in the position of the payee as such which made it impossible for him to be a holder in due course." The courts were divided, however, about whether the payee of an instrument could be a holder in due course under the N.I.L.. Some courts read N.I.L. Section 52(4) to mean that a person could be a holder in due course only if the instrument was "negotiated" to that person. N.I.L. Section 30 stated that "an instrument is negotiated when it is transferred from one person to another in such manner as to constitute the transferee the holder thereof." Normally, an instrument is "issued" to the payee; it is not transferred to the payee. N.I.L. Section 191 defined "issue" as the "first delivery of the instrument . . . to a person who takes it as a holder." Thus, some courts concluded that the payee never could be a holder in due course. Other courts concluded that there was no evidence that the N.I.L. was intended to change the common law rule that the payee could be a holder in due course. Professor Britton states on p. 318: "The typical situations which raise the [issue] are those where the defense of a maker is interposed because of fraud by a [maker who is] principal debtor . . . against a surety co-maker, or where the defense of fraud by a purchasing remitter is interposed by the drawer of the instrument against the good faith purchasing payee."

Present Section 3-302(2) [30-3-302(2) prior to 1991 revision] states: "A payee may be a holder in due course." This provision was intended to resolve the split of authority under the N.I.L.. It makes clear that there was no intent to change the common-law rule that allowed a payee to become a holder in due course. See Comment 2 to present Section 3-302 [30-3-302 prior to 1991 revision]. But there was no need to put subsection (2) in present Section 3-302 [30-3-302 prior to 1991 revision] because the split in authority under the N.I.L. was caused by the particular wording of N.I.L. Section 52(4). The troublesome language in that section is not repeated in present Article 3 [Title 30, chapter 3 prior to 1991 revision] nor is it repeated in proposed Article 3 [Title 30, chapter 3]. Present Section 3-302(2) [30-3-302(2) prior to 1991 revision] has not been repeated in proposed Section 3-302 [30-3-302] because it is surplusage. There is no intent to change the present law. The payee of an instrument can be a holder in due course. But present Section 3-302(2) [30-3-302(2) prior to 1991 revision] may be misread as suggesting that use of the holder-in-due-course doctrine by the payee of an instrument is the normal situation. It is not.

The primary importance of the concept of holder in due course is with respect to assertion of defenses or claims in recoupment (Section 3-305 [30-3-305]) and of claims to the instrument (Section 3-306 [30-3-306]). The holder-in-due-course doctrine assumes the following case as typical. Obligor issues a note or check to Obligee. Obligor is the maker of the note or drawer of the check. Obligee is the payee. Obligor has some defense to Obligor's obligation to pay the instrument. For example, Obligor issued the instrument for goods that Obligee promised to deliver. Obligee never delivered the goods. The failure of Obligee to deliver the goods is a defense. Section 3-303(b) [30-3-303(2)]. Although Obligor has a defense against Obligee, if the instrument is negotiated to Holder and the requirements of subsection (a) [subsection (1) of this section] are met, Holder may enforce the instrument against Obligor free of the defense. Section 3-305(b) [30-3-305(2)]. In the typical case the holder in due course is not the payee of the instrument. Rather, the holder in due course is an immediate or remote transferee of the payee. If Obligor in our example is the only obligor on the check or note, the holder-in-due-course doctrine is irrelevant in determining rights between Obligor and Obligee with respect to the instrument.

But in a small percentage of cases it is appropriate to allow the payee of an instrument to assert rights as a holder in due course. The cases are like those referred to in the quotation from Professor Britton referred to above, or other cases in which conduct of some third party is the basis of the defense of the issuer of the instrument. The following are examples:

Case #1. Buyer pays for goods bought from Seller by giving to Seller a cashier's check bought from Bank. Bank has a defense to payment of the check because Buyer bought the check from Bank with an insufficient funds check. If Bank issued the check in the name of Buyer as payee and Buyer indorsed it over to Seller, it is clear that Seller can be a holder in due course taking free of the defense if Seller had no notice of the defense. Seller is a transferee of the check. There is no good reason why Seller's position should be any different if Bank issued the check in the name of Seller as payee. When Buyer took delivery of the check from Bank, Buyer became the owner of the check even though Buyer was not the holder. Buyer was a remitter. Section 3-103(a)(11) [30-3-102(1)(k)]. At that point nobody was the holder. When Buyer delivered the check to Seller, ownership of the check was transferred to Seller who also became the holder. This is a negotiation. Section 3-201 [30-3-202]. The rights of Seller should not be affected by the fact that in one case the negotiation to Seller was by a holder and in the other case the negotiation was by a remitter. Moreover, it should be irrelevant whether Bank delivered the check to Buyer and Buyer delivered it to Seller or whether Bank delivered it directly to Seller. In either case Seller can be a holder in due course that takes free of Bank's defense.

Case #2. X, by fraudulent misrepresentations, induces Y to join X in a purchase of speculative securities. The purchase is to be financed by a bank loan for part of the price and the balance by cash contributed by X and Y in equal shares. Bank lends money to X and Y by deposit in a joint account of X and Y who sign a note payable to Bank for the amount of the loan. X then withdraws the money from the joint account and absconds. Bank acted in good faith and without notice of the fraud of X against Y. Bank is payee of the note executed by Y, but its right to enforce the note against Y should not be affected by the fact that Y was induced to execute the note by the fraud of X. Bank can be a holder in due course that takes free of the defense of Y. Case #2 is similar to Case #1. In each case the payee of the instrument has given value to the person committing the fraud in exchange for the obligation of the person against whom the fraud was committed. In each case the payee was not party to the fraud and had no notice of it.

Suppose in Case #2 that the note does not meet the requirements of Section 3-104(a)(1) [30-3-104(1)(a)] and thus is not a negotiable instrument and is not covered by Article 3 [Title 30, chapter 3] at all. In that case, Bank cannot be a holder in due course but the result should be the same. Bank's rights are determined by general principles of contract law. Restatement Second, Contracts § 164(2) governs the case. If Y is induced to enter into a contract with Bank by a fraudulent misrepresentation by X, the contract is voidable by Y unless Bank "in good faith and without reason to know of the misrepresentation either gives value or relies materially on the transaction." Comment e to § 164(2) states: "This is the same principle that protects an innocent person who purchases goods or commercial paper in good faith, without notice and for value from one who obtained them from the original owner by a misrepresentation. See Uniform Commercial Code 2-403(1) [30-2-403(1)], 3-305 [30-3-305]. In the cases that fall within [§ 164(2)], however, the innocent person deals directly with the recipient of the misrepresentation, which is made by one not a party to the contract."

The same result follows in Case #2 if Y had been induced to sign the note as an accommodation party (Section 3-419 [30-3-415]). If Bank is a holder in due course, the fraud of X cannot be asserted against Bank under Section 3-305(b) [30-3-305(2)]. But the result is the same without resort to holder-in-due-course doctrine. Y, as an accommodation party, is liable to Bank as maker of the note (Section 3-419(b) [30-3-415(2)]) but has rights against X as a surety or guarantor of X's obligation to pay the note and has a right of recourse against X if Y pays the note. Section 3-419(e) [30-3-415(5)]. Restatement, Security § 119 states that the surety (Y) cannot assert a defense against the creditor (Bank) based on the fraud of the principal (X) if the creditor "without knowledge of the fraud . . . extended credit to the principal on the security of the surety's promise . . .." The underlying principle of § 119 is the same as that of § 164(2) of Restatement Second, Contracts.

Case #3. Corporation draws a check payable to Bank. The check is given to an officer of Corporation who is instructed to deliver it to Bank in payment of a debt owed by Corporation to Bank. Instead, the officer, intending to defraud Corporation, delivers the check to Bank in payment of the officer's personal debt, or the check is delivered to Bank for deposit to the officer's personal account. If Bank obtains payment of the check, Bank has received funds of Corporation which have been used for the personal benefit of the officer. Corporation in this case will assert a claim to the proceeds of the check against Bank. If Bank was a holder in due course of the check it took the check free of Corporation's claim. Section 3-306 [30-3-306]. The issue in this case is whether Bank had notice of the claim when it took the check. If Bank knew that the officer was a fiduciary with respect to the check, the issue is governed by Section 3-307 [30-3-308].

Case #4. Employer, who owed money to X, signed a blank check and delivered it to Secretary with instructions to complete the check by typing in X's name and the amount owed to X. Secretary fraudulently completed the check by typing in the name of Y, a creditor to whom Secretary owed money. Secretary then delivered the check to Y in payment of Secretary's debt. Y obtained payment of the check. This case is similar to Case #3. Since Secretary was authorized to complete the check, Employer is bound by Secretary's act in making the check payable to Y. The drawee bank properly paid the check. Y received funds of Employer which were used for the personal benefit of Secretary. Employer asserts a claim to these funds against Y. If Y is a holder in due course, Y takes free of the claim. Whether Y is a holder in due course depends upon whether Y had notice of Employer's claim.

5. Subsection (c) [subsection (3) of this section] is based on present Section 3-302(3) [30-3-302(3) prior to 1991 revision]. Like present Section 3-302(3) [30-3-302(3) prior to 1991 revision] proposed subsection (c) [subsection (3) of this section] is intended to state existing case law. It covers a few situations in which the purchaser takes an instrument under unusual circumstances which indicate that the purchaser is merely a successor in interest to the prior holder and can acquire no better rights. But if the prior holder was a holder in due course, the purchaser obtains rights of a holder in due course. Subsection (c) [subsection (3) of this section] applies to a purchaser at an execution sale, a sale in bankruptcy or a sale by a state bank commissioner of the assets of an insolvent bank. It applies equally to an attaching creditor or any other person who acquires the instrument by legal process or to a representative, such as an executor, administrator, receiver or assignee for the benefit of creditors, who takes the instrument as part of an estate.

Subsection (c) [subsection (3) of this section] applies to bulk purchases lying outside of the ordinary course of business of the seller. It applies, for example, when a new partnership takes over for value all of the assets of an old one after a new member has entered the firm, or to a reorganized or consolidated corporation taking over in bulk the assets of a predecessor. It has particular application to the purchase by one bank of a substantial part of the paper held by another bank which is threatened with insolvency and seeking to liquidate its assets.

6. Subsection (d) and (e) [subsections (4) and (5) of this section] clarify two matters not specifically addressed by present Article 3 [Title 30, chapter 3]:

Case #5. Payee negotiates a $1,000 note to Holder who agrees to pay $900 for it. After paying $500, Holder learns that Payee defrauded Maker in the transaction giving rise to the note. Under subsection (e) [subsection (5) of this section] Holder may assert rights as a holder in due course to the extent of $555.55 ($500/$900 = .555 X $1,000 = $555.55). This formula rewards Holder with a ratable portion of the bargained for profit.

Case #6. Payee negotiates a note of Maker for $1,000 to Holder as security for payment of Payee's debt to Holder of $600. Maker has a defense which is good against Payee but of which Holder has no notice. Subsection (f) [subsection (6) of this section] governs Case #2. Holder may assert rights as a holder in due course only to the extent of $600. Payee does not get the benefit of the holder-in-due-course status of Holder. With respect to $400 of the note, Maker may assert any rights that Maker has against Payee. A different result follows if the payee of a note negotiated it to a person who took it as a holder in due course and that person pledged the note as security for a debt. Because the defense cannot be asserted against the pledgor, the pledgee can assert rights as a holder in due course for the full amount of the note for the benefit of both the pledgor and the pledgee.

7. There is a large body of statutory and case law restricting the use of the holder in due course doctrine in consumer transactions as well as some business transactions that raise similar issues. Subsection (h) [subsection (8) of this section] subordinates Article 3 [Title 30, chapter 3] to that law and any other similar law that may evolve in the future. Section 3-106(d) [30-3-105(4)] also relates to statutory or administrative law intended to restrict use of the holder-in-due-course doctrine. See Comment 3 to Section 3-106 [30-3-105].

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "(1) A holder in due course is a holder who takes the instrument:

(a) for value; and

(b) in good faith; and

(c) without notice that it is overdue or has been dishonored or of any defense against or claim to it on the part of any person.

(2) A payee may be a holder in due course.

(3) A holder does not become a holder in due course of an instrument:

(a) by purchase of it at judicial sale or by taking it under legal process; or

(b) by acquiring it in taking over an estate; or

(c) by purchasing it as part of a bulk transaction not in regular course of business of the transferor.

(4) A purchaser of a limited interest can be a holder in due course only to the extent of the interest purchased."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

DECISIONS UNDER U.C.C. AFTER 1991 REVISION

Superior Rights as Between Holder of Perfected Security Interest in Collateral and Purchaser of Collateral: Equipment owned by Gauvin and used to secure a promissory note with American Federal Savings and Loan Association (American) was sold to Madison Valley Properties, Inc. (Madison). Upon receipt of the proceeds, Gauvin's girlfriend contacted American for a payoff amount on the promissory note. Gauvin then took a cashier's check from the sale proceeds and converted it to another cashier's check at Valley Bank of Helena (Valley) made out to American for the payoff amount. The check was delivered to American, but later that same day, Valley informed American that the cashier's check had been purchased with stolen funds and was void. American returned the check to Valley, and as a result, the loan was not paid or the lien on the equipment released. American sued Gauvin to recover on the note and sued Madison to recover the equipment. Madison counterclaimed, seeking to quiet title. Summary judgment was granted Madison under the rationale that Madison had superior rights in the collateral equipment. Although American initially received the Valley check in good faith and without notice of the underlying theft, once it was advised of the theft, American could not go forward in good faith and without notice of an adverse claim and Valley's defenses. At the time that it received notice, American still had time and was able to reverse the administrative steps that it had taken to process the loan payment. Notice of the theft could not simply be ignored; therefore, American was required to suspend performance. If it had proceeded in the face of the notice, American could not have claimed holder-in-due-course status. The District Court erred by not first determining whether American was a holder in due course of the cashier's check. Under 30-3-301(1)(a) or (1)(c), American was not a holder in due course because American did not give value. Thus, the Supreme Court reversed the summary judgment award of superior rights in the collateral to Madison. Am. Fed. S&L Ass'n v. Madison Valley Properties, Inc., 1998 MT 93, 288 M 365, 958 P2d 57, 55 St. Rep. 366 (1998).

DECISIONS UNDER UNIFORM NEGOTIABLE INSTRUMENTS LAW

Notice of Payment Stopped: Where payee negotiated check to supplier and drawer stopped payment, payee's father, who purchased check stamped "payment stopped" from supplier for value with full knowledge that payment had been stopped on check, was not a holder in due course. Tesdahl v. Hiebert, 148 M 241, 419 P2d 298 (1966).

Altered Instrument: In an action by bank, which, at request of a payee who was known only by sight, had cashed a $5,000 pencil-written check, bearing indications of material alteration, the maker of which was a stranger, without first presenting check to drawee bank in ordinary course of business, evidence was insufficient to sustain judgment for plaintiff bank against maker as against defenses of alteration and bad faith of holder. Miles City Bank v. Askin, 119 M 581, 179 P2d 750, 171 ALR 790 (1947).

Illegal Consideration: A creditor who made illegal agreement with farmer should pay balance of debt notwithstanding creditor's execution of composition agreement in order to obtain Federal Land Bank loan, was not a "holder in due course" of note executed by farmer's son-in-law for amount due under the illegal agreement, and could not recover thereon. May v. Whitbeck, 111 M 568, 113 P2d 332 (1941).

Definition of Holder in Due Course:

Where plaintiffs in an action on a negotiable instrument by their uncontradicted evidence showed that they became the holders of it before it was overdue, and without notice that it had been dishonored, that they took it in good faith and for value, and that at the time it was negotiated to them they had no notice of any infirmity in the title of the person who negotiated it to them, their showing was sufficient to establish their status as holders in due course, and evidence to establish failure of consideration was inadmissible. Best v. Boyer, 98 M 40, 37 P2d 331 (1934).

A holder of a promissory note who bought it before maturity in good faith paying full value therefor without actual knowledge or notice that it was secured by a mortgage, or of the assignment of the note containing a provision that it was being transferred without recourse, was a holder in due course within the meaning of section 55-502, R.C.M. 1947 (now repealed). Wood v. Ferguson, 71 M 540, 230 P 592 (1924).

Overdue Note:

One who takes a promissory note by assignment after its maturity is not a holder in due course, and all defenses existing as against the original payee are available in his action to recover thereon. Alward v. Broadway Gold Min. Co., 94 M 45, 20 P2d 647 (1933).

A bank which accepted a note 4 years overdue did not become a holder in due course, but took only the title thereto which the assignor, its debtor, had, with the risk of all defects therein, as well as of the defenses to it or demands existing at the time against him with reference to it. NW. Improvement Co. v. Rhoades, 52 M 428, 158 P 832 (1916).

Discount Purchase: In the absence of evidence showing that plaintiff was not a holder in due course of the note sued upon, and mere fact that he purchased it at a 10% discount was not sufficient to raise an inference or suspicion that he bought a tainted instrument. Lister v. Donlan, 85 M 571, 281 P 348, 72 ALR 1 (1929).

Jury Question: While the question whether a holder of a negotiable instrument is a holder in due course is usually one of fact for the jury to decide, where the facts are shown and undisputed, and the transaction discloses nothing which would justify an inference of bad faith, it becomes one of law and it is the duty of the Trial Court to direct a verdict for plaintiff. Lister v. Donlan, 85 M 571, 281 P 348, 72 ALR 1 (1929).

Knowledge of Representative Capacity: In an action on a promissory note which had never been previously negotiated and was overdue when plaintiff acquired it by assignment, and who was therefore not a holder in due course, parol evidence was admissible to show that defendants with plaintiff's knowledge had endorsed the note with the understanding that each was doing so as representative of an association and not in his personal capacity. Anderson v. Border, 75 M 516, 244 P 494 (1926).

Burden of Proof:

To defeat the claim of ownership of coupon Liberty Bonds, negotiable in character, asserted by plaintiff in his action for their conversion, it was incumbent upon defendant bank to show that it was a holder in due course, under sections 55-502, 55-508, and 55-509, R.C.M. 1947 (now repealed). Grosfield v. First Nat'l Bank of Miles City, 73 M 219, 236 P 250 (1925).

Under former section 55-509, R.C.M. 1947 (now repealed), where, after plaintiff endorsee had made out a prima facie case, defendant (drawer) produced evidence tending fairly to prove that the payee had obtained the check through fraud, the burden shifted to plaintiff to prove every fact necessary to show that he was a holder in due course, among them that he took it in good faith and for value, failing in which he was not entitled to recover. Matteson v. Trask, 63 M 160, 206 P 428 (1922).

Knowledge Required to Defeat Holder: To defeat the claim of plaintiff in an action on a promissory note that he was a holder in due course, on the ground that when he acquired it he had notice of a defect of title in the transferor consisting of a breach of faith in the latter as against the maker, it must, under section 55-506, R.C.M. 1947 (now repealed), be made to appear that he had actual knowledge of the infirmity or knowledge of such facts that his taking it under the circumstances amounted to bad faith. Olsen v. Zappone, 83 M 573, 273 P 635 (1924).

Negotiation by Assignment: One taking a note by assignment is not a holder in due course. Price v. Skylstead, 69 M 453, 222 P 1059 (1924).

Payee Prima Facie Holder in Due Course: The payee of a negotiable promissory note, in possession of it, is a prima facie holder in due course, within the meaning of the Uniform Negotiable Instruments Act, negotiation by endorsement and delivery not being necessary to constitute one a holder in due course. Merchants' Nat'l Bank of Billings v. Smith, 59 M 280, 196 P 523, 15 ALR 430 (1921).

Necessity of Endorsement: Where a negotiable instrument is payable to order an endorsement is essential to holding in due course. First Nat'l Bank v. Grow, 57 M 376, 188 P 907 (1920).

Breach of Warranty as Defense: Knowledge of a warranty that an automobile would meet certain requirements as to service did not defeat a bank's claim as a holder in due course of promissory notes taken in payment of the machine before maturity, and without being aware of a breach of such warranty. Baker St. Bank v. Grant, 54 M 7, 166 P 27 (1917).

Reference to Other Instrument: The assignee of a note and mortgage together is not a bona fide holder. Buhler v. Loftus, 53 M 546, 165 P 601 (1917).

Notice of Dishonor: Where the payee in a demand note for $500 assigned it to plaintiff about 20 months after its date, with endorsements thereon showing partial payments amounting to $450 of the principal sum due, and where it appeared that plaintiff, through one of its employees, had notice that there was dispute between the maker and the payee as to whether any balance remained unpaid, plaintiff was not a holder in due course, within the meaning of section 55-502, R.C.M. 1947 (now repealed), but took the paper with notice of its dishonor. Brophy Groc. Co. v. Wilson, 45 M 489, 124 P 510 (1912).

Part Payment of Demand Note: Part payment of the principal of a demand note is evidence of its dishonor. Brophy Groc. Co. v. Wilson, 45 M 489, 124 P 510 (1912).

30-3-303. Value and consideration.

Official Comment

Source: Section 3-303, U.C.C.

Prior Uniform Statutory Provision: Sections 25, 26, 27 and 54, Uniform Negotiable Instruments Law.

Official Comment to 1991 Amendment:

1. Subsection (a) [subsection (1) of this section] is a restatement of present Section 3-303 [30-3-303 prior to 1991 revision] and subsection (b) [subsection (2) of this section] replaces present Section 3-408 [30-3-408 prior to 1991 revision]. The distinction between value and consideration in Article 3 [Title 30, chapter 3] is a very fine one. Whether an instrument is taken for value is relevant to the issue of whether a holder is a holder in due course. If an instrument is not issued for consideration the drawer or maker has a defense to the obligation to pay the instrument. Consideration is defined in subsection (b) [subsection (2) of this section] as "any consideration sufficient to support a simple contract." The definition of value in Section 1-201(44) [30-1-201(44)], which doesn't apply to Article 3 [Title 30, chapter 3], includes "any consideration sufficient to support a simple contract." Thus, outside Article 3 [Title 30, chapter 3], anything that is consideration is also value. A different rule applies in Article 3 [Title 30, chapter 3]. Subsection (b) of Section 3-303 [30-3-303(2)] states that if an instrument is issued for value it is also issued for consideration.

Case #1. X owes Y $1,000. The debt is not represented by a note. Later X issues a note to Y for the debt. Under subsection (a)(3) [subsection (1)(c) of this section] X's note is issued for value. Under subsection (b) [subsection (2) of this section] the note is also issued for consideration whether or not, under contract law, X is deemed to have given consideration for the note.

Case #2. X issues a check to Y in consideration of Y's promise to perform services in the future. Although the executory promise is consideration for issuance of the check it is value only to the extent the promise is performed. Subsection (a)(1) [subsection (1)(a) of this section].

Case #3. X issues a note to Y in consideration of Y's promise to perform services. If at the due date of the note Y's performance is not yet due, Y may enforce the note because it was issued for consideration. But if at the due date of the note, Y's performance is due and has not been performed, X has a defense. Subsection (b) [subsection (2) of this section].

2. The policy basis for subsection (a) [subsection (1) of this section] is that the holder that gives an executory promise of performance will not suffer an out-of-pocket loss to the extent the executory promise is unperformed at the time the holder learns of the defense on the instrument. Suppose Payee negotiates a note of Maker to Holder in exchange for Holder's promise to perform services in the future. Before Holder's performance is due, Maker dishonors the note because of a defense good against Payee. Dishonor of the note excuses Holder's performance. The note was taken for Payee's obligation to pay for the services. That obligation was suspended when the note was taken, but it revives when the note is dishonored. Section 3-310(b) [30-3-310(2)]. Since Payee's obligation to pay for the services is unsatisfied, Holder need not perform. Thus, Holder is protected from an out-of-pocket loss even if the note is not enforceable. There is not the same necessity for giving Holder the status of holder in due course as in the case in which an instrument has been taken for property or performed services.

3. Subsection (a)(2) [subsection (1)(b) of this section] equates value with the obtaining of a security interest or a nonjudicial lien in the instrument. The term "security interest" covers Article 9 [Title 30, chapter 9A] cases in which an instrument is taken as collateral as well as bank collection cases in which a bank acquires a security interest under Section 4-208 [30-4-215]. The acquisition of a common-law or statutory banker's lien is also value under subsection (a)(2) [subsection (1)(b) of this section]. An attaching creditor or other person who acquires a lien by judicial proceedings does not give value for the purposes of subsection (a)(2) [subsection (1)(b) of this section] and is not a holder in due course. Section 3-302(c) [30-3-302(3)].

4. Subsection (a)(3) [subsection (1)(c) of this section] follows present Section 3-303(b) [30-3-303(b) prior to 1991 revision] which adapts the generally accepted rule that the holder takes for value if the instrument is taken in payment of or as security for an antecedent debt, even though there is no extension of time or other concession, and whether or not the debt is due. Subsection (a)(3) [subsection (1)(c) of this section] extends the same rule to any claim against any person; there is no requirement that the claim arise out of contract. In particular the provision is intended to apply to an instrument given in payment of or as security for the debt of a third person, even though no concession is made in return.

5. Subsection (a)(4) and (5) [subsections (1)(d) and (1)(e) of this section] restate present Section 3-303(c) [30-3-303(c) prior to 1991 revision]. They state generally recognized exceptions to the rule that an executory promise is not value. A negotiable instrument is value because it carries the possibility of negotiation to a holder in due course, after which the party who gives it is obliged to pay. The same reasoning applies to any irrevocable commitment to a third person, such as a letter of credit issued when an instrument is taken.

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "Taking for value. A holder takes the instrument for value:

(a) to the extent that the agreed consideration has been performed or that he acquires a security interest in or a lien on the instrument otherwise than by legal process; or

(b) when he takes the instrument in payment of or as security for an antecedent claim against any person whether or not the claim is due; or

(c) when he gives a negotiable instrument for it or makes an irrevocable commitment to a third person."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

DECISIONS UNDER UNIFORM NEGOTIABLE INSTRUMENTS LAW

Taking as Security: The transferee of a negotiable instrument as collateral security for a preexisting debt is a taker for value. First Nat'l Bank of Lewistown v. Wilson, 57 M 384, 188 P 371 (1920).

30-3-304. Overdue instrument.

Official Comment

Source: Section 3-304, U.C.C.

Prior Uniform Statutory Provision: Sections 45, 52, 53, 55 and 56, Uniform Negotiable Instruments Law.

Official Comment to 1991 Amendment:

1. To be a holder in due course, one must take without notice that an instrument is overdue. Section 3-302(a)(2)(iii) [30-3-302(1)(b)(iii)]. Proposed Section 3-304 [30-3-304] replaces subsection (3) of present Section 3-304 [30-3-304(3) prior to 1991 revision]. For the sake of clarity it treats demand and time instruments separately. Subsection (a) [subsection (1) of this section] applies to demand instruments. A check becomes stale after 90 days. Under present Section 3-304(3)(c) [30-3-304(3)(c) prior to 1991 revision], a holder that takes a demand note has notice that it is overdue if it is taken "more than a reasonable length of time after its issue." In substitution for this test, subsection (a)(3) [subsection (1)(c) of this section] requires the trier of fact to look at both the circumstances of the particular case and the nature of the instrument and trade usage. Whether a demand note is stale may vary a great deal depending on the facts of the particular case.

2. Subsections (b) and (c) [subsections (2) and (3) of this section] cover time instruments. They follow the distinction made in the present law between defaults in payment of principal and interest. In subsection (b) [subsection (2) of this section] installment instruments and single payment instruments are treated separately. If an installment is late, the instrument is overdue until the default is cured.

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "Notice to purchaser. (1) The purchaser has notice of a claim or defense if:

(a) the instrument is so incomplete, bears such visible evidence of forgery or alteration, or is otherwise so irregular as to call into question its validity, terms or ownership or to create an ambiguity as to the party to pay; or

(b) the purchaser has notice that the obligation of any party is voidable in whole or in part, or that all parties have been discharged.

(2) The purchaser has notice of a claim against the instrument when he has knowledge that a fiduciary has negotiated the instrument in payment of or as security for his own debt or in any transaction for his own benefit or otherwise in breach of duty.

(3) The purchaser has notice that an instrument is overdue if he has reason to know:

(a) that any part of the principal amount is overdue or that there is an uncured default in payment of another instrument of the same series; or

(b) that acceleration of the instrument has been made; or

(c) that he is taking a demand instrument after demand has been made or more than a reasonable length of time after its issue. A reasonable time for a check drawn and payable within the states and territories of the United States and the District of Columbia is presumed to be 30 days.

(4) Knowledge of the following facts does not of itself give the purchaser notice of a defense or claim:

(a) that the instrument is antedated or postdated;

(b) that it was issued or negotiated in return for an executory promise or accompanied by a separate agreement, unless the purchaser has notice that a defense or claim has arisen from the terms thereof;

(c) that any party has signed for accommodation;

(d) that an incomplete instrument has been completed, unless the purchaser has notice of any improper completion;

(e) that any person negotiating the instrument is or was a fiduciary;

(f) that there has been default in payment of interest on the instrument or in payment of any other instrument, except one of the same series.

(5) The filing or recording of a document does not of itself constitute notice within the provisions of this chapter to a person who would otherwise be a holder in due course.

(6) To be effective notice must be received at such time and in such manner as to give a reasonable opportunity to act on it."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

DECISIONS UNDER UNIFORM NEGOTIABLE INSTRUMENTS LAW

Failure to Make Inquiry: In action by bank which cashed check against drawer, evidence supported determination that circumstances surrounding presentment of check were sufficient to have caused bank to become suspicious of apparent alterations and infirmities, and bank's failure to take notice thereof constituted bad faith so as to overcome legal presumption that it was a holder in due course. Miles City Bank v. Askin, 127 M 86, 257 P2d 896 (1953).

Amount Paid: Purchase of note at 10% discount is not sufficient to raise an inference of bad faith on the part of the purchaser. Lister v. Donlan, 85 M 571, 281 P 348, 72 ALR 1 (1929).

Facts Known by Holder: To defeat the claim of plaintiff in an action on a promissory note that he was a holder in due course, on the ground that when he acquired it he had notice of a defect of title in the transferor consisting of a breach of faith in the latter as against the maker, it must, under section 55-506, R.C.M. 1947 (since repealed), be made to appear that he had actual knowledge of the infirmity or knowledge of such facts that his taking it under the circumstances amounted to bad faith. Olsen v. Zappone, 83 M 573, 273 P 635 (1929).

Knowledge as Imputable to Principal: Knowledge of vice-president of loaning bank, imputed to him as president of the borrowing bank, is not chargeable to the loaning bank, being acquired outside his duties to the bank of which he is not an active officer. Grosfield v. First Nat'l Bank of Miles City, 73 M 219, 236 P 250 (1925).

Trouble with Prior Notes: Notice of dishonor of another note given in the same transaction prevents a purchase in good faith. First Nat'l Bank of Lewistown v. Wilson, 57 M 384, 188 P 371 (1920).

30-3-305. Defenses and claims in recoupment.

Official Comment

Source: Section 3-305, U.C.C.

Prior Uniform Statutory Provision: Sections 15, 16 and 57, Uniform Negotiable Instruments Law.

Official Comment to 1991 Amendment:

1. Subsection (a) [subsection (1) of this section] states the defenses to the obligation of a party to pay the instrument. Subsection (a)(1) [subsection (1)(a) of this section] states the "real defenses" that may be asserted against any person entitled to enforce the instrument.

Subsection (a)(1)(i) [subsection (1)(a)(i) of this section] allows assertion of the defense of infancy against a holder in due course, even though the effect of the defense is to render the instrument voidable but not void. The policy is one of protection of the infant even at the expense of occasional loss to an innocent purchaser. No attempt is made to state when infancy is available as a defense or the conditions under which it may be asserted. In some jurisdictions it is held that an infant cannot rescind the transaction or set up the defense unless the holder is restored to the position held before the instrument was taken which, in the case of a holder in due course, is normally impossible. In other states an infant who has misrepresented age may be estopped to assert infancy. Such questions are left to other law, as an integral part of the policy of each state as to the protection of infants.

Subsection (a)(1)(ii) [subsection (1)(a)(ii) of this section] covers mental incompetence, guardianship, ultra vires acts or lack of corporate capacity to do business, or any other incapacity apart from infancy. Such incapacity is largely statutory. Its existence and effect is left to the law of each state. If under the state law the effect is to render the obligation of the instrument entirely null and void, the defense may be asserted against a holder in due course. If the effect is merely to render the obligation voidable at the election of the obligor, the defense is cut off.

Duress, which is also covered by subsection (a)[(1)](ii) [subsection (1)(a)(ii) of this section], is a matter of degree. An instrument signed at the point of a gun is void, even in the hands of a holder in due course. One signed under threat to prosecute the son of the maker for theft may be merely voidable, so that the defense is cut off. Illegality is most frequently a matter of gambling or usury, but may arise in many other forms under a great variety of statutes. The statutes differ greatly in their provisions and the interpretations given them. They are primarily a matter of local concern and local policy. All such matters are therefore left to the local law. If under that law the effect of the duress or the illegality is to make the obligation entirely null and void, the defense may be asserted against a holder in due course. Otherwise it is cut off.

Subsection (a)(1)(iii) [subsection (1)(a)(iii) of this section] refers to "real" or "essential" fraud, sometimes called fraud in the essence or fraud in the factum, as effective against a holder in due course. The common illustration is that of the maker who is tricked into signing a note in the belief that it is merely a receipt or some other document. The theory of the defense is that the signature on the instrument is ineffective because the signer did not intend to sign such an instrument at all. Under this provision the defense extends to an instrument signed with knowledge that it is a negotiable instrument, but without knowledge of its essential terms.

The test of the defense is that of excusable ignorance of the contents of the writing signed. The party must not only have been in ignorance, but must also have had no reasonable opportunity to obtain knowledge. In determining what is a reasonable opportunity all relevant factors are to be taken into account, including the intelligence, education, business experience, and ability to read or understand English of the signer. Also relevant is the nature of the representations that were made, whether the signer had good reason to rely on the representations or to have confidence in the person making them, the presence or absence of any third person who might read or explain the instrument to the signer, or any other possibility of obtaining independent information, and the apparent necessity, or lack of it, for acting without delay. Unless the misrepresentation meets this test, the defense is cut off by a holder in due course.

Subsection (a)(1)(iv) [subsection (1)(a)(iv) of this section] states specifically that the defense of discharge in bankruptcy or other insolvency proceedings is not cut off when the instrument is purchased by a holder in due course. Subsection (2)(e) of present Section 3-305 [30-3-305(2)(e) prior to 1991 revision] is omitted. The substance of that provision is stated in Section 3-601(b) [30-3-601(2)].

As is the case under present Section 3-305 [30-3-305 prior to 1991 revision], forgery and alteration are not listed as real defenses because they are not technically defenses. Forgery of the signature of a person as maker or drawer of an instrument does not give rise to any obligation of that person. Section 3-401 [30-3-401]. Thus, there is no obligation to which a defense could relate. Alteration is also not treated as a defense. Rather, the obligations of various parties to an instrument are stated by taking into account the possibility of alteration. See, for example, Section 3-412 [30-3-413] and Section 3-413 [30-3-422]. Rights with respect to altered instruments are separately stated in Section 3-407 [30-3-407].

2. Subsection (a)(2) [subsection (1)(b) of this section] states other defenses that, pursuant to subsection (b) [subsection (2) of this section], are cut off by a holder in due course. These defenses comprise those specifically stated in Article 3 [Title 30, chapter 3] and those based on common law contract principles. Article 3 [Title 30, chapter 3] defenses are nonissuance of the instrument, conditional issuance, and issuance for a special purpose (Section 3-105(b) [30-3-125(2)]); failure of the owner to countersign a traveler's check (Section 3-106(c) [30-3-105(3)]); modification of the obligation by a separate agreement (Section 3-117 [30-3-119]); payment that violates a restrictive indorsement (Section 3-206(f) [30-3-205(6)]); instruments issued without consideration or for which promised performance has not been given (Section 3-303(b) [30-3-303(2)]), and breach of warranty when a draft is accepted (Section 3-417(b) [30-3-424(2)]). The most prevalent common law defenses are fraud, misrepresentation or mistake in the issuance of the instrument. In most cases the holder in due course will be an immediate or remote transferee of the payee of the instrument. In most cases the holder-in-due-course doctrine is irrelevant if defenses are being asserted against the payee of the instrument, but in a small number of cases the payee of the instrument may be a holder in due course. Those cases are discussed in Comment 4 to Section 3-302 [30-3-302].

Assume Buyer issues a note to Seller in payment of the price of goods that Seller fraudulently promises to deliver but which are never delivered. Seller negotiates the note to Holder who has no notice of the fraud. If Holder is a holder in due course, Holder is not subject to Buyer's defense of fraud. But in some cases an original party to the instrument is a holder in due course. For example, Buyer fraudulently induces Bank to issue a cashier's check to the order of Seller. The check is delivered by Bank to Seller, who has no notice of the fraud. Seller can be a holder in due course and can take the check free of Bank's defense of fraud. This case is discussed in Comment 4 to Section 3-302 [30-3-302]. Present Section 3-305 [30-3-305 prior to 1991 revision] states that a holder in due course takes free of defenses of "any party to the instrument with whom the holder has not dealt." The meaning of this language was not at all clear and if read literally may produce the wrong result. In the hypothetical case, it could be argued that Seller "dealt" with Bank because Bank delivered the check to Seller. But it is clear that Seller should take free of Bank's defense against Buyer regardless of whether Seller took delivery of the check from Buyer or from Bank. The quoted language is not included in proposed Section 3-305 [30-3-305]. It is not necessary. If Buyer issues an instrument to Seller and Buyer has a defense against Seller, that defense can obviously be asserted. Buyer and Seller are the only people involved. The holder-in-due-course doctrine has no relevance. The doctrine applies only to cases in which more than two parties are involved. Its essence is that the holder in due course does not have to suffer the consequences of a defense of the obligor on the instrument that arose from an occurrence with a third party.

3. Subsection (a)(3) [subsection (1)(c) of this section] is concerned with claims in recoupment which can be illustrated by the following example. Buyer issues a note to the order of Seller in exchange for a promise of Seller to deliver specified equipment. If Seller fails to deliver the equipment, Buyer has a defense to the note because the performance that was the consideration for the note was not performed. Section 3-303(b) [30-3-303(2)]. This defense is included in Section 3-305(a)(2) [30-3-305(1)(b)]. That defense can always be asserted against Seller. This result is the same as that reached under present Section 3-408 [30-3-408, now repealed].

But suppose Seller delivered the promised equipment and it was accepted by Buyer. The equipment, however, was defective and Buyer incurred expenses with respect to its repair. In this case, Buyer does not have a defense under Section 3-303(b) [30-3-303(2)]. Seller delivered the promised equipment which was accepted. Under Article 2 [Title 30, chapter 2] Buyer is obliged to pay the price of the equipment which is represented by the note. But Buyer may have a claim against Seller for breach of warranty. If Buyer has a warranty claim, the claim may be asserted against Seller as a counterclaim or as a claim in recoupment to reduce the amount owing on the note. It is not relevant whether Seller is or is not a holder in due course of the note or whether Seller knew or had notice that Buyer had the warranty claim. It is obvious that holder-in-due-course doctrine cannot be used to allow Seller to cut off a warranty claim that Buyer has against Seller. Subsection (b) [subsection (2) of this section] specifically covers this point by stating that a holder in due course is not subject to a "claim in recoupment . . . against a person other than the holder."

Suppose Seller negotiates the note to Holder. If Holder had notice of Buyer's warranty claim at the time the note was negotiated to Holder, Holder is not a holder in due course (Section 3-302(a)(2) [30-3-302(1)(b)]) and Buyer may assert the claim against Holder (Section 3-305(a)(3) [30-3-305(1)(c)]) but only as a claim in recoupment, i.e. to reduce the amount owed on the note. If the warranty claim is $1,000 and the unpaid note is $10,000, Buyer owes $9,000 to Holder. If the warranty claim is more than the unpaid amount of the note, Buyer owes nothing to Holder, but Buyer cannot recover the unpaid amount of the warranty claim from Holder. If Buyer had already partially paid the note, Buyer is not entitled to recover the amounts paid. The claim can be used only as an offset to amounts owing on the note. If Holder had no notice of Buyer's claim and otherwise qualifies as a holder in due course, Buyer may not assert the claim against Holder. Section 3-305(b) [30-3-305(2)].

The result under proposed Section 3-305 [30-3-305] is consistent with the result reached under present Article 3 [Title 30, chapter 3, prior to 1991 revision], but the rules for reaching the result are stated differently. Under present Article 3 [Title 30, chapter 3, prior to 1991 revision] Buyer could assert rights against Holder only if Holder was not a holder in due course, and Holder's status depends upon whether Holder had notice of a defense by Buyer. Courts have held that Holder has that notice if Holder has notice of Buyer's warranty claim. The rationale is that the case is one of "failure of consideration." This rationale does not distinguish between cases in which the seller fails to perform and those in which the buyer accepts the performance of seller but makes a claim against the seller because the performance is faulty. The term "failure of consideration" is subject to varying interpretations and is not used in proposed Article 3 [Title 30, chapter 3]. The use of the term "claims in recoupment" in Section 3-305(a)(3) [30-3-305(1)(c)] is a more precise statement of the nature of Buyer's right against Holder. The use of the term does not change the law because the treatment of a defense under subsection (a)(2) [subsection (1)(b) of this section] and a claim in recoupment under subsection (a)(3) [subsection (1)(c) of this section] is essentially the same.

Under present Article 3 [Title 30, chapter 3, prior to 1991 revision], case law is divided on the issue of the extent to which an obligor on a note can assert against a transferee who is not a holder in due course a debt or other claim that the obligor has against the original payee of the instrument. Some courts limit claims to those that arose in the transaction that gave rise to the note. This is the approach taken in proposed Section 3-305(a)(3) [30-3-305(1)(c)]. Other courts allowed the obligor on the note to use any debt or other claim, no matter how unrelated to the note, to offset the amount owed on the note. Under current judicial authority and non-UCC statutory law, there will be many cases in which a transferee of a note arising from a sale transaction will not qualify as a holder in due course. For example, applicable law may require the use of a note to which there cannot be a holder in due course. See Section 3-106(d) [30-3-105(4)] and Comment 3 to Section 3-106 [30-3-105]. It is reasonable to provide that the buyer should not be denied the right to assert claims arising out of the sale transaction. Subsection (a)(3) [subsection (1)(c) of this section] is based on the belief that it is not reasonable to require the transferee to bear the risk that wholly unrelated claims may also be asserted.

4. Subsection (c) [subsection (3) of this section] concerns claims and defenses of a person other than the obligor on the instrument. It follows subsection (4) of present Section 3-306 [30-3-306(4) prior to 1991 revision]. It applies principally to cases in which an obligation is paid with the instrument of a third person. For example, Buyer buys goods from Seller and negotiates to Seller a cashier's check issued by Bank in payment of the price. Section 3-201(a) [30-3-202(1)]. Shortly after delivering the check to Seller, Buyer learns that Seller had defrauded Buyer in the sale transaction. Seller may enforce the check against Bank even though Seller is not a holder in due course. Bank has no defense to its obligation to pay the check and it may not assert defenses, claims in recoupment, or claims to the instrument of Buyer, unless there is an exception stated in subsection (c) [subsection (3) of this section]. Buyer may have a claim to the instrument under Section 3-306 [30-3-306] based on a right to rescind the negotiation to Seller because of Seller's fraud. Section 3-202(b) [30-3-209(2)] and Comment to Section 3-201 [30-3-202]. Bank cannot assert that claim unless Buyer is joined in the action in which Seller is trying to enforce payment of the check. In that case Bank may pay the amount of the check into court and the court will decide whether that amount belongs to Buyer or Seller. The last sentence of subsection (c) [subsection (3) of this section] allows the issuer of an instrument such as a cashier's check to refuse payment in the rare case in which the issuer can prove that the instrument is a stolen instrument and the person seeking enforcement does not have rights of a holder in due course.

5. Subsection (d) [subsection (4) of this section] applies to instruments signed for accommodation (Section 3-419 [30-3-415]) and this subsection equates the obligation of the accommodation party to that of the accommodated party. The accommodation party can assert whatever defense or claim the accommodated party had against the person enforcing the instrument. The only exceptions are discharge in bankruptcy, infancy and lack of capacity. The same rule does not apply to an indorsement by a holder of the instrument in negotiating the instrument. The indorser, as transferor, makes a warranty to the indorsee, as transferee, that no defense or claim in recoupment is good against the indorser. Section 3-416(a)(4) [30-3-417(1)(d)]. Thus, if the indorsee sues the indorser because of dishonor of the instrument, the indorser may not assert the defense or claim in recoupment of the maker or drawer against the indorsee.

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "Rights of a holder in due course. To the extent that a holder is a holder in due course he takes the instrument free from:

(1) all claims to it on the part of any person; and

(2) all defenses of any party to the instrument with whom the holder has not dealt except:

(a) infancy, to the extent that it is a defense to a simple contract; and

(b) such other incapacity, or duress, or illegality of the transaction, as renders the obligation of the party a nullity; and

(c) such misrepresentation as has induced the party to sign the instrument with neither knowledge nor reasonable opportunity to obtain knowledge of its character or its essential terms; and

(d) discharge in insolvency proceedings; and

(e) any other discharge of which the holder has notice when he takes the instrument."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

DECISIONS UNDER U.C.C. AFTER 1991 REVISION

Superior Rights as Between Holder of Perfected Security Interest in Collateral and Purchaser of Collateral: Equipment owned by Gauvin and used to secure a promissory note with American Federal Savings and Loan Association (American) was sold to Madison Valley Properties, Inc. (Madison). Upon receipt of the proceeds, Gauvin's girlfriend contacted American for a payoff amount on the promissory note. Gauvin then took a cashier's check from the sale proceeds and converted it to another cashier's check at Valley Bank of Helena (Valley) made out to American for the payoff amount. The check was delivered to American, but later that same day, Valley informed American that the cashier's check had been purchased with stolen funds and was void. American returned the check to Valley, and as a result, the loan was not paid or the lien on the equipment released. American sued Gauvin to recover on the note and sued Madison to recover the equipment. Madison counterclaimed, seeking to quiet title. Summary judgment was granted Madison under the rationale that Madison had superior rights in the collateral equipment. Although American initially received the Valley check in good faith and without notice of the underlying theft, once it was advised of the theft, American could not go forward in good faith and without notice of an adverse claim and Valley's defenses. At the time that it received notice, American still had time and was able to reverse the administrative steps that it had taken to process the loan payment. Notice of the theft could not simply be ignored; therefore, American was required to suspend performance. If it had proceeded in the face of the notice, American could not have claimed holder-in-due-course status. The District Court erred by not first determining whether American was a holder in due course of the cashier's check. Under 30-3-301(1)(a) or (1)(c), American was not a holder in due course because American did not give value. Thus, the Supreme Court reversed the summary judgment award of superior rights in the collateral to Madison. Am. Fed. S&L Ass'n v. Madison Valley Properties, Inc., 1998 MT 93, 288 M 365, 958 P2d 57, 55 St. Rep. 366 (1998).

DECISIONS UNDER UNIFORM NEGOTIABLE INSTRUMENTS LAW

Failure of Consideration: Failure of consideration is not available as against a bona fide purchaser. Best v. Boyer, 98 M 40, 37 P2d 331 (1934).

Want or Failure of Consideration: Want or failure of consideration for a negotiable promissory note constitutes no defense as against a holder in due course under this section. Lister v. Donlan, 85 M 571, 281 P 348, 72 ALR 1 (1929).

Extrinsic Evidence: Extrinsic evidence to vary the terms of a note is inadmissible when it is in the hands of a holder in due course. Olsen v. Zappone, 83 M 573, 273 P 635 (1929).

Larceny: That a negotiable instrument (Liberty Bond) has been stolen and negotiated by the thief is no defense against a bona fide purchaser. Grosfield v. First Nat'l Bank of Miles City, 73 M 219, 236 P 250 (1925).

Delivery Not Shown: Under section 55-216, R.C.M. 1947 (now repealed), delivery of a promissory note, in order to be effectual, must be made by or under the authority of the maker of the instrument, and therefore where no such delivery is shown the payee named therein cannot recover on it. Baroch v. Greater Mont. Oil Co., 70 M 93, 225 P 800 (1924).

Collateral Agreement: An independent collateral agreement between the parties to a note limiting liability thereon cannot be set up against a subsequent holder in due course. Wood v. Ferguson, 71 M 540, 230 P 592 (1924).

Admissibility of Note in Evidence: In an action on a promissory note, its production by plaintiff raised a presumption of a valid and intentional delivery of it to the payee by the maker, and it was properly admitted as against the objection that plaintiff was not the owner or holder thereof. Ely, Salyards & Co. v. Farmers' Elev. Co., 69 M 265, 221 P 522 (1923).

Defenses Available Against Holder Not in Due Course: The Uniform Negotiable Instruments Act deals with negotiable instruments only so long as they are in the hands of holders in due course; if in other hands, they are subject to the same defenses as if nonnegotiable. Merchants' Nat'l Bank of Billings v. Smith, 59 M 280, 196 P 523, 15 ALR 430 (1921).

30-3-306. Claims to an instrument.

Official Comment

Source: Section 3-306, U.C.C.

Prior Uniform Statutory Provision: Sections 16, 28, 58 and 59, Uniform Negotiable Instruments Law.

Official Comment to 1991 Amendment:

This section expands on the reference to "claims to" the instrument mentioned in present Sections 3-305 [30-3-305 prior to 1991 revision] and 3-306 [30-3-306 prior to 1991 revision]. Claims covered by the section include not only claims to ownership but also any other claim of a property or possessory right. It includes the claim to a lien or the claim of a person in rightful possession of an instrument who was wrongfully deprived of possession. Also included is a claim based on Section 3-202(b) [30-3-209(2)] for rescission of a negotiation of the instrument by the claimant. Claims to an instrument under Section 3-306 [30-3-306] are different from claims in recoupment referred to in Section 3-305(a)(3) [30-3-305(1)(c)].

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "Rights of one not holder in due course. Unless he has the rights of a holder in due course any person takes the instrument subject to:

(a) all valid claims to it on the part of any person; and

(b) all defenses of any party which would be available in an action on a simple contract; and

(c) the defenses of want or failure of consideration, nonperformance of any condition precedent, nondelivery, or delivery for a special purpose (30-3-408); and

(d) the defense that he or a person through whom he holds the instrument acquired it by theft, or that payment or satisfaction to such holder would be inconsistent with the terms of a restrictive endorsement. The claim of any third person to the instrument is not otherwise available as a defense to any party liable thereon unless the third person himself defends the action for such party."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

DECISIONS UNDER U.C.C. AFTER 1991 REVISION

Superior Rights as Between Holder of Perfected Security Interest in Collateral and Purchaser of Collateral: Equipment owned by Gauvin and used to secure a promissory note with American Federal Savings and Loan Association (American) was sold to Madison Valley Properties, Inc. (Madison). Upon receipt of the proceeds, Gauvin's girlfriend contacted American for a payoff amount on the promissory note. Gauvin then took a cashier's check from the sale proceeds and converted it to another cashier's check at Valley Bank of Helena (Valley) made out to American for the payoff amount. The check was delivered to American, but later that same day, Valley informed American that the cashier's check had been purchased with stolen funds and was void. American returned the check to Valley, and as a result, the loan was not paid or the lien on the equipment released. American sued Gauvin to recover on the note and sued Madison to recover the equipment. Madison counterclaimed, seeking to quiet title. Summary judgment was granted Madison under the rationale that Madison had superior rights in the collateral equipment. Although American initially received the Valley check in good faith and without notice of the underlying theft, once it was advised of the theft, American could not go forward in good faith and without notice of an adverse claim and Valley's defenses. At the time that it received notice, American still had time and was able to reverse the administrative steps that it had taken to process the loan payment. Notice of the theft could not simply be ignored; therefore, American was required to suspend performance. If it had proceeded in the face of the notice, American could not have claimed holder-in-due-course status. The District Court erred by not first determining whether American was a holder in due course of the cashier's check. Under 30-3-301(1)(a) or (1)(c), American was not a holder in due course because American did not give value. Thus, the Supreme Court reversed the summary judgment award of superior rights in the collateral to Madison. Am. Fed. S&L Ass'n v. Madison Valley Properties, Inc., 1998 MT 93, 288 M 365, 958 P2d 57, 55 St. Rep. 366 (1998).

DECISIONS UNDER U.C.C. PRIOR TO 1991 REVISION

Parol Evidence Inadmissible to Show Sham or Fraud: Plaintiff and defendant were in the business of developing oil and gas property. Defendant executed a promissory note in favor of plaintiff and gave plaintiff a "letter agreement" supplementing and clarifying the note. In plaintiff's action on the note, defendant attempted to introduce evidence of a contrary oral agreement that the note was a sham intended to induce third parties to give plaintiff investment funds and that it was never intended that the note be paid. The parol evidence rule prevented introduction of the evidence. In addition, defendant was not entitled to relief under the rule that delivery of an instrument for a special purpose is a defense against one not a holder of the instrument in due course. The sham claim in this case does not constitute a special purpose. Perez-Lizano v. Ayers, 215 M 95, 695 P2d 467, 42 St. Rep. 208 (1985).

Lack of Consideration or Setoff: There was no issue of material fact precluding summary judgment, either of lack of consideration or of setoff, because the express language of the note sued on stated that consideration existed, and the second action was a personal claim unrelated to the note. Keller v. Llewellyn, 175 M 164, 573 P2d 166 (1977).

DECISIONS UNDER UNIFORM NEGOTIABLE INSTRUMENTS LAW

Delivery Not Shown: Under section 55-216, R.C.M. 1947 (now repealed), delivery of a promissory note, in order to be effectual, must be made by or under the authority of the maker of the instrument, and therefore where no such delivery is shown the payee named therein cannot recover on it. Baroch v. Greater Mont. Oil Co., 70 M 93, 225 P 800 (1924).

Admissibility of Note in Evidence: In an action on a promissory note, its production by plaintiff raised a presumption of a valid and intentional delivery of it to the payee by the maker, and it was properly admitted as against the objection that plaintiff was not the owner or holder thereof. Ely, Salyards & Co. v. Farmers' Elev. Co., 69 M 265, 221 P 522 (1923).

Defenses Available Against Holder Not in Due Course: The Uniform Negotiable Instruments Act deals with negotiable instruments only so long as they are in the hands of holders in due course; if in other hands, they are subject to the same defenses as if nonnegotiable. Merchants' Nat'l Bank of Billings v. Smith, 59 M 280, 196 P 523, 15 ALR 430 (1921).

Want or Failure of Consideration: Want or failure of consideration is a good defense against a holder not in due course. First Nat'l Bank of Lewistown v. Wilson, 57 M 384, 188 P 371 (1920).

30-3-307. Proof of signatures and status as holder in due course.

Official Comment

Source: Section 3-308, U.C.C.

Prior Uniform Statutory Provision: Section 59, Uniform Negotiable Instruments Law.

Official Comment to 1991 Amendment:

1. Section 3-308 is a modification of present Section 3-307 [30-3-307 prior to 1991 revision]. The first two sentences of subsection (a) [subsection (1) of this section] are a restatement of present Section 3-307(1) [30-3-307(1) prior to 1991 revision]. The purpose of the requirement of a specific denial in the pleadings is to give the plaintiff notice of the defendant's claim of forgery or lack of authority as to the particular signature, and to afford the plaintiff an opportunity to investigate and obtain evidence. If local rules of pleading permit, the denial may be on information and belief, or it may be a denial of knowledge or information sufficient to form a belief. It need not be under oath unless the local statutes or rules require verification. In the absence of such specific denial the signature stands admitted, and is not in issue. Nothing in this section is intended, however, to prevent amendment of the pleading in a proper case.

The question of the burden of establishing the signature arises only when it has been put in issue by specific denial. "Burden of establishing" is defined in Section 1-201 [30-1-201]. The burden is on the party claiming under the signature, but the signature is presumed to be authentic and authorized except as stated in the second sentence of subsection (a) [subsection (1) of this section]. "Presumed" is defined in Section 1-201 [30-1-201] and means that until some evidence is introduced which would support a finding that the signature is forged or unauthorized, the plaintiff is not required to prove that it is authentic. The presumption rests upon the fact that in ordinary experience forged or unauthorized signatures are very uncommon, and normally any evidence is within the control of, or more accessible to, the defendant. The defendant is therefore required to make some sufficient showing of the grounds for the denial before the plaintiff is required to introduce evidence. The defendant's evidence need not be sufficient to require a directed verdict, but it must be enough to support the denial by permitting a finding in the defendant's favor. Until introduction of such evidence the presumption requires a finding for the plaintiff. Once such evidence is introduced the burden of establishing the signature by a preponderance of the total evidence is on the plaintiff. The presumption does not arise if the action is to enforce the obligation of a purported signer who has died or become incompetent before the evidence is required, and so is disabled from obtaining or introducing it. "Action" is defined in Section 1-201 [30-1-201] and includes a claim asserted against the estate of a deceased or an incompetent.

The last sentence of subsection (a) [subsection (1) of this section] is a new provision that is necessary to take into account proposed Section 3-402(a) [30-3-403(1)] that allows an undisclosed principal to be liable on an instrument signed by an authorized representative. In that case the person enforcing the instrument must prove that the undisclosed principal is liable.

2. Subsection (b) [subsection (2) of this section] restates present Section 3-307(2) and (3) [30-3-307(2) and (3) prior to 1991 revision]. Once signatures are proved or admitted a holder, by mere production of the instrument, proves "entitlement to enforce the instrument" because under Section 3-301 [30-3-301] a holder is a person entitled to enforce the instrument. Any other person in possession of an instrument may recover only if that person has the rights of a holder. Section 3-301 [30-3-301]. That person must prove a transfer giving that person such rights under Section 3-203(b) [30-3-210(2)] or that such rights were obtained by subrogation or succession.

If a plaintiff producing the instrument proves entitlement to enforce the instrument, either as a holder or a person with rights of a holder, the plaintiff is entitled to recovery unless the defendant proves a defense or claim in recoupment. Until that proof is made, the issue as to whether the plaintiff has rights of a holder in due course does not arise. In the absence of a defense or claim in recoupment, any person entitled to enforce the instrument is entitled to recover. If a defense or claim in recoupment is proved, the plaintiff may seek to cut off the defense or claim in recoupment by proving that the plaintiff is a holder in due course or that the plaintiff has rights of a holder in due course under Section 3-203(b) [30-3-210(2)] or by subrogation or succession. All elements of Section 3-302(a) [30-3-302(1)] must be proved.

Nothing in this section is intended to say that the plaintiff must necessarily prove rights as a holder in due course. The plaintiff may elect to introduce no further evidence, in which case a verdict may be directed for the plaintiff or the defendant, or the issue of the defense or claim in recoupment may be left to the jury, according to the weight and sufficiency of the defendant's evidence. The plaintiff may elect to rebut the defense or claim in recoupment by proof to the contrary, in which case a verdict may be directed for either party or the issue may be for the jury. Subsection (b) [subsection (2) of this section] means only that if the plaintiff claims the rights of a holder in due course against the defense or claim in recoupment, the plaintiff has the burden of proof on that issue.

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "Burden of establishing signatures, defenses and due course. (1) Unless specifically denied in the pleadings each signature on an instrument is admitted. When the effectiveness of a signature is put in issue:

(a) the burden of establishing it is on the party claiming under the signature; but

(b) the signature is presumed to be genuine or authorized except where the action is to enforce the obligation of a purported signer who has died or become incompetent before proof is required.

(2) When signatures are admitted or established, production of the instrument entitles a holder to recover on it unless the defendant establishes a defense.

(3) After it is shown that a defense exists a person claiming the rights of a holder in due course has the burden of establishing that he or some person under whom he claims is in all respects a holder in due course."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

DECISIONS UNDER U.C.C. PRIOR TO 1991 REVISION

Recovery on Written Instrument Absent Defense — Parol Evidence Not Allowed: Under Montana's Uniform Commercial Code, when signatures to an instrument are admitted or established, production of the instrument entitles the holder to recover on it unless the defendant establishes a defense. Parol evidence will not be allowed to contradict, alter, or vary a contract that has been reduced to a writing. Niemen v. Howell, 234 M 471, 764 P2d 854, 45 St. Rep. 2058 (1988).

Foreclosure of Mortgage Securing Note — Payment to Holder Required: The Dahls executed a note to Sythe and also executed a real estate mortgage in Sythe's favor. The note was placed in an escrow account in the Culbertson State Bank, and the bank was designated as the place where payment was to be made. Sythe assigned the note to the bank as security for a note obtained by him. Sythe later gave the bank a written assignment of the mortgage. Defendant Dahl was given written notice of this assignment. The bank did not receive any payments from Sythe on his notes or from Dahl on the note assigned to the bank. The bank brought an action for the foreclosure of the mortgage against Dahl. Dahl contended that the note was discharged because it was paid in full, with payments being made to Sythe. The bank was never able to make service of process on Sythe. The bank was a "holder" of the note since it was in possession of the note endorsed by Sythe. As a holder and having produced the note, the bank was entitled to recover unless the defendant established a defense. Defendant's sole defense was that he had paid the note to Sythe. The defense of payment only discharges the maker's liability on the instrument if payment is made to the holder. Defendant never attempted to prove payment to the holder. Since the bank was the holder of the note and a valid assignee of the mortgage securing the note, it was entitled to a decree of foreclosure. Culbertson St. Bank v. Dahl, 190 M 33, 617 P2d 1295, 37 St. Rep. 1752 (1980).

DECISIONS UNDER UNIFORM NEGOTIABLE INSTRUMENTS LAW

Presumption of Holder in Due Course: The presumption declared by this section makes the production of a note properly indorsed prima facie evidence of a right to recover thereon. Best v. Boyer, 98 M 40, 37 P2d 331 (1934).

Burden of Proof: Under section 55-509, R.C.M. 1947 (now repealed), where, after plaintiff endorsee had made out a prima facie case, defendant (drawer) produced evidence tending fairly to prove that the payee had obtained the check through fraud, the burden shifted to plaintiff to prove every fact necessary to show that he was a holder in due course, among them that he took it in good faith and for value, failing in which he was not entitled to recover. Matteson v. Trask, 63 M 160, 206 P 428 (1922).

30-3-308. Notice of breach of fiduciary duty.

Official Comment

Source: Section 3-307, U.C.C.

Official Comment:

1. Present Sections 3-304(2) and (4)(e) [30-3-304(2) and (4)(e) prior to 1991 revision], taken with the accompanying Comment 5, are confusing as to whether they apply when the instrument is made payable to a fiduciary as such or is made payable by a fiduciary as such to the fiduciary personally. Proposed Section 3-307 [30-3-308] avoids this confusion by stating rules that comprehensively cover the issue of when the taker of an instrument has notice of breach of a fiduciary duty.

2. Subsection (a) [subsection (1) of this section] states the application of the section and defines its basic terms. This section applies only when the taker knows it is dealing with a fiduciary. These definitions are consonant with the meaning usually ascribed to these terms. “Taker” includes a payor bank, a depositary bank that takes an instrument for collection or a purchaser of the instrument. Subsection (b)(i) [subsection (2)(a) of this section] is based on Uniform Fiduciaries Act Section 4 in providing that if the instrument is payable to the fiduciary, as such, or to the represented person, the taker has notice of a claim if the instrument is negotiated for the fiduciary’s personal debt. If fiduciary funds are deposited to a personal account of the fiduciary or to an account that is not an account of the represented person or of the fiduciary, as such, there is a split of authority concerning whether the bank is on notice of a breach of fiduciary duty. Subsection (b)(iii) [subsection (2)(c) of this section] states that the bank is given notice of breach of fiduciary duty because of the deposit. The Uniform Fiduciaries Act states that the bank is not on notice unless it has knowledge of facts that makes its receipt of the deposit an act of bad faith.

3. Subsection (c) [subsection (3) of this section] is based on Uniform Fiduciaries Act Section 6 and applies when the instrument is drawn by the fiduciary as such to the fiduciary personally. The term “personally” is used as it is used in the Uniform Fiduciaries Act to mean that the instrument is payable to the payee as an individual and not as a fiduciary. Here the taker may assume that the fiduciary may use the instrument for the personal benefit of the fiduciary.

4. Subsection (d) [subsection (4) of this section] can be illustrated by a hypothetical case. Corporation draws a check payable to Bank. X, an officer or employee of corporation delivers the check to Bank. The person signing the check on behalf of Corporation is X or another person. If Bank takes this check from X knowing X is a fiduciary, Bank is on notice of a claim by Corporation if it takes the instrument under the same circumstances stated in subsection (b) [subsection (2) of this section]. This subsection rejects the contrary view of Eldon’s Super Fresh Stores, Inc. v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 296 Minn. 130, 207 N.W.2d 282 (1973).

Case Notes

Existence of Fiduciary Duty Considered Question of Law, Not Fact — Summary Judgment on Question Proper if No Genuine Issue of Material Fact Exists: To resolve several inconsistent prior opinions, the Supreme Court held that the issue of whether a fiduciary duty exists between two parties is a question of law, not fact, and thus may be resolved on summary judgment if no genuine issues of material fact exist. Similarly, the issue of whether a special relationship exists between two parties that would give rise to a fiduciary relationship is also a question of law, not fact. In order to determine whether a special relationship exists in cases in which it does not normally exist, such as between a bank and a customer, a court may be required to make a fact-intensive inquiry. The circumstances of a particular relationship are factual, so disputes over material facts will preclude summary judgment, but the conclusion drawn by a court from undisputed facts is one of law, not of fact. Gliko v. Permann, 2006 MT 30, 331 M 112, 130 P3d 155 (2006), overruling Davis v. Church of Jesus Christ of Latter Day Saints, 258 M 286, 852 P2d 640 (1993), and Kondelik v. First Fidelity Bank of Glendive, 259 M 446, 857 P2d 687 (1993).

30-3-309. Enforcement of lost, destroyed, or stolen instrument.

Official Comment

Source: Section 3-309, U.C.C.

Official Comment:

Proposed Section 3-309 [30-3-309] is a modification of present Section 3-804 [30-3-804, now repealed]. The rights stated are those of “a person entitled to enforce the instrument” at the time of loss rather than those of an “owner” as in present Section 3-804 [30-3-804, now repealed]. Under subsection (b) [subsection (2) of this section], judgment to enforce the instrument cannot be given unless the court finds that the defendant will be adequately protected against a claim to the instrument by a holder that may appear at some later time. The court is given discretion in determining how adequate protection is to be assured. Present Section 3-804 [30-3-804, now repealed] allows the court to "require security indemnifying the defendant against loss." Under proposed Section 3-309 [30-3-309] adequate protection is a flexible concept. For example, there is substantial risk that a holder in due course may make a demand for payment if the instrument was payable to bearer when it was lost or stolen. On the other hand if the instrument was payable to the person who lost the instrument and that person did not indorse the instrument, no other person could be a holder of the instrument. In some cases there is risk of loss only if there is doubt about whether the facts alleged by the person who lost the instrument are true. Thus, the type of adequate protection that is reasonable in the circumstances may depend on the degree of certainty about the facts in the case.

30-3-310. Effect of instrument on obligation for which taken.

Official Comment

Source: Section 3-310, U.C.C.

Official Comment:

1. Proposed Section 3-310 [30-3-310] is a modification of present Section 3-802 [30-3-802, now repealed]. As a practical matter, application of present Section 3-802 [30-3-802, now repealed] is limited to cases in which a check or a note was given for an obligation. Subsections (a) and (b) of proposed Section 3-310 [30-3-310(1) and (2)] are therefore stated in terms of checks and notes in the interests of clarity. Subsection (c) [subsection (3) of this section] covers the rare cases in which some other instrument is given to pay an obligation.

2. Subsection (a) [subsection (1) of this section] deals with the case in which a certified check, cashier's check or teller's check is given in payment of an obligation. In that case the obligation is discharged unless there is an agreement to the contrary. Proposed subsection (a) [subsection (1) of this section] drops the exception in present Section 3-802 [30-3-802, now repealed] for cases in which there is a right of recourse on the instrument against the obligor. Under present Section 3-802(1)(a) [30-3-802, now repealed] the obligation is not discharged if there is a right of recourse on the instrument against the obligor. Proposed subsection (a) [subsection (1) of this section] changes this result. The underlying obligation is discharged, but any right of recourse on the instrument is preserved.

3. Subsection (b) [subsection (2) of this section] concerns cases in which an uncertified check or a note is taken for an obligation. The typical case is that in which a buyer pays for goods or services by giving the seller the buyer's personal check, or in which the buyer signs a note for the purchase price. Subsection (b) [subsection (2) of this section] also applies to the uncommon cases in which a check or note of a third person is given in payment of the obligation. Subsection (b) [subsection (2) of this section] preserves the rule under present Section 3-802(1)(b) [30-3-802, now repealed] that the buyer's obligation to pay the price is suspended, but subsection (b) [subsection (2) of this section] spells out the effect more precisely. If the check or note is dishonored, the seller may sue on either the dishonored instrument or the contract of sale if the seller has possession of the instrument and is the person entitled to enforce it. If the right to enforce the instrument is held by somebody other than the seller, the seller can't enforce the right to payment of the price under the sales contract because that right is represented by the instrument which is enforceable by somebody else. Thus, if the seller sold the note or the check to a holder and has not reacquired it after dishonor, the only right that survives is the right to enforce the instrument.

The last sentence of subsection (b)(3) [subsection (2)(c) of this section] applies to cases in which an instrument of another person is indorsed over to the obligee in payment of the obligation. For example, Buyer delivers an uncertified personal check of X payable to the order of Buyer to Seller in payment of the price of goods. Buyer indorses the check over to Seller. Buyer is liable on the check as indorser. If Seller neglects to present the check for payment or to deposit it for collection within 30 days of the indorsement, Buyer's liability as indorser is discharged. Section 3-415(e) [30-3-414(5)]. Under the last sentence of Section 3-310(b)(3) [30-3-310(2)(c)] Buyer is also discharged on the obligation to pay for the goods.

4. There is uncertainty concerning the applicability of present Section 3-802 [30-3-802, now repealed] to the case in which the check given for the obligation has been stolen from the payee, the payee's signature has been forged, and the forger has obtained payment. The last sentence of proposed subsection (b)(4) [subsection (2)(d) of this section] addresses this issue. If the payor bank pays a holder, the drawer is discharged on the underlying obligation because the check was paid. Subsection (b)(1) [subsection (2)(a) of this section]. If the payor bank pays a person not entitled to enforce the instrument, as in the hypothetical case, the suspension of the underlying obligation continues because the check has not been paid. Section 3-603(a) [30-3-604(1)]. The payee's cause

of action is against the depositary bank or payor bank in conversion under proposed Section 3-420 [30-3-419] or against the drawer under proposed Section 3-309 [30-3-309]. The payee cannot merely ignore the instrument and sue the drawer on the underlying contract. This would impose on the drawer the risk that the check when stolen was indorsed in blank or to bearer.

5. Subsection (c) [subsection (3) of this section] deals with rare cases in which other instruments are taken for obligations. If a bank is the obligor on the instrument, subsection (a) [subsection (1) of this section] applies and the obligation is discharged. In any other case subsection (b) [subsection (2) of this section] applies.

Case Notes

Retention of Personal Check as Suspending Underlying Obligation — No Default During Period of Suspension: The Quigleys agreed to purchase property from the Ackers and to assume the obligations of the buyer under the original sale contract. About 5 years later, the Quigleys missed a payment, but they subsequently tendered a personal, uncertified check for the missed payment to the escrow agent. The Ackers instructed the escrow agent to hold the check and then sent a default notice to the Quigleys, who did not cure the default. About 1 month later, the Quigleys received a termination notice informing them that the entire balance on the contract had been accelerated. Four days later, the Ackers returned the Quigleys' personal check to them. The Ackers' retention of the Quigleys' check was held to be a taking for an underlying obligation, suspending the obligation until the time that the check was returned. Because the obligation was suspended, there was, by definition, no default during the suspension. Consequently, the default and termination notices were based on an erroneous assessment of default and had no legal effect, and the District Court's conclusion that the notices were defective was a correct interpretation of the law. Quigley v. Acker, 1998 MT 72, 288 M 190, 955 P2d 1377, 55 St. Rep. 295 (1998), following Grumet v. Bristol, 484 A2d 1099 (N.H. 1984).

30-3-311. Accord and satisfaction by use of instrument.

Official Comment

Source: Section 3-311, U.C.C.

Official Comment:

1. This section deals with an informal method of dispute resolution carried out by use of a negotiable instrument. In the typical case there is a dispute concerning the amount that is owed on a claim.

Case #1. The claim is for the price of goods or services sold to a consumer who asserts that he or she is not obliged to pay the full price for which the consumer was billed because of a defect or breach of warranty with respect to the goods or services.

Case #2. A claim is made on an insurance policy. The insurance company alleges that it is not liable under the policy for the amount of the claim. In either case the person against whom the claim is asserted may attempt an accord and satisfaction of the disputed claim by tendering a check to the claimant for some amount less than the full amount claimed by the claimant. A statement will be included on the check or in a communication accompanying the check to the effect that the check is offered as full payment or full satisfaction of the claim. Frequently, there is also a statement to the effect that obtaining payment of the check is an agreement by the claimant to a settlement of the dispute for the amount tendered. The case law is in conflict over the question of whether obtaining payment of the check has the effect of an agreement to the settlement proposed by the debtor. This issue is governed by a common law rule, but some courts hold that the common law is modified by Section 1-207 [30-1-207] which they interpret as applying to full settlement checks.

2. Comment d. to Restatement of Contracts, Section 281 discusses the full satisfaction check and the applicable common law rule. In a case like Case #1, the buyer can propose a settlement of the disputed bill by a clear notation on the check indicating that the check is tendered as full satisfaction of the bill. Under the common law rule the seller, by obtaining payment of the check accepts the offer of compromise by the buyer. The result is the same if the seller adds a notation to the check indicating that the check is accepted under protest or in only partial satisfaction of the claim. Under the common law rule the seller can refuse the check or can accept it subject to the condition stated by the buyer, but the seller can't accept the check and refuse to be bound by the condition. The rule applies only to an unliquidated claim or a claim disputed in good faith by the buyer. The dispute in the courts is whether Section 1-207 [30-1-207] changes the common law rule. The Restatement states that section "need not be read as changing this well-established rule."

3. A proposed amendment to Section 1-207 [30-1-207] follows decisions that hold that Section 1-207 [30-1-207] was not intended to change the common law rule. The amendment states that Section 1-207 [30-1-207] "does not apply to an accord and satisfaction." Under the amendment, Section 3-311 [30-3-311] governs full satisfaction checks. Proposed section 3-311 [30-3-311] follows the common law rule with a minor variation to reflect modern business conditions. In cases covered by Section 3-311 [30-3-311] there will often be an individual on one side of the dispute and a business organization on the other. This section is not designed to favor either the individual or the business organization. In Case #1 the person seeking the accord and satisfaction is an individual. In Case #2 the person seeking the accord and satisfaction is an insurance company. Section 3-311 [30-3-311] is based on a belief that the common law rule produces a fair result and that informal dispute resolution by full satisfaction checks should be encouraged.

4. Subsection (a) [subsection (1) of this section] states three requirements for application of Section 3-311 [30-3-311]. The person seeking the accord and satisfaction must prove that those requirements are met. If that person also proves that the communication required by subsection (b) [subsection (2) of this section] was given, the claim is discharged unless subsection (c) [subsection (3) of this section] applies. Normally the communication required by subsection (b) [subsection (2) of this section] is written on the check. Thus, the canceled check can be used to prove the communication as well as the fact that the claimant obtained payment of the check. Subsection (b) [subsection (2) of this section] requires a "conspicuous" statement in the communication that the instrument was tendered in full satisfaction of the claim. "Conspicuous" is defined in Section 1-201(10) [30-1-201(10)]. The statement is conspicuous if "it is so written that a reasonable person against whom it is to operate ought to have noticed it." If the claimant can reasonably be expected to examine the check, almost any statement on the check should be noticed and is therefore conspicuous. In cases in which the claimant is an individual the claimant will receive the check and will have to indorse it. Since the statement concerning tender in full satisfaction normally will appear above the space provided for the claimant's indorsement of the check, the claimant "ought to have noticed" the statement.

Subsection (c) [subsection (3) of this section] is a limitation on subsection (b) [subsection (2) of this section] in cases in which the claimant is an organization. If the claimant is an organization payment of the check might be obtained without notice to the personnel of the organization concerned with the disputed claim. Subsection (c) [subsection (3) of this section] is designed to protect the claimant against an inadvertent accord and satisfaction. Some business organizations have claims against very large numbers of customers. Examples are department stores, public utilities and the like. These claims are normally paid by checks sent by customers to a designated office at which clerks employed by the claimant or a bank acting for the claimant process the checks and record the amounts paid. If the processing office is not designed to deal with communications extraneous to recording the amount of the check and the account number of the customer, payment of a full satisfaction check can easily be obtained without knowledge by the claimant of the existence of the full satisfaction statement. Normally, the clerks of the claimant have no reason to look at the reverse side of a check. Indorsement by the claimant normally is done by mechanical means or, in some cases, no indorsement is made. Section 4-205(1) [30-4-205(1)]. Subsection (c) [subsection (3) of this section] allows the claimant to protect itself by advising customers by a conspicuous statement (Section 1-201(10) [30-1-201(10)]) that communications regarding disputed debts must be sent to a particular person, office or place. The statement must be given to the customer within a reasonable time before the tender is made. This requirement is designed to assure that the customer has reasonable notice that the full satisfaction check must be sent to a particular place. The reasonable time requirement could be satisfied by a notice on the billing statement sent to customer. If the full satisfaction check is sent to the designated destination and the check is paid, the claim is discharged. If the claimant proves that the check was not received at the designated destination the claim is not discharged under subsection (b) [subsection (2) of this section] unless subsection (d) [subsection (4) of this section] applies.

Subsection (d) [subsection (4) of this section] allows the customer to avoid the effect of subsection (c) [subsection (3) of this section], by proving that an agent of the claimant having direct responsibility with respect to the disputed claim received the full satisfaction check and communication indicating that a full satisfaction tender was being made or knew about it before collection was initiated. For example, if the check and communication are received by a collection agency acting for the claimant to collect the disputed claim, obtaining payment of the check will result in an accord and satisfaction even if the claimant gave notice that full satisfaction checks be sent to some other office. Similarly, if a customer asserting a claim for breach of warranty with respect to defective goods purchased in a retail outlet of a large chain store delivers the full satisfaction check to the manager of the retail outlet at which the goods were purchased, obtaining payment of the check will also result in an accord and satisfaction. On the other hand, if the check is mailed to the chief executive officer of the chain store subsection (d) [subsection (4) of this section] would probably not be satisfied. The chief executive officer of a large corporation may have general responsibility for operations of the company, but does not normally have direct responsibility for resolving a small disputed bill to a customer. A check for a relatively small amount mailed to a high executive officer of a large organization is not likely to receive the executive's personal attention.

In some cases the disputed claim may have been assigned to a finance company or bank as part of a financing arrangement with respect to accounts receivable. If the account debtor was notified of the assignment, the claimant is the assignee of the account receivable and the "agent of the claimant" in subsection (d) [subsection (4) of this section] refers to an agent of the assignee.

Case Notes

Amendment of Judgment Proper Based on Impermissible Double Recovery Yet Jury's Determination of Breach Supported by Substantial Evidence — Accord and Satisfaction Not Argued and Not Supported by Facts: The plaintiff filed a motion for a new trial or amendment of judgment, arguing that there was insufficient evidence to justify the jury's damages award of $25,000 for the plaintiff's breach of the implied covenant of good faith and fair dealing. The trial court found that this argument had merit because the award would be an impermissible double recovery for the defendant and, accordingly, granted the plaintiff's request that the award be vacated. However, the plaintiff never asserted that there was not substantial evidence supporting the jury's determination that the plaintiff breached the second agreement, nor did the plaintiff argue waiver or accord and satisfaction as defenses. Thus, though the parties disputed its terms, there was sufficient evidence for the jury to find that all the elements of a contract existed, that the plaintiff breached a second agreement, and that the defendant was damaged. Moreover, the Supreme Court determined that the evidence was substantive enough for the jury to have found in favor of the defendant and to have rejected the waiver and accord and satisfaction arguments the plaintiff presented on appeal. Ryffel Family Partnership v. Alpine Country Constr., Inc., 2016 MT 350, 386 Mont. 165, 386 P.3d 971.

30-3-312. Lost, destroyed, or stolen cashier's check, teller's check, or certified check.

Official Comment

Source: Section 3-312, U.C.C.

Compiler's Comments

Saving Clause: Section 3, Ch. 33, L. 2001, was a saving clause.

Effective Date: Section 4, Ch. 33, L. 2001, provided that this section is effective on passage and approval. Approved March 13, 2001.

Part 4
Liability of Parties

Part Case Notes

DECISIONS UNDER U.C.C. PRIOR TO 1991 REVISION

Finding of Judgment or Insolvency Required: When the record did not indicate that the bank obtained a judgment and when the District Court had not made a finding that the signer of a contract was insolvent, it was improper to allow the bank a setoff of funds from a guarantor's checking account. Citizens First Nat'l Bank of Wolf Point v. Moe Motor Co., 248 M 495, 813 P2d 400, 48 St. Rep. 528 (1991).

Guarantor Owes Pro Rata Share: Appellant and four other shareholders in company executed continuing guaranties for promissory notes on behalf of their shared business. Appellant subsequently signed away his share in company and left the business. Although the court considered appellant's equitable defense that he was not liable for his pro rata share of the notes because the other four guarantors personally profited from the sale of the business after appellant departed, he remains liable for his pro rata share. He signed the guaranty knowing the lender could sue him directly on the notes. All five shareholders shared equal liability on the promissory notes, and appellant is required to contribute his one-fifth pro rata share. Citizens St. Bank v. Bossard, 226 M 75, 733 P2d 1296, 44 St. Rep. 468 (1987).

Guarantors' Right of Contribution When Benefits Unequal: Where the defendant claimed he was promised stock in a corporation in exchange for his guaranty of a note made by the corporation but subsequently revoked the guaranty when no stock was issued to him, the District Court erred in granting summary judgment against the defendant in an action for contribution brought by the other guarantors when the corporation defaulted on the note. Contribution among co-obligors is an equitable concept, and an equitable defense of one obligor must be permitted to be raised and presented. The defendant was entitled to present his proof of lack of equality of benefits and was erroneously prevented from doing so by the District Court's summary judgment. Bossard v. Sullivan, 206 M 392, 670 P2d 1389, 40 St. Rep. 1733 (1983).

Guarantor's Duty: In the language of a guaranty the guarantor assured that all sums stated in the note "shall be promptly paid in full, in accordance with the provisions thereof, at maturity, by acceleration, or otherwise", which brings the guarantor within the provisions of this section. Consequently, if the instrument is not paid when due, the guarantor must pay it according to its tenor. Stewart v. Casey, 182 M 185, 595 P2d 1176 (1979).

30-3-401. Signature.

Official Comment

Source: Section 3-401, U.C.C.

Prior Uniform Statutory Provision: Section 18, Uniform Negotiable Instruments Law.

Official Comment to 1991 Amendment:

1. Obligation on an instrument depends on a signature that is binding on the obligor. The signature may be made by the obligor personally or by an agent authorized to act for the obligor. Signature by agents is covered by Section 3-402 [30-3-403]. It is not necessary that the name of the obligor appear on the instrument, so long as there is a signature that binds the obligor. Signature includes an indorsement.

2. A signature may be handwritten, typed, printed or made in any other manner. It need not be subscribed, and may appear in the body of the instrument, as in the case of "I, John Doe, promise to pay . . ." without any other signature. It may be made by mark, or even by thumbprint. It may be made in any name, including any trade name or assumed name, however false and fictitious, which is adopted for the purpose. Parol evidence is admissible to identify the signer, and when the signer is identified the signature is effective. Indorsement in a name other than that of the indorser is governed by Section 3-204(d) [30-3-203(4)].

This section is not intended to affect any other law requiring a signature by mark to be witnessed, or any signature to be otherwise authenticated, or requiring any form of proof.

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "(1) No person is liable on an instrument unless his signature appears thereon.

(2) A signature is made by use of any name, including any trade or assumed name, upon an instrument, or by any word or mark used in lieu of a written signature."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

DECISIONS UNDER U.C.C. AFTER 1991 REVISION

Parol Evidence Held Inadmissible to Prove Representative Capacity of Maker of Note — Definition of Debtor — Unambiguous Terms Notwithstanding Security Agreement — Statute Not Retroactive — Former Statute Inapplicable: By use of a note and security agreement, Carelli sold 38 elk to Hall who, as Stireses' partner, operated the Elk Valley Game Ranch (Game Ranch). Later, Carelli brought an action against Stireses, alleging that Stireses were also liable on the debt because Hall had orally told Carelli at the time of the sale that the elk were being purchased for the Game Ranch. The Supreme Court held that Hall's oral statements to Carelli were inadmissible on the issue of Stireses' liability on the note for three reasons: (1) The note was clear and unambiguous in that Hall's representative capacity did not appear on the note, Hall was the "debtor" as defined in the security agreement, and a reference to the Game Ranch in the security agreement did not make the note ambiguous so as to require explanation by parol evidence. (2) The Supreme Court held that a 1991 amendment to 30-3-403 regarding the capacity in which a person signs an instrument, if applied in this case, would cause a difference in the liability of the parties. Therefore, the amendment is substantive. Because there was no expression of legislative intent that the 1991 version be applied retroactively, the 1985 version of 30-3-403 and not the 1991 version applies, and parol evidence is not relevant to that 1985 version. (3) The facts of the case did not fall within the terms of the 1985 version of 30-3-403. Carelli v. Hall, 279 M 202, 926 P2d 756, 53 St. Rep. 1116 (1996).

DECISIONS UNDER UNIFORM NEGOTIABLE INSTRUMENTS LAW

Absence of Name From Note:

A person whose name does not appear on a promissory note is not liable thereon. Young v. Bray, 54 M 415, 170 P 1044 (1918); Kohrs v. Smith, 45 M 467, 124 P 275 (1912).

To hold a person or his estate liable on a promissory note, his name must appear thereon. First Nat'l Bank of Missoula v. Cottonwood Land Co., 51 M 544, 154 P 582 (1916). See also First St. Bank of Philipsburg v. Mussigbrod, 83 M 68, 271 P 695 (1928).

30-3-403. Signature by representative.

Official Comment

Source: Section 3-402, U.C.C.

Prior Uniform Statutory Provision: Sections 19, 20 and 21, Uniform Negotiable Instruments Law.

Official Comment to 1991 Amendment:

1. Subsection (a) [subsection (1) of this section] states when the represented person is bound on an instrument when the instrument is signed by a representative. If under the law of agency the represented person would be bound by the act of the representative in signing either the name of the represented person or that of the representative, the signature is the authorized signature of the represented person. Present Section 3-401(1) [30-3-401(1) prior to 1991 revision] states that "no person is liable on an instrument unless his signature appears thereon." This has been interpreted as meaning that an undisclosed principal is not liable on an instrument. This is an exception to ordinary agency law that binds an undisclosed principal on a simple contract.

There is no reason to retain this exception and it is changed by subsection (a) [subsection (1) of this section] which returns to ordinary rules of agency. If P, the principal, authorized A, the agent, to borrow money on P's behalf and A signed A's name to a note without disclosing that the signature was on behalf of P, A is liable on the instrument. But if the person entitled to enforce the note can also prove that P authorized A to sign on P's behalf, why shouldn't P also be liable on the instrument? To recognize the liability of P takes nothing away from the currency of negotiable instruments. Furthermore, imposing liability on P has the merit of making it impossible to have an instrument on which nobody is liable even though it was authorized by P. That result can occur under present Section 3-401(1) [30-3-401(1) prior to 1991 revision] if an authorized agent signs "as agent" but does not identify the principal on the note. The agent can escape liability on the note by proving that the agent and the payee who is seeking enforcement of the note did not intend that the agent be liable on the note when the note was issued. Present Section 3-403(2)(b) [30-3-403(2)(b) prior to 1991 revision]. The principal is not liable on the note under present 3-401(1) [30-3-401(1) prior to 1991 revision] because the principal's name does not appear on the note. Thus, nobody is liable on the note even though all parties knew that the note was signed by the agent on behalf of the principal. Under proposed Section 3-402 [30-3-403] the principal would be liable on the note.

2. Subsection (b) [subsection (2) of this section] concerns the question of when an agent who signs an instrument on behalf of a principal is bound on the instrument. The approach followed by present Section 3-403 [30-3-403 prior to 1991 revision] is to specify the form of signature that imposes or avoids liability. This approach is unsatisfactory. There are many ways in which there can be ambiguity about a signature. It is better to state a general rule. Subsection (b)(1) [subsection (2)(a) of this section] states that if the form of the signature unambiguously shows that it is made on behalf of an identified represented person (for example, "P, by A, Treasurer") the agent is not liable. This is a workable standard for a court to apply. Subsection (b)(2) [subsection (2)(b) of this section] partly changes present Section 3-403(2) [30-3-403(2) prior to 1991 revision]. Subsection (b)(2) [subsection (2)(b) of this section] relates to cases in which the agent signs on behalf of a principal but the form of the signature does not fall within subsection (b)(1) [subsection (2)(a) of this section]. The following cases are illustrative. In each case John Doe is the authorized agent of Richard Roe and John Doe signs a note on behalf of Richard Roe. In each case the intention of the original parties to the instrument is that Roe is to be liable on the instrument but Doe is not to be liable.

Case #1. Doe signs "John Doe" without indicating in the note that Doe is signing as agent. The note does not identify Richard Roe as the represented person.

Case #2. Doe signs "John Doe, Agent" but the note does not identify Richard Roe as the represented person.

Case #3. The name "Richard Roe" is written on the note and immediately below that name Doe signs "John Doe" without indicating that Doe signed as agent. In each case Doe is liable on the instrument to a holder in due course without notice that Doe was not intended to be liable. In none of the cases does Doe's signature unambiguously show that Doe was signing as agent for an identified principal. A holder in due course should be able to resolve any ambiguity against Doe.

But the situation is different if a holder in due course is not involved. In each case Roe is liable on the note. Subsection (a) [subsection (1) of this section]. If the original parties to the note did not intend that Doe also be liable, imposing liability on Doe is a windfall to the person enforcing the note. Under subsection (b)(2) [subsection (2)(b) of this section] Doe is prima facie liable because his signature appears on the note and the form of the signature does not unambiguously refute personal liability. But Doe can escape liability by proving that the original parties did not intend that he be liable on the note. This is a change from present Section 3-403(2)(a) [30-3-403(2)(a) prior to 1991 revision].

A number of cases have involved situations in which an agent has signed the agent's name to a note, without qualification and without naming the person represented, intending to bind the principal but not the agent. The agent attempted to prove that the other party had the same intention. Some of these cases involved mistake, and in some there was evidence that the agent may have been deceived into signing in that manner. Some of the cases have refused to allow proof of the intention of the parties and have imposed liability on the agent based on present Section 3-403(2)(a) [30-3-403(2)(a) prior to 1991 revision] even though both parties to the instrument may have intended that the agent not be liable. Subsection (b)(2) [subsection (2)(b) of this section] changes the result of those cases, and is consistent with proposed Section 3-117 [30-3-119] which allows oral or written agreements to modify or nullify apparent obligations on the instrument.

Present Section 3-403 [30-3-403 prior to 1991 revision] speaks of the represented person being "named" in the instrument. Proposed Section 3-402 [30-3-403] speaks of the represented person being "identified" in the instrument. This change in terminology is intended to reject decisions under present Section 3-403(2) [30-3-403(2) prior to 1991 revision] requiring that the instrument state the legal name of the represented person.

3. Subsection (c) [subsection (3) of this section] is directed at the check cases. It states that if the check identifies the represented person the agent who signs on the signature line does not have to indicate agency status. Virtually all checks used today are in personalized form which identify the person on whose account the check is drawn. In this case, nobody is deceived into thinking that the person signing the check is meant to be liable. This subsection is meant to overrule cases such as Griffin v. Ellinger, 538 S.W.2d 97 (Texas 1976).

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "Signature by authorized representative. (1) A signature may be made by an agent or other representative, and his authority to make it may be established as in other cases of representation. No particular form of appointment is necessary to establish such authority.

(2) An authorized representative who signs his own name to an instrument:

(a) is personally obligated if the instrument neither names the person represented nor shows that the representative signed in a representative capacity;

(b) except as otherwise established between the immediate parties, is personally obligated if the instrument names the person represented but does not show that the representative signed in a representative capacity, or if the instrument does not name the person represented but does show that the representative signed in a representative capacity.

(3) Except as otherwise established the name of an organization preceded or followed by the name and office of an authorized individual is a signature made in a representative capacity."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

DECISIONS UNDER U.C.C. AFTER 1991 REVISION

Parol Evidence Held Inadmissible to Prove Representative Capacity of Maker of Note — Definition of Debtor — Unambiguous Terms Notwithstanding Security Agreement — Statute Not Retroactive — Former Statute Inapplicable: By use of a note and security agreement, Carelli sold 38 elk to Hall who, as Stireses' partner, operated the Elk Valley Game Ranch (Game Ranch). Later, Carelli brought an action against Stireses, alleging that Stireses were also liable on the debt because Hall had orally told Carelli at the time of the sale that the elk were being purchased for the Game Ranch. The Supreme Court held that Hall's oral statements to Carelli were inadmissible on the issue of Stireses' liability on the note for three reasons: (1) The note was clear and unambiguous in that Hall's representative capacity did not appear on the note, Hall was the "debtor" as defined in the security agreement, and a reference to the Game Ranch in the security agreement did not make the note ambiguous so as to require explanation by parol evidence. (2) The Supreme Court held that a 1991 amendment to this section regarding the capacity in which a person signs an instrument, if applied in this case, would cause a difference in the liability of the parties. Therefore, the amendment is substantive. Because there was no expression of legislative intent that the 1991 version be applied retroactively, the 1985 version of this section and not the 1991 version applies, and parol evidence is not relevant to that 1985 version. (3) The facts of the case did not fall within the terms of the 1985 version of this section. Carelli v. Hall, 279 M 202, 926 P2d 756, 53 St. Rep. 1116 (1996).

DECISIONS UNDER U.C.C. PRIOR TO 1991 REVISION

Parol Evidence Held Inadmissible to Prove Representative Capacity of Maker of Note — Definition of Debtor — Unambiguous Terms Notwithstanding Security Agreement — Statute Not Retroactive — Former Statute Inapplicable: By use of a note and security agreement, Carelli sold 38 elk to Hall who, as Stireses' partner, operated the Elk Valley Game Ranch (Game Ranch). Later, Carelli brought an action against Stireses, alleging that Stireses were also liable on the debt because Hall had orally told Carelli at the time of the sale that the elk were being purchased for the Game Ranch. The Supreme Court held that Hall's oral statements to Carelli were inadmissible on the issue of Stireses' liability on the note for three reasons: (1) The note was clear and unambiguous in that Hall's representative capacity did not appear on the note, Hall was the "debtor" as defined in the security agreement, and a reference to the Game Ranch in the security agreement did not make the note ambiguous so as to require explanation by parol evidence. (2) The Supreme Court held that a 1991 amendment to this section regarding the capacity in which a person signs an instrument, if applied in this case, would cause a difference in the liability of the parties. Therefore, the amendment is substantive. Because there was no expression of legislative intent that the 1991 version be applied retroactively, the 1985 version of this section and not the 1991 version applies, and parol evidence is not relevant to that 1985 version. (3) The facts of the case did not fall within the terms of the 1985 version of this section. Carelli v. Hall, 279 M 202, 926 P2d 756, 53 St. Rep. 1116 (1996).

Question of Personal Obligation When Successor Corporation Not Named and Representative Capacity Not Noted — Directed Verdict Improper: Defendant, who was general manager of a development company but who held no ownership interest, signed a memorandum guaranteeing payment of an advertising account prior to the company's reincorporation under another name. He was held personally obligated for payment on a motion for directed verdict. However, the Supreme Court reversed upon finding that the memorandum neither named as principal the successor company, which was not in existence at the time the note was drafted, nor noted defendant's representative capacity. These fact questions precluded a directed verdict on defendant's obligation. Huisenga v. Parkman, 231 M 210, 752 P2d 175, 45 St. Rep. 552 (1988).

Debtor's Signature in Representative and Personal Capacities — Subject to Personal Liability: Debtor entered an agreement with creditor by signing a "check-note" that consisted of two parts. The first part was in the name of the corporation and was signed by debtor in his capacity as corporate representative. The second part was an unconditional promise to pay and was signed in debtor's name only, without reference to the corporation or the debtor's signatory capacity. The District Court incorrectly concluded that debtor's signature unambiguously imparted personal liability for the debt. However, the finding that the parties intended to make debtor personally liable was supported by substantial evidence, including the fact that debtor omitted any reference to his signatory capacity in the second signature. Accounts Management Corp. v. Lyman Ranch, 230 M 35, 748 P2d 919, 44 St. Rep. 2233 (1987), distinguished in Carelli v. Hall, 279 M 202, 926 P2d 756, 53 St. Rep. 1116 (1996).

Summary Judgment Improper — Capacity in Which Promissory Note Signed: Summary judgment was not proper in an action on a promissory note when defendants had been sued individually but claimed, despite the appearance of the note, to have executed the note in their capacity as officers of a landscaping company. Although generally an unambiguous note cannot be varied by parol evidence, 30-4-403 specifically allows proof beyond the provisions of the note itself; thus, defendants' contentions established the existence of an issue of material fact. Clarks Fork Nat'l Bank v. Papp, 215 M 494, 698 P2d 851, 42 St. Rep. 577 (1985), distinguished in Carelli v. Hall, 279 M 202, 926 P2d 756, 53 St. Rep. 1116 (1996).

Deposit of Check Made to Another — When No Customer Warranties Breached — When Settlement of Check Final: A bank initiated an action against a customer to recover the amount of a check she deposited. The check was a paycheck made out to her former husband. She had deposited his paychecks for a time, and the Supreme Court found an agency relationship in the situation. On the occasion leading to this action, the appellant had deposited the check unsigned to her checking account. The bank stamped the check "deposited to the credit of" and filled in the name of the former husband. Meanwhile, the former husband told the check's issuer his ex-wife had forged his name on the check and deposited it. The issuer completed necessary documents and issued a new check. The former husband then disappeared, being suspected of embezzlement. Whether the customer breached her warranties under the U.C.C. depended on whether the settlement on the check became final. The Supreme Court overruled the trial court and held the settlement had become final. The return of the check occurred after the posting. The bank where the check was deposited was not entitled to a refund under 30-4-212. The customer warranties issue was decided by the principle that an agency could not be denied by a principal accepting its benefits. Because the appellant was not in breach of customer warranties, the bank's remedy, if any, was against the maker or the payee, the appellant's former husband. First Nat'l Bank v. Nunn, 192 M 487, 628 P2d 1110, 38 St. Rep. 869 (1981).

DECISIONS UNDER UNIFORM NEGOTIABLE INSTRUMENTS LAW

Pleading of Execution by Principal: An allegation in an action on a promissory note that it was executed by a certain person is sustained by proof of execution by an authorized agent of such person, and ratification of the acts of the agent can be proved under the general allegation that the principal executed it. Coffman v. Niece, 110 M 541, 105 P2d 661 (1940).

Nonnegotiable Instruments: In the absence of a special agreement to that effect, one who signs his name on the back of a nonnegotiable note is not an endorser in the sense that term is used in the Uniform Negotiable Instruments Law; hence an instruction in the language of section 55-604, R.C.M. 1947 (now repealed), that a person who places his signature upon an instrument otherwise than as maker, drawer or acceptor is deemed to be an endorser, was inapplicable in an action on such a note. Newer v. First Nat'l Bank of Harlem, 74 M 549, 241 P 613 (1925).

Effect of Signature by Agent: Under section 55-219, R.C.M. 1947 (now repealed), the signature of any party to a negotiable instrument may be made by a duly authorized agent. Commercial Nat'l Bank of Great Falls v. Reichelt, 62 M 302, 204 P 1037 (1922).

Corporate Officer: Under section 55-220, R.C.M. 1947 (now repealed), the endorsement, "J. H. Irwin, Presdt. Great Northern Surety Co.", on a note made payable to the company was its endorsement and not that of the individual signer, the contention that the words following the name were merely descriptio personae and did not indicate the character in which he acted not being maintainable under the Negotiable Instruments Law. Commercial Nat'l Bank of Great Falls v. Reichelt, 62 M 302, 204 P 1037 (1922).

Business Association: Persons conducting business as a voluntary association, using a common or trade name, may be held jointly and severally liable upon a note executed in the trade name by their agent authorized to do so. Larson v. Marcy, 61 M 1, 201 P 685 (1921).

30-3-404. Unauthorized signatures.

Official Comment

Source: Section 3-403, U.C.C.

Prior Uniform Statutory Provision: Section 23, Uniform Negotiable Instruments Law.

Official Comment to 1991 Amendment:

1. "Unauthorized" signature is defined in Section 1-201(43) [30-1-201(43)] as one that includes a forgery as well as a signature made by one exceeding actual or apparent authority. Present Section 3-404(1) [30-3-404(1) prior to 1991 revision] states that an unauthorized signature is inoperative as the signature of the person whose name is signed unless that person "is precluded from denying it." Under present Section 3-406 [30-3-406 prior to 1991 revision] if negligence by the person whose name is signed contributes to an unauthorized signature, that person "is precluded from asserting the . . . lack of authority." Both of these sections have been applied to cases in which a forged signature appears on an instrument and the person asserting rights on the instrument alleges that the negligence of the purported signer contributed to the forgery. Since the standards for liability between the two sections differ, the overlap between the sections causes great confusion. Proposed Section 3-403(a) [30-3-404(1)] deals with the problem by removing the preclusion language that appears in present Section 3-404 [30-3-404 prior to 1991 revision].

2. The except clause of the first sentence of subsection (a) [subsection (1) of this section] states the generally accepted rule that the unauthorized signature, while it is wholly inoperative as that of the person whose name is signed, is effective to impose liability upon the signer or to transfer any rights that the signer may have in the instrument. The signer's liability is not in

damages for breach of warranty of authority, but is full liability on the instrument in the capacity in which the signer signed. It is, however, limited to parties who take or pay the instrument in good faith; and one who knows that the signature is unauthorized cannot recover from the signer on the instrument.

3. The last sentence of subsection (a) [subsection (1) of this section] allows an unauthorized signature to be ratified. Ratification is a retroactive adoption of the unauthorized signature by the person whose name is signed and may be found from conduct as well as from express statements. For example, it may be found from the retention of benefits received in the transaction with knowledge of the unauthorized signature. Although the forger is not an agent, ratification is governed by the rules and principles applicable to ratification of unauthorized acts of an agent.

Ratification is effective only for the purposes of this Article. The unauthorized signature becomes valid so far as its effect as a signature is concerned. The ratification relieves the signer of liability on the instrument. It does not of itself relieve the signer of liability to the person whose name is signed. It does not in any way affect the criminal law. No policy of the criminal law prevents the person whose name is forged to assume liability to others on the instrument by ratifying the forgery, but the ratification cannot affect the rights of the state. While the ratification may be taken into account with other relevant facts in determining punishment, it does not relieve the signer of criminal liability.

4. Subsection (b) [subsection (2) of this section] clarifies the meaning of "unauthorized" in cases in which an instrument contains less than all of the signatures that are required as authority to pay a check. Judicial authority is split on the issue whether the one-year notice period under present Section 4-406(4) [30-4-406(4) prior to 1991 revision] bars a customer's suit against a payor bank that paid a check containing less than all of the signatures required by the customer to authorize payment of the check. Some cases take the view that if a customer requires that a check contain the signatures of both A and B to authorize payment and only A signs, there is no unauthorized signature within the meaning of that term in Section 4-406(4) [30-4-406(4) prior to 1991 revision] because A's signature is neither unauthorized nor forged. The other cases correctly point out that it is the customer's signature at issue and not that of A; hence, the customer's signature is unauthorized if all signatures required to authorize payment of the check are not on the check. Subsection (b) [subsection (2) of this section] follows the latter line of cases.

Subsection (b) [subsection (2) of this section] refers to "the authorized signature of an organization." The definition of "organization" in Section 1-201(28) [30-1-201(28)] is very broad. It covers not only commercial entities but also "two or more persons having a joint or common interest." Hence subsection (b) [subsection (2) of this section] would apply when a husband and wife are both required to sign an instrument.

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "(1) Any unauthorized signature is wholly inoperative as that of the person whose name is signed unless he ratifies it or is precluded from denying it; but it operates as the signature of the unauthorized signer in favor of any person who in good faith pays the instrument or takes it for value.

(2) Any unauthorized signature may be ratified for all purposes of this chapter. Such ratification does not of itself affect any rights of the person ratifying against the actual signer."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

DECISIONS UNDER U.C.C. PRIOR TO 1991 REVISION

Question Whether Checks Cashed Without Authorization — Summary Judgment Improper: The District Court improperly granted summary judgment to bank when it assumed, absent evidence in the record, that checks were cashed by an unauthorized signer. The determination that the signature was unauthorized could not be made without dealing with the rights and liabilities between the signer and the person to whom the checks were originally made out. First Nat'l Bank in Eureka v. Giles, 225 M 467, 733 P2d 357, 44 St. Rep. 407 (1987).

30-3-405. Impostors — fictitious payees.

Official Comment

Source: Section 3-404, U.C.C.

Prior Uniform Statutory Provision: Section 9(3), Uniform Negotiable Instruments Law.

Official Comment to 1991 Amendment:

1. Subsection (a) [subsection (1) of this section] is based on present Section 3-405(1)(a) [30-3-405(1)(a) prior to 1991 revision]. The present provision can be read to mean that the indorsement must be in the exact name of the named payee. Subsection (c) [subsection (3) of this section] requires only that the indorsement be substantially similar. Subsection (a) [subsection (1) of this section] also changes present law in a case in which the impostor is impersonating an agent. Under present Section 3-405(1)(a) [30-3-405(1)(a) prior to 1991 revision], if Impostor impersonates Smith and induces the drawer to draw a check to the order of Smith, Impostor can negotiate the check. If Impostor impersonates Smith, the president of Smith Corporation, and the check is to the order of Smith Corporation, the section does not apply. See the last paragraph of Comment 2 to present Section 3-405 [30-3-405 prior to 1991 revision]. [Comment now deleted.] Proposed subsection (a) [subsection (1) of this section] gives Impostor the power to negotiate the check in both cases.

2. Subsection (b) [subsection (2) of this section] is based in part on present Section 3-405(1)(b) [30-3-405(1)(b) prior to 1991 revision] and in part on N.I.L. Section 9(3). It covers cases in which an instrument is payable to a fictitious or nonexisting person and to cases in which the payee is a real person but the drawer or maker does not intend the payee to have any interest in the instrument. Subsection (b) [subsection (2) of this section] applies to any instrument, but its primary importance is with respect to checks of corporations and other organizations. It also applies to forged check cases. The following cases illustrate subsection (b) [subsection (2) of this section]:

Case #1. Treasurer is authorized to draw checks in behalf of Corporation. Treasurer fraudulently draws a check of Corporation payable to Supplier Co., a non-existent company. Subsection (b) [subsection (2) of this section] applies because Supplier Co. is a fictitious person and because Treasurer did not intend Supplier Co. to have any interest in the check. Under subsection (b)(1) [subsection (2)(a) of this section] Treasurer, as the person in possession of the check, becomes the holder of the check. Treasurer indorses the check in the name "Supplier Co." and deposits it in Depositary Bank. Under subsection (b)(2) and (c)(i) [subsection (2)(b) and (3)(a) of this section], the indorsement is effective to make Depositary Bank the holder and therefore a person entitled to enforce the instrument. Section 3-301 [30-3-301].

Case #2. Same facts as Case #1 except that Supplier Co. is an actual company that does business with Corporation. If Treasurer intended to steal the check when the check was drawn, the result in Case #2 is the same as the result in Case #1. Subsection (b) [subsection (2) of this section] applies because Treasurer did not intend Supplier Co. to have any interest in the check. It does not make any difference whether Supplier Co. was or was not a creditor of Corporation when the check was drawn. If Treasurer did not decide to steal the check until after the check was drawn, the case is covered by Section 3-405 [30-3-420] rather than Section 3-404(b) [30-3-405(2)], but the result is the same. See Case #6 in Comment 3 to Section 3-405 [30-3-420].

Case #3. Checks of Corporation must be signed by two officers. President and Treasurer both sign a check of Corporation payable to Supplier Co., a company that does business with Corporation from time to time but to which Corporation does not owe any money. Treasurer knows that no money is owed to Supplier Co. and does not intend that Supplier Co. have any interest in the check. President believes that money is owed to Supplier Co. Treasurer obtains possession of the check after it is signed. Subsection (b) [subsection (2) of this section] applies because Treasurer is "a person whose intent determines to whom an instrument is payable" and Treasurer does not intend Supplier Co. to have any interest in the check. Treasurer becomes holder of the check and may negotiate it by indorsing it in the name "Supplier Co.".

Case #4. Checks of Corporation are signed by a check-writing machine. Names of payees of checks produced by the machine are determined by information entered into the computer that operates the machine. Thief, a person who is not an employee or other agent of Corporation, obtains access to the computer and causes the check-writing machine to produce a check payable to Supplier Co., a non-existent company. Subsection (b)(ii) [subsection (2) (part) of this section] applies. Thief then obtains possession of the check. At that point Thief becomes the holder of the check because Thief is the person in possession of the instrument. Subsection (b)(1) [subsection (2)(a) of this section]. Under Section 3-301 [30-3-301] Thief, as holder, is the "person entitled to enforce the instrument" even though Thief does not have title to the check and is in wrongful possession of it. Thief indorses the check in the name "Supplier Co." and deposits it in Depositary Bank. Under subsection (b)(2) and (c)(i) [subsections (2)(b) and (3)(a) of this section], the indorsement is effective. The bank becomes the holder and the person entitled to enforce the check. Although the check was issued without authority given by Corporation, the drawee bank is entitled to pay the check and charge Corporation's account under an agreement with

Corporation allowing the bank to debit Corporation's account for payment of checks produced by the check-writing machine whether or not authorized. The indorsement is also effective if Supplier Co. is a real person. In that case subsection (b)(i) [subsection (2)(part) of this section] applies. Under Section 3-110(b) [30-3-126(2)] Thief is the person whose intent determines to whom the check is payable, and Thief did not intend Supplier Co. to have any interest in the check. If the drawee bank pays the check, there is no breach of warranty under Section 3-417(a)(1) [30-3-424(1)(a)] because Depositary Bank was a person entitled to enforce the check when it was forwarded for payment.

Case #5. Thief, who is not an employee or agent of Corporation, steals check forms of Corporation. John Doe is president of Corporation and is authorized to sign checks on behalf of Corporation as drawer. Thief draws a check in the name of Corporation as drawer by forging the signature of Doe. Thief makes the check payable to the order of Supplier Co. with the intention of stealing it. Whether Supplier Co. is a fictitious person or a real person, Thief becomes the holder of the check and the person entitled to enforce it. The analysis is the same as that in Case #4. Thief deposits the check in an account in Depositary Bank which Thief opened in the name "Supplier Co." Thief either indorses the check in an assumed name other than "Supplier Co." or does not indorse the check at all. Under Section 4-205 [30-4-205] a depositary bank may become holder of a check deposited to the account of a customer without the customer's indorsement. Subsection (c)(ii) [subsection (3)(b) of this section] treats deposit to an account in a name substantially similar to that of the payee as the equivalent of indorsement in the name of the payee. Thus, the deposit is an effective indorsement of the check. Depositary Bank becomes the holder of the check and the person entitled to enforce the check. If the check is paid by the drawee bank, there is no breach of warranty under Section 3-417(a)(1) [30-3-424(1)(a)] with respect to the indorsement and, unless Depositary Bank knew about the forgery of Doe's signature, there is no breach of warranty under Section 3-417(a)(3) [30-3-424(1)(c)]. Because the check was a forged check the drawee bank is not entitled to charge Corporation's account unless Section 3-406 [30-3-406] or Section 4-406 [30-4-406] applies.

3. In cases governed by subsection (a) [subsection (1) of this section] the dispute will normally be between the drawer of the check that was obtained by the impostor and the drawee bank that paid it. The drawer is precluded from obtaining recredit of the drawer's account by arguing that the check was paid on a forged indorsement so long as the drawee bank acted in good faith in paying the check. Cases governed by subsection (b) [subsection (2) of this section] are illustrated by Cases #1 through #5 in Comment 2. In Cases #1, #2, and #3 there is no forgery of the check, thus the drawer of the check takes the loss if there is no lack of good faith by the banks involved. Cases #4 and #5 are forged check cases. Depositary Bank is entitled to retain the proceeds of the check if it didn't know about the forgery. Unless Section 3-406 [30-6-406] applies the loss is taken by the drawee bank if a forged check is paid, and that is the result in Case #5. In Case #4 the loss is taken by Corporation, the purported drawer, because an agreement between Corporation and the drawee bank allowed the bank to debit Corporation's account despite the unauthorized use of the check-writing machine. Subsection (d) [subsection (4) of this section] allows the person who suffers a loss as a result of payment of a check covered by subsection (a) or (b) [subsection (1) or (2) of this section] to recover a portion of the loss from a person that pays the check or takes it for value or for collection if that person failed to exercise ordinary care and that failure contributed to the loss. In most cases the defendant will be either the drawee bank or the depositary bank. The person suffering the loss under subsection (a) or (b) [subsection (1) or (2) of this section] has a cause of action against the offending bank to recover a portion of the loss. The amount of loss to be allocated to each party is left to the trier of fact. Ordinary care is defined in Section 3-103(a)(7) [30-3-102(1)(g)].

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "Impostors — signature in name of payee. (1) An endorsement by any person in the name of a named payee is effective if:

(a) an impostor by use of the mails or otherwise has induced the maker or drawer to issue the instrument to him or his confederate in the name of the payee; or

(b) a person signing as or on behalf of a maker or drawer intends the payee to have no interest in the instrument; or

(c) an agent or employee of the maker or drawer has supplied him with the name of the payee intending the latter to have no such interest.

(2) Nothing in this section shall affect the criminal or civil liability of the person so endorsing."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

30-3-406. Negligence contributing to forged signature or alteration of instrument.

Official Comment

Source: Section 3-406, U.C.C.

Official Comment to 1991 Amendment:

1. Proposed Section 3-406(a) [30-3-406(1)] is based on present Section 3-406 [30-3-406 prior to 1991 revision]. With respect to alteration, present Section 3-406 [30-3-406 prior to 1991 revision] adopts the doctrine of Young v. Grote, 4 Bing. 253 (1827), which held that a drawer who so negligently draws an instrument as to facilitate its material alteration is liable to a drawee who pays the altered instrument in good faith. Under Section 3-406 [30-3-406] the doctrine is expanded to apply not only to drafts but to all instrument [sic]. It includes in the protected class any "person that, in good faith, pays the instrument or takes it for value." Section 3-406 [30-3-406] rejects decisions holding that the maker of a note owes no duty of care to the holder because at the time the instrument is issued there is no contract between them. By issuing the instrument and "setting it afloat upon a sea of strangers" the maker or drawer voluntarily enters into a relation with later holders which justifies imposition of a duty of care. In this respect an instrument so negligently drawn as to facilitate alteration does not differ in principle from an instrument containing blanks which may be filled. Under Section 3-407 [30-3-407] a person paying an altered instrument or taking it for value, in good faith and without notice of the alteration may enforce rights with respect to the instrument according to its original terms. If negligence of the obligor substantially contributes to an alteration, this section gives the holder or the payor the alternative right to treat the altered instrument as though it had been issued in the altered form.

No attempt is made to define particular conduct that will constitute "failure to exercise ordinary care [that] substantially contributes to an alteration." Rather, "ordinary care" is defined in Section 3-103(a)(7) [30-3-102(1)(g)] in general terms. The question is left to the court or the jury for decision in the light of the circumstances in the particular case including reasonable commercial standards that may apply.

Section 3-406 [30-3-406] does not make the negligent party liable in tort for damages resulting from the alteration. If the negligent party is estopped from asserting the alteration the person taking the instrument is fully protected because the taker can treat the instrument as having been issued in the altered form.

2. Section 3-406 [30-3-406] applies equally to a failure to exercise ordinary care that substantially contributes to the making of a forged signature on an instrument. Proposed Section 3-406 [30-3-406] refers to "forged signature" rather than "unauthorized signature" that appeared in present Section 3-406 [30-3-406 prior to 1991 revision] because it more accurately describes the scope of the provision. Unauthorized signature is a broader concept that includes not only forgery but also the signature of an agent which does not bind the principal under the law of agency. The agency cases are resolved independently under agency law. Section 3-406 [30-3-406] is not necessary in those cases.

The "substantially contributes" test of present Section 3-406 [30-3-406 prior to 1991 revision] is continued in this section in preference to a "direct and proximate cause" test. The "substantially contributes" test is meant to be less stringent than a "direct and proximate cause" test. Under the less stringent test the preclusion should be easier to establish. Conduct "substantially contributes" to a material alteration or forged signature if it is a contributing cause of the alteration or signature and a substantial factor in bringing it about. Since Section 3-404(d) [30-3-405(4)] and Section 3-405(b) [30-3-420(2)] also use the words "substantially contributes" the analysis of these words also applies to those provisions.

3. The following cases illustrate the kind of conduct that can be the basis of a preclusion under Section 3-406(a) [30-3-406(1)]:

Case #1. Employer signs checks drawn on Employer's account by use of a rubber stamp of Employer's signature. Employer keeps the rubber stamp along with Employer's personalized blank check forms in an unlocked desk drawer. An unauthorized person fraudulently uses the check forms to write checks on Employer's account. The checks are signed by use of the rubber stamp. If Employer demands that Employer's account in the drawee bank be recredited because the forged check was not properly payable, the drawee bank may defend by asserting that Employer is precluded from asserting the forgery. The trier of fact could find that Employer failed to exercise ordinary care to safeguard the rubber stamp and the check forms and that the failure substantially contributed to the forgery of Employer's signature by the unauthorized use of the rubber stamp.

Case #2. An insurance company draws a check to the order of Sarah Smith in payment of a claim of a policyholder, Sarah Smith, who lives in Alabama. The insurance company also has a policyholder with the same name who lives in Illinois. By mistake, the insurance company mails the check to the Illinois Sarah Smith who indorses the check and obtains payment. Because the payee of the check is the Alabama Sarah Smith, the indorsement by the Illinois Sarah Smith is a forged indorsement. Section 3-110(a) [30-3-126(1)]. The trier of fact could find that the insurance company failed to exercise ordinary care when it mailed the check to the wrong person and that the failure substantially contributed to the making of the forged indorsement. In that event the insurance company could be precluded from asserting the forged indorsement against the drawee bank that honored the check.

Case #3. A company writes a check for $10. The figure "10" and the word "ten" are typewritten in the appropriate spaces on the check form. A large blank space is left after the figure and the word. The payee of the check, using a typewriter with a typeface similar to that used on the check, writes the word "thousand" after the word "ten" and a comma and three zeros after the figure "10". The drawee bank in good faith pays $10,000 when the check is presented for payment and debits the account of the drawer in that amount. The trier of fact could find that the drawer failed to exercise ordinary care in writing the check and that the failure substantially contributed to the alteration. In that case the drawer is precluded from asserting the alteration against the drawee if the check was paid in good faith.

4. Subsection (b) [subsection (2) of this section] differs from present Section 3-406 [30-3-406 prior to 1991 revision] in that it adopts a concept of comparative negligence. If the person precluded under subsection (a) [subsection (1) of this section] proves that the person asserting the preclusion failed to exercise ordinary care and that failure contributed to the loss, the loss may be allocated between the two parties on a comparative negligence basis. For example, in an altered check case there may be an issue whether the depositary bank might have prevented the loss if its employee had examined the check more carefully to detect the alteration. In a forged indorsement case there may be an issue whether the depositary bank should have been alerted to possible fraud when a new account is opened for a corporation shortly before a very large check payable to a payee with the same name is deposited. Circumstances surrounding the opening of the account may have suggested that the corporation to which the check was payable may not be the same as the corporation for which the account was opened. In each of these cases the relative negligence of each of the parties can be weighed by the trier of fact.

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "Negligence contributing to alteration or unauthorized signature. Any person who by his negligence substantially contributes to a material alteration of the instrument or to the making of an unauthorized signature is precluded from asserting the alteration or lack of authority against a holder in due course or against a drawee or other payor who pays the instrument in good faith and in accordance with the reasonable commercial standards of the drawee's or payor's business."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

DECISIONS UNDER U.C.C. PRIOR TO 1991 REVISION

Negotiation of Check Endorsed by Someone Other Than Payee Held Not Commercially Reasonable: Defendant payor bank negotiated a check endorsed by someone other than the payee. District Court denied plaintiff drawer's motion for summary judgment. On appeal, the Supreme Court reversed and held that summary judgment was proper on this issue because the bank's action was not commercially reasonable as a matter of law. Eatinger v. First Nat'l Bank of Lewistown, 199 M 377, 649 P2d 1253, 39 St. Rep. 1465 (1982).

30-3-407. Alteration.

Official Comment

Source: Section 3-407, U.C.C.

Prior Uniform Statutory Provision: Sections 14, 15, 124 and 125, Uniform Negotiable Instruments Law.

Official Comment to 1991 Amendment:

1. This provision restates present Section 3-407 [30-3-407 prior to 1991 revision]. Present Section 3-407 [30-3-407 prior to 1991 revision] defines a "material" alteration as any alteration that changes the contract of the parties in any respect. Proposed Section 3-407 [30-3-407] refers

to such a change as an alteration. As under subsection (2) of present Section 3-407 [30-3-407(2) prior to 1991 revision], discharge because of alteration occurs only in the case of an alteration fraudulently made. There is no discharge if a blank is filled in the honest belief that it is authorized or if a change is made with a benevolent motive such as a desire to give the obligor the benefit of a lower interest rate. Changes favorable to the obligor are unlikely to be made with any fraudulent intent, but if such an intent is found the alteration may operate as a discharge.

Discharge is a personal defense of the party whose obligation is modified and anyone whose obligation is not affected is not discharged. But if an alteration discharges a party there is also discharge of any party having a right of recourse against the discharged party because the obligation of the party with the right of recourse is affected by the alteration. Assent to the alteration given before or after it is made will prevent the party from asserting the discharge. The phrase "or is precluded from asserting the defense" in subsection (b) [subsection (2) of this section] recognizes the possibility of an estoppel or other ground barring the defense which does not rest on assent.

2. Under subsection (c) [subsection (3) of this section] a person paying a fraudulently altered instrument or taking it for value, in good faith and without notice of the alteration, is not affected by a discharge under subsection (b) [subsection (2) of this section]. The person paying or taking the instrument may assert rights with respect to the instrument according to its original terms or, in the case of an incomplete instrument that is altered by unauthorized completion, according to its terms as completed. If blanks are filled or an incomplete instrument is otherwise completed, subsection (c) [subsection (3) of this section] places the loss upon the party who left the instrument incomplete by permitting enforcement in its completed form. This result is intended even though the instrument was stolen from the maker or drawer and completed after the theft.

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "(1) Any alteration of an instrument is material which changes the contract of any party thereto in any respect, including any such change in:

(a) the number or relations of the parties; or

(b) an incomplete instrument, by completing it otherwise than as authorized; or

(c) the writing as signed, by adding to it or by removing any part of it.

(2) As against any person other than a subsequent holder in due course:

(a) alteration by the holder which is both fraudulent and material discharges any party whose contract is thereby changed unless that party assents or is precluded from asserting the defense;

(b) no other alteration discharges any party and the instrument may be enforced according to its original tenor, or as to incomplete instruments according to the authority given.

(3) A subsequent holder in due course may in all cases enforce the instrument according to its original tenor, and when an incomplete instrument has been completed, he may enforce it as completed."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

DECISIONS UNDER UNIFORM NEGOTIABLE INSTRUMENTS LAW

Material Alterations: In conviction of grand larceny, in which defendant had stolen and subsequently cashed check, the tearing of the check and its repair did not constitute spoliation under section 55-907, R.C.M. 1947 (now repealed), so as to make the check a nonnegotiable instrument. St. v. Romero, 146 M 77, 404 P2d 500 (1965).

Marks of Alteration: Where a check on its face showed signs of alteration, the figures having been written with different pencil than balance of writing and the surface of paper underlying such figures bearing unmistakable signs of erasure so that alteration appeared suspicious, it would not be presumed that alteration was made prior to delivery and with assent of maker. Miles City Bank v. Askin, 119 M 581, 179 P2d 750, 171 ALR 790 (1947).

Negligence: Where an alteration of a check is so obvious as to impart notice thereof to bank cashing for payee, a finding is authorized that bank's action amounted to bad faith toward maker or at least gross negligence. Miles City Bank v. Askin, 119 M 581, 179 P2d 750, 171 ALR 790 (1947).

Holder in Due Course: Where check has been materially altered after its execution and delivery and holder is a holder in due course, not a party to the alteration, holder may recover on check according to its original tenor as established by evidence. Miles City Bank v. Askin, 119 M 581, 179 P2d 750, 171 ALR 790 (1947).

Recovery From Endorser: Where a check is paid on a forged endorsement by a bank other than the drawee, and there is no estoppel to assert the forgery, the rights of the drawee bank against the paying bank on its endorsement are fixed by sections 65 and 66 of the UNIL not by 55-906, R.C.M. 1947 (now repealed). First Nat'l Bank of Miles City v. Fed. Reserve Bank of Minneapolis, 88 M 589, 294 P 1105 (1931).

30-3-409. Drawee not liable on unaccepted draft.

Official Comment

Source: Section 3-408, U.C.C.

Prior Uniform Statutory Provision: Sections 127 and 189, Uniform Negotiable Instruments Law.

Official Comment to 1991 Amendment:

1. This section is a restatement of present Section 3-409(1) [30-3-409(1) prior to 1991 revision]. Subsection (2) of present Section 3-409 [30-3-409(2) prior to 1991 revision] is deleted as misleading and superfluous. Comment 3 says of [present] subsection (2) [30-3-409(2) prior to 1991 revision]: "It is intended to make it clear that this section does not in any way affect any liability which may arise apart from the instrument." [Comment now deleted.] In reality [present] subsection (2) [30-3-409(2) prior to 1991 revision] has not made anything clear and has been a source of confusion. If all it means is that a bank that has not certified a check may engage in other conduct that might make it liable to a holder, it states the obvious and is superfluous. Section 1-103 [30-1-102] is adequate to cover those cases. But some courts have mistakenly looked to present Sections 3-409(2) [30-3-409(2) prior to 1991 revision] for substantive content, and it offers none. For instance, in Graybar Electric Co., Inc., v. Brookline Trust Co., 39 UCC Rep. Serv. 1721 (Mass. 1984), the court cited [present] Section 3-409(2) [30-3-409(2) prior to 1991 revision] to show that a bank may be liable on a personal money order without an express acceptance because of an implied representation that it intends to accept.

2. Liability with respect to drafts may arise under other law. For example, Section 4-302 [30-4-302] imposes liability on a payor bank for late return of an item.

Compiler's Comments

1991 Amendment: Substituted current catchline for former catchline that read: "Draft not an assignment"; deleted former (2) that read: "(2) Nothing in this section shall affect any liability in contract, tort or otherwise arising from any letter of credit or other obligation or representation which is not an acceptance"; and made minor changes in style.

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

DECISIONS UNDER U.C.C. PRIOR TO 1991 REVISION

Lack of Consideration or Setoff: There was no issue of material fact precluding summary judgment, either of lack of consideration or of setoff, because the express language of the note sued on stated that consideration existed, and the second action was a personal claim unrelated to the note. Keller v. Llewellyn, 175 M 164, 573 P2d 166 (1977).

DECISIONS UNDER UNIFORM NEGOTIABLE INSTRUMENTS LAW

Novation: Where there was fraud and partial failure of consideration in that makers of original note never received from payees part of loan for which note was given, execution of renewal note to payees did not cut off defenses under original note. Jensen v. Franklin, 135 M 341, 340 P2d 832 (1959).

Question for Jury:

In action by payees against makers for balance due on renewal note, wherein makers contended that $1,000 makers never received on $20,000 loan was to represent drawing account for makers, and payees contended that the $1,000 represented payees' share of profits from purchase of machinery at reduced rate, question whether there had been partial failure of consideration because makers never received $1,000 was for jury. Jensen v. Franklin, 135 M 341, 340 P2d 832 (1959).

Where a defendant sets up want of consideration and the evidence is conflicting, the question of consideration becomes one for the jury. Stagg v. Stagg, 96 M 573, 32 P2d 856 (1934); Miles Sav. Bank v. Liquin & Swandal, 90 M 513, 4 P2d 482 (1931); Fifty Associates Co. v. Quigley, 56 M 348, 185 P 155 (1919).

Partial Failure: In action by payees for balance due on renewal note wherein makers who had borrowed money and given note and renewal note therefor to payees alleged in answer that payees misrepresented amount due on original note and that makers believed the representations and executed renewal note for more than correct amount, answer sufficiently alleged elements of fraud and partial failure of consideration, which would be defense pro tanto. Jensen v. Franklin, 135 M 341, 340 P2d 832 (1959).

Evidence of Prior Indebtedness: When defendant signed written guaranty to pay for goods sold by plaintiff to a codefendant and thereafter, while unpaid indebtedness remained on this contract a "renewal contract" was executed by the same parties, in action against guarantor on second contract where defense was lack of consideration, the first contract was admissible to prove consideration for the second, since it showed the guarantor's prior indebtedness, a valid consideration under section 55-302, R.C.M. 1947 (now repealed). W. T. Rawleigh Co. v. Miller, 105 M 456, 73 P2d 552 (1937).

Promissory Note Constitutes Valuable Consideration: A promissory note given in consideration of an oil and gas lease was a valuable consideration, and the fact that the lessor more than a year after its delivery returned it to the lessee was immaterial; it having been the property of the lessor, he could do with it as he saw fit. Nadeau v. The Texas Co., 104 M 558, 69 P2d 586 (1937).

Transfer to Secure Antecedent Debt: While the cancellation or satisfaction of an antecedent debt constitutes a sufficient consideration for a transfer under section 55-302, R.C.M. 1947 (now repealed), and may make the transferee a bona fide purchaser, the mere transfer of property to secure an antecedent debt does not make the transferee an innocent purchaser. Rasmussen v. Lee & Co., Inc., 104 M 278, 66 P2d 119 (1937).

Pleading Want of Consideration:

Under section 55-305, R.C.M. 1947 (now repealed), absence of consideration is a matter of defense as against any person not a holder in due course. This is an affirmative defense and must be pleaded. Sommer v. Wigen, 103 M 327, 62 P2d 333 (1936).

In an action by the payee of a promissory note against the maker, defendant's general averment that the note "was executed without any consideration whatever and there was a total absence and failure of consideration" was sufficient without setting out the evidentiary facts upon which defendant relied. U.S. Nat'l Bank of Red Lodge v. Chappell, 71 M 553, 230 P 1084 (1924).

Presumption of Continued Existence: In view of the ease with which a note and mortgage may be transferred without the necessity of making a public record thereof, the presumption that a thing once shown to have existed will be presumed to have continued as long as is usual with things of that nature (26-1-602), standing alone was too weak as proof of ownership to establish a prima facie case of want or absence of consideration after 15 years. Sommer v. Wigen, 103 M 327, 62 P2d 333 (1936).

Validity of Original Note: The surrender of a note which was obtained through undue influence or misrepresentation does not constitute any consideration for a new note. Stagg v. Stagg, 96 M 573, 32 P2d 856 (1934).

Effect of Words "Value Received": The words "value received" import consideration. Miles Sav. Bank v. Liquin & Swandal, 90 M 513, 4 P2d 482 (1931).

Preexisting Debt:

A preexisting debt constitutes value and, therefore, the surrender of an old promissory note upon execution of one to take its place is a sufficient consideration for the latter, and the fact that the obligation surrendered is that of another person is immaterial. First St. Bank of Philipsburg v. Mussigbrod, 83 M 68, 271 P 695 (1928).

An antecedent or preexisting debt constitutes value, and therefore one who takes property in satisfaction of such a debt is a purchaser for value and entitled to full protection as such. Hackney v. Birely, 67 M 155, 215 P 642 (1923); Schauer v. Morgan, 67 M 455, 216 P 347 (1923); Mulany v. Murray, 68 M 245, 216 P 1105 (1923).

Burden of Proof:

The burden of showing a want of consideration to support a written instrument lies with the party seeking to invalidate it on that ground, the presumption being that there was a consideration. Farmers & Miners' St. Bank v. Probst, 81 M 248, 263 P 693 (1928).

In an action on a promissory note against the maker, plaintiff is not required to prove consideration, a note being deemed to have been issued for a valuable consideration, and absence of it being a matter of defense. Alley v. Butte & W. Min. Co., 77 M 477, 251 P 517 (1926).

Partially Valid Consideration: A note given in aid of a contract which is invalid under the Statute of Frauds is without consideration and payment thereof cannot be enforced; but where only a portion of a note is given in payment of such a void contract, the remaining portion being based upon a valid consideration, payment may be enforced as to such latter portion. Eccles v. Kendrick, 80 M 120, 259 P 609 (1927).

Extension of Time as Consideration: Where the vendor of land accepted a note in payment of interest past due on a deferred payment of the purchase price, he waived the right given him under the contract of sale to declare the contract terminated by its breach, and extended the time in which the amount might be paid, and such extension was a sufficient consideration for the note. Edwards v. Muri, 73 M 339, 237 P 209 (1925).

Sufficiency of Consideration: Where plaintiff, in possession of public land under a claim of right to desert entry and upon which he had made improvements consisting of about 3 miles of fencing, located defendants thereon, delivered possession and surrendered the improvements to them, defendants giving a note for $650 in payment, there was sufficient consideration for the instrument. McConnell v. Blackley, 66 M 510, 214 P 64 (1923).

Detriment to Promisee: Detriment to the promisee is sufficient consideration. Ford v. Drake, 46 M 314, 127 P 1019 (1912).

Notes Generally: In the case of a note which is negotiable in form consideration is presumed. Ford v. Drake, 46 M 314, 127 P 1019 (1912).

Note of Bank Officer: The note of a bank officer in substitution for assets withdrawn rests on good consideration. St. Bank v. Forsyth, 41 M 249, 108 P 914, 28 L.R.A., N.S. 501 (1910).

Agreement as to Nonliability: A promissory note made and executed without consideration and received by the payee under an agreement that the maker shall never be called on to pay the same cannot be enforced against the maker in an action by the payee. St. Bank v. Forsyth, 41 M 249, 108 P 914, 28 L.R.A., N.S. 501 (1910).

Forbearance to Sue: Forbearance to sue is a good consideration for a negotiable instrument, but the claim must be enforceable to make forbearance good consideration. Bank of Ontario v. Hoskins, 33 M 306, 83 P 493 (1905).

30-3-410. Acceptance of draft — certified check.

Official Comment

Source: Section 3-409, U.C.C.

Prior Uniform Statutory Provision: Sections 132, 133, 134, 135, 136, 137, 138, 161—170, and 191, Uniform Negotiable Instruments Law.

Official Comment to 1991 Amendment:

1. The first three subsections of Section 3-409 [30-3-410] are a restatement of present Section 3-410 [30-3-410 prior to 1991 revision]. Subsection (d) [subsection (4) of this section] adds a definition of certified check which is a type of accepted draft.

2. Subsection (a) [subsection (1) of this section] states the generally recognized rule that the mere signature of the drawee on the instrument is a sufficient acceptance. Customarily the signature is written vertically across the face of the instrument, but since the drawee has no reason to sign for any other purpose a signature in any other place, even on the back of the instrument, is sufficient. It need not be accompanied by such words as "Accepted," "Certified," or "Good." It must not, however, bear any words indicating an intent to refuse to honor the draft. The last sentence of subsection (a) [subsection (1) of this section] states the generally recognized rule that an acceptance written on the draft takes effect when the drawee notifies the holder or gives notice according to instructions.

3. The purpose of subsection (c) [subsection (3) of this section] is to provide a definite date of payment if none appears on the instrument. An undated acceptance of a draft payable "thirty days after sight" is incomplete. Unless the acceptor writes in a different date the holder is authorized to complete the acceptance according to the terms of the draft by supplying a date of presentment. Any date which the holder chooses to write in is effective providing the choice of date is made in good faith.

4. The last sentence of subsection (d) [subsection (4) of this section] states the generally recognized rule that in the absence of agreement a bank is under no obligation to certify a check. A check is a demand instrument calling for payment rather than acceptance. The bank may be liable for breach of any agreement with the drawer, the holder, or any other person by which it undertakes to certify. Its liability is not on the instrument, since the drawee is not so liable until acceptance. Section 3-408 [30-3-409]. Any liability is for breach of the separate agreement.

Compiler's Comments

1991 Amendment: Substituted current catchline for former catchline that read: "Definition and operation of acceptance"; in (1), near middle of first sentence after "signed", substituted "agreement to pay a" for "engagement to honor the" and substituted last sentence relating to time and effect of acceptance for former sentence that read: "It becomes operative when completed by delivery or notification"; inserted (4) defining certified check; and made minor changes in style.

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

DECISIONS UNDER U.C.C. PRIOR TO 1991 REVISION

Supply of Presentment Date by Holder: The holder of a 160-day sight draft may supply a date of presentment when the drawee fails to provide his written acceptance or date thereof. Thus, the holder of the draft could in good faith treat the date on which the collecting bank acknowledged receipt of the draft as the date of acceptance and could properly treat the draft as dishonored when payment was received 162 days after the date the draft was received from the bank. Clawson v. Berklund, 188 M 48, 610 P2d 1168 (1980).

DECISIONS UNDER UNIFORM NEGOTIABLE INSTRUMENTS LAW

Burden of Proof: In the absence of proof showing the length of time for which the check in this action was held by the bank upon which drawn before returning it dishonored, the contention of defendant drawer that the bank having held it for more than 24 hours, his obligation thereon was discharged under this section, may not be sustained; the burden of proving payment in this manner having been upon him. Cellars v. Dwinnell, 87 M 73, 285 P 181 (1930).

Application to Checks: The provisions of sections 55-1105 and 55-1106, R.C.M. 1947 (now repealed), (Uniform Negotiable Instruments Law), that the drawee of a bill of exchange is allowed 24 hours after presentment in which to decide whether he will or will not accept it, and will be deemed to have accepted it if he fails to return it within that time, are applicable to a check which, under section 55-1702, R.C.M. 1947 (now repealed), is declared to be a bill of exchange drawn on a bank. Blackwelder v. Fergus Motor Co., 80 M 374, 260 P 734 (1927); Clarke v. Nat'l Bank of Mont., 78 M 48, 252 P 373 (1926).

Time of Retention: Failure of the drawee bank to return a check within 24 hours as "nonaccepted" constitutes acceptance and creates debtor and creditor relation between the payee and the drawee bank. Blackwelder v. Fergus Motor Co., 80 M 374, 260 P 734 (1927).

30-3-412. Acceptance varying draft.

Official Comment

Source: Section 3-410, U.C.C.

Prior Uniform Statutory Provision: Sections 139, 140, 141 and 142, Uniform Negotiable Instruments Law.

Official Comment to 1991 Amendment:

1. This section is a restatement of present Section 3-412 [30-3-412 prior to 1991 revision]. It applies to conditional acceptances, acceptances for part of the amount, acceptances to pay at a different time from that required by the draft, or to the acceptance of less than all of the drawees. It applies to any other engagement changing the essential terms of the draft. If the drawee makes a varied acceptance the holder may either reject it or assent to it. The holder may reject by insisting on acceptance of the draft as presented. Refusal by the drawee to accept the draft as presented is dishonor. In that event the drawee is not bound by the varied acceptance and is entitled to have it canceled.

If the holder assents to the varied acceptance, the drawee's obligation as acceptor is according to the terms of the varied acceptance. Under subsection (c) [subsection (3) of this section] the effect of the holder's assent is to discharge any drawer or indorser who does not also assent. The assent of the drawer or indorser must be affirmatively expressed. Mere failure to object within a reasonable time is not assent which will prevent the discharge.

2. Under subsection (b) [subsection (2) of this section] an acceptance does not vary from the terms of the draft if it provides for payment at any particular bank or place in the United States unless the acceptance states that the draft is to be paid only at such bank or place. Section 3-501(b)(1) [30-3-504(2)(a)] states that if an instrument is payable at a bank in the United States presentment must be made at the place of payment (Section 3-111 [30-3-127]) which in this case is at the designated bank.

Compiler's Comments

1991 Amendment: In (1), at beginning, substituted "If the terms of a drawee's acceptance vary from the terms of" for "Where the drawee's proffered acceptance in any manner varies" and at end of second sentence substituted "may cancel the acceptance" for "is entitled to have his acceptance canceled"; and in (3), after "draft", inserted "the obligation of" and near end substituted "expressly assent to the acceptance" for "affirmatively assent".

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

30-3-413. Obligation of maker.

Official Comment

Source: Section 3-412, U.C.C.

Prior Uniform Statutory Provision: Sections 60, 61 and 62, Uniform Negotiable Instruments Law.

Official Comment to 1991 Amendment:

1. The obligations of the maker, acceptor, drawer, and indorser are stated in four separate sections. Proposed Section 3-412 [30-3-413] states the obligation of the maker and is consistent with present Section 3-413(1) [30-3-413(1) prior to 1991 revision]. Under proposed Section 3-105(b) [30-3-125(2)] nonissuance of either a complete or incomplete instrument is a defense by a maker or drawer against a person that is not a holder in due course.

2. The obligation of the maker may be modified in the case of alteration if, under Section 3-406 [30-3-406], the maker is precluded from asserting the alteration.

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "Contract of maker, drawer and acceptor. (1) The maker or acceptor engages that he will pay the instrument according to its tenor at the time of his engagement or as completed pursuant to 30-3-115 on incomplete instruments.

(2) The drawer engages that upon dishonor of the draft and any necessary notice of dishonor or protest he will pay the amount of the draft to the holder or to any endorser who takes it up. The drawer may disclaim this liability by drawing without recourse.

(3) By making, drawing or accepting the party admits as against all subsequent parties including the drawee the existence of the payee and his then capacity to endorse."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

DECISIONS UNDER U.C.C. PRIOR TO 1991 REVISION

Partial Enforcement of Promissory Note: Respondent signed a promissory note to her former husband in the amount of $2,000. She did not make any payments on the note. At trial, she testified that the only consideration she had received for the note was $1,000 and the use of a pickup. Thus, the lower court's decision to enforce the note only partially was not clearly erroneous. In re Marriage of Jones, 218 M 441, 709 P2d 158, 42 St. Rep. 1722 (1985).

Effective Date of Disability Insurance: Disability insurance, subject to acceptance by the insurer, commences on the date when the debtor becomes obligated to the creditor. A promissory note takes effect from the time of its delivery. The promissory note was considered delivered at the time it was mailed to the bank. The note thereupon became the property of the payee when it was posted to the bank. It was beyond the control of the makers at that time. The time of mailing therefore became the "time of his engagement" under 30-3-413 fixing the liability of the maker. It was at that time that the insured became obligated to the creditor under 33-21-204, and the disability insurance financed by the note became effective. First Sec. Bank v. Goddard, 181 M 407, 593 P2d 1040 (1979).

Out-of-State Bank Not Party to Be Joined: Interest in loans transferred to out-of-state bank under participation agreement between lending Montana bank and out-of-state bank prior to commencement of action does not make out-of-state bank true party in interest or person to be joined if feasible when borrower sued on loan agreement and notes payable to lending Montana bank because loan agreement only establishes rights and liabilities between lending Montana bank and borrower, while participation agreement only establishes rights and liabilities between lending Montana bank and out-of-state bank. Neither establishes any contractual relationship, rights or liabilities between borrower and out-of-state bank. Additionally lending Montana bank is owner and sole payee on notes and as holder of notes is entitled to sue in its own name. State ex rel. Drum v. District Court, 169 M 494, 548 P2d 1377 (1976).

DECISIONS UNDER UNIFORM NEGOTIABLE INSTRUMENTS LAW

Absolute and Contingent Liability: The liability of the maker of a promissory note is absolute, while that of an endorser is contingent upon the default of the maker. Anderson v. Border, 75 M 516, 244 P 494 (1926).

Existence and Capacity of Payee: By making a promissory note to a corporation the maker admits the payee's corporate existence and its capacity to endorse. Commercial Nat'l Bank of Great Falls v. Reichelt, 62 M 302, 204 P 1037 (1922).

30-3-414. Obligation of indorser.

Official Comment

Source: Section 3-415, U.C.C.

Prior Uniform Statutory Provision: Sections 38, 44, 66, 67 and 68, Uniform Negotiable Instruments Law.

Official Comment to 1991 Amendment:

1. Subsection (a) and (b) [subsections (1) and (2) of this section] restate the substance of present Section 3-414(1) [30-3-414(1) prior to 1991 amendment]. Subsection (2) of present Section 3-414 [30-3-414 prior to 1991 revision] has been dropped because it is superfluous. Although notice of dishonor is not mentioned in subsection (a) [subsection (1) of this section], it must be given in some cases to charge an indorser. It is covered in subsection (c) [subsection (3) of this section].

2. Proposed Section 3-503 [30-3-508] states when notice of dishonor is required and how it must be given. If required notice of dishonor is not given in compliance with Section 3-503 [30-3-508], subsection (c) of Section 3-415 [30-3-414(3)] states that the effect is to discharge the indorser's obligation.

3. Subsection (d) [subsection (4) of this section] is similar in effect to Section 3-414(b) [30-3-423(2)]. See Comment 2 to Section 3-414 [30-3-423]. If a draft is indorsed after it is accepted by a bank, the indorser incurs the obligation stated in subsection (a) [subsection (1) of this section].

4. Subsection (e) [subsection (5) of this section] modifies present Section 3-503(2)(b) [30-3-503(2)(b) prior to 1991 revision] and Section 3-502(1)(a) [30-3-502(1)(a) prior to 1991 revision] by stating a 30-day rather than a seven-day period, and stating it as an absolute rather than a presumptive period.

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "Contract of endorser — order of liability. (1) Unless the endorsement otherwise specifies (as by such words as "without recourse") every endorser engages that upon dishonor and any necessary notice of dishonor and protest he will pay the instrument according to its tenor at the time of his endorsement to the holder or to any subsequent endorser who takes it up, even though the endorser who takes it up was not obligated to do so.

(2) Unless they otherwise agree endorsers are liable to one another in the order in which they endorse, which is presumed to be the order in which their signatures appear on the instrument."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

DECISIONS UNDER UNIFORM NEGOTIABLE INSTRUMENTS LAW

Nonnegotiable Instrument:

A promissory note, negotiable on its face, executed prior to the 1923 amendment of section 55-205, R.C.M. 1947 (now repealed), was nonnegotiable when secured by a mortgage on real property, and the assignee of the mortgage with the note endorsed in blank, taking it with full knowledge that it was a mortgage note, took it as a nonnegotiable instrument. Barnes v. Rowles, 84 M 393, 276 P 15, 79 ALR 717 (1929).

The provisions of section 55-607, R.C.M. 1947 (now repealed), prescribing the extent of the liability of a general endorser, relate only to negotiable instruments; hence the blank endorsement of a nonnegotiable note did not carry with it a legal liability on the part of the endorser to pay the amount of the note, in the absence of a special agreement to pay, and the holding of the court in an action to foreclose that plaintiffs were not entitled to a deficiency judgment as against him was correct. Barnes v. Rowles, 84 M 393, 276 P 15, 79 ALR 717 (1929).

Independent Contract: The contract of an endorser is separate and distinct from the contract expressed by the note. Morgan v. Huffman, 76 M 396, 247 P 326 (1926).

30-3-415. Instruments signed for accommodation.

Official Comment

Source: Section 3-419, U.C.C.

Prior Uniform Statutory Provision: Sections 28, 29 and 64, Uniform Negotiable Instruments Law.

Official Comment to 1991 Amendment:

1. An accommodation party is a person who signs an instrument to benefit the accommodated party either by signing at the time value is obtained by the accommodated party or later, and who is not a direct beneficiary of the value obtained. An accommodation party will usually be

a co-maker or anomalous indorser. Subsection (a) [subsection (1) of this section] distinguishes between direct and indirect benefit. For example, if X cosigns a note of Corporation that is given for a loan to Corporation, X is an accommodation party if no part of the loan was paid to X or for X's direct benefit. This is true even though X may receive indirect benefit from the loan because X is employed by Corporation or is a stockholder of Corporation, or even if X is the sole stockholder so long as Corporation and X are recognized as separate entities.

2. It does not matter whether an accommodation party signs gratuitously either at the time the instrument is issued or after the instrument is in the possession of a holder. Subsection (b) of Section 3-419 [30-3-415(2)] takes the view stated in Comment 3 [now deleted] to present Section 3-415 [30-3-415 prior to 1991 revision] that there need be no consideration running to the accommodation party: "The obligation of the accommodation party is supported by any consideration for which the instrument is taken before it is due. Subsection (2) [subsection (2) of this section prior to 1991 revision] is intended to change occasional decisions holding that there is no sufficient consideration where an accommodation party signs a note after it is in the hands of a holder who has given value. The [accommodation] party is liable to the holder in such a case even though there is no extension of time or other concession."

3. Whether a person is an accommodation party is a question of fact that is discussed in Comment 1. But it is almost always the case that a co-maker who signs with words of guaranty after the signature is an accommodation party. The same is true of an anomalous indorser. In either case a person taking the instrument is put on notice of the accommodation status of the co-maker or indorser. This is relevant to Section 3-605(g) [30-3-607(7)]. But, under subsection (c) [subsection (3) of this section], signing with words of guaranty or as an anomalous indorser also creates a presumption that the signer is an accommodation party. A party challenging accommodation party status would have to rebut this presumption by producing evidence that the signer was in fact a direct beneficiary of the value given for the instrument.

4. Subsection (b) [subsection (2) of this section] states that an accommodation party is liable on the instrument in the capacity in which the party signed the instrument. In most cases that capacity will be either that of a maker or indorser of a note. But subsection (d) [subsection (4) of this section] provides a limitation on subsection (b) [subsection (2) of this section]. If the signature of the accommodation party is accompanied by words indicating unambiguously that the party is guaranteeing collection rather than payment of the instrument, liability is limited to that stated in subsection (d) [subsection (4) of this section], which is based on present Section 3-416(2) [30-3-416(2) prior to 1991 revision].

Present Article 3 [Title 30, chapter 3, prior to 1991 revision] is confusing because the obligation of a guarantor is covered both in Section 3-415 [30-3-414] and in Section 3-416 [30-3-417]. The latter section suggests that a signature accompanied by words of guaranty creates an obligation distinct from that of an accommodation party. Proposed Article 3 [Title 30, chapter 3] eliminates that confusion by stating the obligation of a guarantor only in Section 3-419 [30-3-415]. Portions of present Section 3-416 [30-3-416, now repealed] are preserved. Present Section 3-416(2) [30-3-416, now repealed] is reflected in proposed Section 3-419(d) [30-3-415(4)] and present Section 3-416(4) [30-3-416, now repealed] is reflected in proposed Section 3-419(c) [30-3-415(3)].

5. Subsection (e) [subsection (5) of this section] restates subsection (5) of present subsection [sic] 3-415 [30-3-415(5) prior to 1991 revision]. Since the accommodation party that pays the instrument is entitled to enforce the instrument against the accommodated party, the accommodation party also obtains rights to any security interest or other collateral that secures payment of the instrument.

Compiler's Comments

1993 Amendment: Chapter 10 in (1), after "another", substituted "party" for "part".

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "Contract of accommodation party. (1) An accommodation party is one who signs the instrument in any capacity for the purpose of lending his name to another party to it.

(2) When the instrument has been taken for value before it is due the accommodation party is liable in the capacity in which he has signed even though the taker knows of the accommodation.

(3) As against a holder in due course and without notice of the accommodation oral proof of the accommodation is not admissible to give the accommodation party the benefit of discharges dependent on his character as such. In other cases the accommodation character may be shown by oral proof.

(4) An endorsement which shows that it is not in the chain of title is notice of its accommodation character.

(5) An accommodation party is not liable to the party accommodated, and if he pays the instrument has a right of recourse on the instrument against such party."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

DECISIONS UNDER UNIFORM NEGOTIABLE INSTRUMENTS LAW

Impairment of Collateral — Defenses of Accommodation Maker: A Shaklee distributor negotiated with Storms Trust for a $10,000 loan to increase his inventory. Trustee Storms drafted a promissory note but refused to approve the loan until the distributor's wife had signed the note. The agreement granted Storms a security interest in the purchased inventory, yet Storms failed to record the security agreement. The distributor subsequently secured a second loan from a bank, which filed a financing statement on the inventory. The distributor defaulted on both loans. Storms took possession of the inventory but relinquished possession upon the bank's demand. Storms obtained a judgment against both the distributor and his wife. Wife appealed a District Court judgment for the full balance due on the promissory note and contract, contending she was discharged from liability on the note because Storms failed to perfect a security interest in the inventory, causing an impairment of collateral. Storms argued the wife was primarily liable as co-maker without benefit of defenses. The court stated that the law discharges all parties who occupy the position of a surety, including accommodation makers, endorsers, and acceptors. At the note signing, Storms had notice that the wife signed merely to aid her husband in obtaining the loan. Therefore, the wife was an accommodation maker entitled to the benefit of the defense of discharge. Storms' failure to perfect his security interest resulted in its loss to another secured party and entitled the wife to a discharge to the extent of the collateral's value. El-Ce Storms Trust v. Svetahor, 223 M 113, 724 P2d 704, 43 St. Rep. 1575 (1986).

Exoneration by Death of Surety: Where deceased had previously cosigned a promissory note for the purpose of lending his name to another party, he became an accommodation maker. As such he is primarily responsible for the payment of the note, without necessity of resort to the principal, and it was error for the District Court to disallow the holder's claim against the deceased's estate. In re Estate of Harbaugh, 196 M 274, 639 P2d 495, 39 St. Rep. 84 (1982).

Defenses of Accommodation Maker: Where a person who agreed to sign a note as original maker failed to do so, accommodation maker could interpose any defense that such person could have interposed. May v. Whitbeck, 111 M 568, 113 P2d 332 (1941).

Admissibility of Evidence: Evidence tending to show that the maker of a negotiable instrument was merely an accommodation maker was properly excluded in an action by a holder in due course, since under section 55-306, R.C.M. 1947 (now repealed), an accommodation maker is liable to a holder for value (even though the latter knew at the time of taking the instrument that the former was but an accommodation maker). Lister v. Donlan, 85 M 571, 281 P 348, 72 ALR 1 (1929).

Absolute Liability of Maker: The liability of the maker of a promissory note is absolute, while that of an endorser is contingent upon the default of the maker. Anderson v. Border, 75 M 516, 244 P 494 (1926).

Joint Liability Inferred: While it is the general rule that where a number of persons successively sign a note, they are prima facie liable in the order in which their names appear even though they are in fact accommodation endorsers, their intention that there should be a joint, rather than a successive, liability may be inferred from the circumstances incident to the endorsements, and parol evidence is admissible to show that there was an agreement between them to that effect. Anderson v. Border, 75 M 516, 244 P 494 (1926).

Endorsement After Delivery: Section 55-605, R.C.M. 1947 (now repealed), with reference to liability of irregular or accommodation endorsers, has no application where a party places his endorsement on a promissory note after its delivery to the payee unless he does so pursuant to an agreement or understanding had prior to delivery that the endorsement should relate back and be considered as having been made before delivery; in the absence of such an agreement the endorsement constitutes a contract of guaranty rather than one of surety. Anderson v. Border, 75 M 516, 244 P 494 (1926).

Consideration to Accommodation Maker Not Required: Where defendant signed a renewal note taking the place of a note signed by her husband and another, at the request of the husband for the purpose of lending her name to him as comaker, she was an accommodation maker within the meaning of section 55-306, R.C.M. 1947 (now repealed), and not a guarantor, and liable as such to a holder for value though the latter knew her to be only an accommodation maker and that no consideration moved to her for signing it, the consideration moving to one or both of her comakers having been sufficient to uphold the note. Mulany v. Murray, 68 M 245, 216 P 1105 (1923).

Release of Mortgage Given by Principal: Defendant, an accommodation maker, was primarily liable on the note, though the payee bank at the time it took the instrument knew that he was lending his name to his comaker, and was not discharged from liability by the act of the bank in releasing mortgage security furnished by the latter, without his (defendant's) knowledge or consent. Merchants' Nat'l Bank of Billings v. Smith, 59 M 280, 196 P 523, 15 ALR 430 (1921).

Accommodation Maker Primarily Liable: Under the Negotiable Instruments Law, an accommodation maker of a promissory note is primarily liable and is not discharged by an extension of time given his comaker; the fact that plaintiff, a holder for value, knew that defendant was an accommodation maker did not change the rule. First St. Bank of Hilger v. Lang, 55 M 146, 174 P 597, 9 ALR 1139 (1918).

30-3-417. Transfer warranties.

Official Comment

Source: Section 3-416, U.C.C.

Prior Uniform Statutory Provision: Sections 65 and 69, Uniform Negotiable Instruments Law.

Official Comment to 1991 Amendment:

1. Subsection (a) [subsection (1) of this section] is taken from subsection (2) of present Section 3-417 [30-3-417(2) prior to 1991 revision]. Subsections (3) and (4) of present Section 3-417 [30-3-417(3) and (4) prior to 1991 revision] are deleted. Warranties under subsection (a) [subsection (1) of this section] in favor of the immediate transferee apply to all persons who transfer an instrument for consideration whether or not the transfer is accompanied by indorsement. Any consideration sufficient to support a simple contract will support those warranties. If there is an indorsement the warranty runs with the instrument and the remote holder may sue the indorser-warrantor directly and thus avoid a multiplicity of suits.

2. Since the purpose of transfer (Section 3-203(a) [30-3-210(1)]) is to give the transferee the right to enforce the instrument, subsection (a)(1) [subsection (1)(a) of this section] is a warranty that the transferor is a person entitled to enforce the instrument (Section 3-301 [30-3-301]). Under Section 3-203(b) [30-3-210(2)] transfer gives the transferee any right of the transferor to enforce the instrument. Subsection (a)(1) [subsection (1)(a) of this section] is in effect a warranty that there are no unauthorized or missing indorsements that prevent the transferor from making the transferee a person entitled to enforce the instrument.

3. The rationale of subsection (a)(4) [subsection (1)(d) of this section] is that the transferee does not undertake to buy an instrument that is not enforceable in whole or in part, unless there is a contrary agreement. Even if the transferee takes as a holder in due course who takes free of the defense or claim in recoupment, the warranty gives the transferee the option of proceeding against the transferor rather than litigating with the obligor on the instrument the issue of the holder-in-due-course status of the transferee. Subsection (3) of present Section 3-417 [30-3-417(3) prior to 1991 revision] which limits this warranty is deleted. The rationale is that the purpose of a "no recourse" indorsement is to avoid the obligation to guarantee payment and has no relation to disclaimer of warranties.

4. Under subsection (a)(5) [subsection (1)(e) of this section] the transferor does not warrant against difficulties of collection, impairment of the credit of the obligor or even insolvency. The transferee is expected to determine such questions before taking the obligation. If insolvency proceedings as defined in Section 1-201(22) [30-1-201(22)] have been instituted against the party who is expected to pay and the transferor knows it, the concealment of that fact amounts to a fraud upon the transferee, and the warranty against knowledge of such proceedings is provided accordingly.

5. Transfer warranties may be disclaimed with respect to any instrument except a check. Between the immediate parties disclaimer may be made by agreement. In the case of an indorser, disclaimer of transferor's liability, to be effective, must appear in the indorsement with words such as "without warranties" or some other specific reference to warranties. But in the case of a check, subsection (c) of proposed Section 3-416 [30-3-417(3)] provides that transfer warranties cannot be disclaimed at all because of the reliance of the banking system on these warranties in the collection process.

6. Subsection (b) [subsection (2) of this section] states the measure of damages for breach of warranty. There is no express provision for attorney's fees, but attorney's fees are not meant

to be necessarily excluded. They could be granted because they fit within the phrase "expenses incurred as a result of the breach." The intention is to leave to other state law the issue as to when attorney's fees are recoverable.

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "Warranties on presentment and transfer. (1) Any person who obtains payment or acceptance and any prior transferor warrants to a person who in good faith pays or accepts that:

(a) he has a good title to the instrument or is authorized to obtain payment or acceptance on behalf of one who has a good title; and

(b) he has no knowledge that the signature of the maker or drawer is unauthorized, except that this warranty is not given by a holder in due course acting in good faith:

(i) to a maker with respect to the maker's own signature; or

(ii) to a drawer with respect to the drawer's own signature, whether or not the drawer is also the drawee; or

(iii) to an acceptor of a draft if the holder in due course took the draft after the acceptance or obtained the acceptance without knowledge that the drawer's signature was unauthorized; and

(c) the instrument has not been materially altered, except that this warranty is not given by a holder in due course acting in good faith:

(i) to the maker of a note; or

(ii) to the drawer of a draft whether or not the drawer is also the drawee; or

(iii) to the acceptor of a draft with respect to an alteration made prior to the acceptance if the holder in due course took the draft after the acceptance, even though the acceptance provided "payable as originally drawn" or equivalent terms; or

(iv) to the acceptor of a draft with respect to an alteration made after the acceptance.

(2) Any person who transfers an instrument and receives consideration warrants to his transferee and if the transfer is by endorsement to any subsequent holder who takes the instrument in good faith that:

(a) he has a good title to the instrument or is authorized to obtain payment or acceptance on behalf of one who has a good title and the transfer is otherwise rightful; and

(b) all signatures are genuine or authorized; and

(c) the instrument has not been materially altered; and

(d) no defense of any party is good against him; and

(e) he has no knowledge of any insolvency proceeding instituted with respect to the maker or acceptor or the drawer of an unaccepted instrument.

(3) By transferring "without recourse" the transferor limits the obligation stated in subsection (2)(d) to a warranty that he has no knowledge of such a defense.

(4) A selling agent or broker who does not disclose the fact that he is acting only as such gives the warranties provided in this section, but if he makes such disclosure warrants only his good faith and authority."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

DECISIONS UNDER U.C.C. AFTER 1991 REVISION

Applicability of Discovery Doctrine to Uniform Commercial Code Conversion Cases: Over a 2½-year period, one of plaintiff's employees forged signatures on more than 100 company checks and money orders, made them payable to herself, and deposited the proceeds in her personal account at defendant credit union. Plaintiff ultimately filed an action against the credit union, seeking damages in the amount of the checks and money orders and alleging unlawful conversion of negotiable instruments under 30-3-419 and breach of transfer warranties under 30-4-207. The credit union moved for summary judgment on grounds that the conversion action was barred by the statutes of limitations in 30-4-207(5) and subsection (4) of this section. However, the statutes of limitations in 30-4-207(5) and subsection (4) of this section apply only to breach of warranty actions, not to conversion actions. The credit union then asserted that the discovery doctrine should apply. The doctrine is an equitable exception to the general rule that the statute of limitations begins to run as soon as the cause of action accrues, allowing instead that the applicable statute of limitations begins to run once plaintiff knew or should have known that a cause of action existed. In a case of first impression, the Supreme Court declined to apply the discovery doctrine to the Uniform Commercial Code conversion claim. Conversion actions are subject to the statute of limitations in 30-3-122(7), which requires commencement of a conversion action within 3 years of the action's accrual. The public would be poorly served by a rule that shifts the responsibility for careful bookkeeping and employee supervision away from those in the best position to monitor accounts and employees. Although predictably harsh in some cases, the 3-year statute of limitations will be strictly applied as best serving the goals of the Uniform Commercial Code. The facts regarding the date of the conversion and the filing of plaintiff's complaint were not in dispute, so the credit union was entitled to judgment as a matter of law on the conversion claim. Yarbro, Ltd. v. Missoula Fed. Credit Union, 2002 MT 152, 310 M 346, 50 P3d 158 (2002).

DECISIONS UNDER UNIFORM NEGOTIABLE INSTRUMENTS LAW

Forged Prior Endorsement: Plaintiff's right of action does not depend upon any express promise or warranty, but rather upon the implied warranty that all preceding endorsements are genuine and that it had good title to the check (sections 55-606, 55-607, R.C.M. 1947 (now repealed)). The endorsement of the payee having been forged, the warranties were broken, defendant had no title whatever to the check and, consequently, no right to collect any money thereon, and plaintiff is entitled to recover the amount paid and its right to recover was not affected by delay in giving notice of the forgery after discovery. First Nat'l Bank in Miles City v. Fed. Reserve Bank of Minneapolis, 88 M 589, 294 P 1105 (1931).

Warranties Enumerated: An unqualified endorsement of a promissory note warrants to all subsequent holders in due course that the instrument is genuine, that the endorser has good title to it, that all prior parties had capacity to contract, that the note at the time of his endorsement was valid and subsisting, that it will be paid according to its tenor, and that in case of its dishonor he will pay the amount of it to the holder or to any subsequent endorser who may be compelled to pay it. Wood v. Ferguson, 71 M 540, 230 P 592 (1924).

30-3-419. Conversion of instrument.

Official Comment

Source: Section 3-420, U.C.C.

Prior Uniform Statutory Provision: Section 137, Uniform Negotiable Instruments Law.

Official Comment:

1. Section 3-420 [30-3-419] is a modification of present Section 3-419 [30-3-419 prior to 1991 revision]. Present Section 3-419(1) [30-3-419(1) prior to 1991 revision] purports to state when an instrument is converted, but in fact the three cases stated do not include all the situations in which an instrument is converted. The first sentence of proposed Section 3-420(a) [30-3-419(1)] states a general rule that the law of conversion applicable generally to personal property also apply [sic] to instruments. Paragraphs (a) and (b) of present Section 3-419(1) [30-3-419(1)(a) and (1)(b) prior to 1991 revision] are deleted as inappropriate in cases of noncash items that may be delivered for acceptance or payment in collection letters that contain varying instructions as to what to do in the event of nonpayment on the day of delivery. It is better to leave such cases to be covered by the general law of conversion that would address the issue of when, under the circumstances prevailing, the presenter's right to possession has been denied. The second sentence of Section 3-420(a) [30-3-419(1)] makes clear that it includes not only cases of forged indorsement, but also cases in which the instrument lacks an indorsement necessary for negotiation. Thus, it covers cases of two-payee checks in which only one payee has indorsed as well as cases in which the indorsement of the payee is lacking. This amendment is for clarification only. It does not change current law.

The cases are divided on the issue of whether the drawer of a check with a forged indorsement can assert rights against a depositary bank that took the check. The last sentence of Section 3-420(a) [30-3-419(1)] resolves the conflict by following the rule stated in Stone & Webster Engineering Corp. v. First National Bank & Trust Co., 184 N.E.2d 358 (Mass. 1962). There is no reason why a drawer should have an action in conversion. The check represents an obligation of the drawer rather than property of the drawer. The drawer has an adequate remedy against the payor bank for recredit of the drawer's account for unauthorized payment of the check.

There is also a split of authority on the issue of whether a payee who never received the instrument is a proper plaintiff in a conversion action. The typical case is one in which a check is stolen from the drawer. Or the case may be one in which the check is mailed to an address different from that of the payee and is stolen after it arrives at that address. The thief forges the indorsement of the payee and obtains payment by depositing the check to an account in a depositary bank. The issue is whether the payee may bring an action in conversation [sic] against the depositary bank or the drawee bank. Under the last sentence of Section 3-420(a) [30-3-419(1)] the payee has no conversion action because the check was never delivered to the payee. Until delivery, the payee does not have any interest in the check. The payee never became the holder of the check nor a person entitled to enforce the check. Section 3-301 [30-3-301]. Nor is the payee injured by the fraud. Normally the drawer of a check intends to pay an obligation owed to the payee. But if the check is never delivered to the payee, the obligation owed to the payee is not affected. If the check falls into the hands of a thief who obtains payment after forging the signature of the payee as an indorsement, the obligation owed to the payee continues to exist after the thief receives payment. Since the payee's right to enforce the underlying obligation is unaffected by the fraud of the thief, there is no reason to give any remedy to the payee. The drawer of the check has no conversion remedy, but the drawee is not entitled to charge the drawer's account when the drawee wrongfully honored the check. The remedy of the drawee is against the depositary bank for breach of warranty under Section 3-417(a)(1) [30-3-424(1)(a)]. The loss will fall on the person who gave value to the thief for the check.

The situation is different if the check is delivered to the payee. If the check is taken for an obligation owed to the payee, the last sentence of Section 3-310(b)(4) [30-3-310(2)(d)] provides that the obligation may not be enforced to the extent of the amount of the check. The payee's rights are restricted to enforcement of the payee's rights in the instrument. In this event the payee is injured by the theft and has a cause of action for conversion.

The payee receives delivery when the check comes into the payee's possession, as for example when it is put into the payee's mailbox. Delivery to an agent is delivery to the payee. If a check is payable to more than one payee, delivery to one of the payees is deemed to be delivery to all of the payees. Occasionally, the person asserting a conversion cause of action is an indorsee rather than the original payee. If the check is stolen before the check can be delivered to the indorsee and the indorsee's indorsement is forged, the analysis is similar. For example, a check is payable to the order of A. A indorses it to B and puts it into an envelope addressed to B. The envelope is never delivered to B. Rather, Thief steals the envelope, forges B's indorsement to the check and obtains payment. Because the check was never delivered to B, the indorsee, B has no cause of action for conversion, but A does have such an action. A is the owner of the check. B never obtained rights in the check. If A intended to negotiate the check to B in payment of an obligation, that obligation was not affected by the conduct of Thief. B can enforce that obligation. Thief stole A's property not B's.

2. Subsection (2) of present Section 3-419 [30-3-419(2) prior to 1991 revision] is amended because it is not clear why the present law distinguishes between the liability of the drawee and that of other converters. Why should there be a conclusive presumption that the liability is face amount if a drawee refuses to pay or return an instrument or makes payment on a forged indorsement, while the liability of a maker who does the same thing is only presumed to be the face amount? Moreover, it is not clear what face amount means. If a note for $10,000 is payable in a year at 10% interest, it is common to refer to $10,000 as the face amount, but if the note is converted the loss to the owner also includes the loss of interest. Subsection (b) of Section 3-420 [30-3-419(2)] by referring to "amount payable on the instrument" allows the full amount due under the instrument to be recovered.

The "but" clause in subsection (b) [subsection (2) of this section] addresses the problem of conversion actions in multiple payee checks. Proposed Section 3-110(d) [30-3-126(4)] states that an instrument cannot be enforced unless all payees join in the action. But an action for conversion might be brought by a payee having no interest or a limited interest in the proceeds of the check. This clause prevents such a plaintiff from receiving a windfall. An example is a check by the owner of a building payable to the building contractor and a supplier of building material. Depending upon the contract between the contractor and the supplier, the amount of the check may be due entirely to the contractor, entirely to the supplier or part may be due to one and the rest to the other.

3. Subsection (3) of present Section 3-419 [30-3-419(3) prior to 1991 revision] has drawn criticism from the courts, who see no reason why a depositary bank should have the defense stated in the subsection. See Knesz v. Central Jersey Bank & Trust Co., 477 Atl.2d 806 (N.J. 1984). The depositary bank is ultimately liable in the case of a forged indorsement check because of its warranty to the payor bank under present Section 4-207(1)(a) [30-4-207(1)(a) prior to 1991 revision] and it is usually the most convenient defendant in cases involving multiple checks drawn on different banks. There is no basis for requiring the owner of the check to bring multiple actions against the various payor banks and to require those banks to assert warranty rights against the depositary bank. Subsection (c) of proposed Section 3-420 [30-3-419(3)] limits the defense of subsection (c) [subsection (3) of this section] to collecting banks other than the depositary bank. Under proposed Section 3-405 [30-3-420], which puts the loss in cases of forged indorsement by employees on the employer, forged indorsement losses by depositary banks should be substantially reduced.

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "Conversion of instrument — innocent representative. (1) An instrument is converted when:

(a) a drawee to whom it is delivered for acceptance refuses to return it on demand; or

(b) any person to whom it is delivered for payment refuses on demand either to pay or to return it; or

(c) it is paid on a forged endorsement.

(2) In an action against a drawee under subsection (1) the measure of the drawee's liability is the face amount of the instrument. In any other action under subsection (1) the measure of liability is presumed to be the face amount of the instrument.

(3) Subject to the provisions of this code concerning restrictive endorsements a representative, including a depositary or collecting bank, who has in good faith and in accordance with the reasonable commercial standards applicable to the business of such representative dealt with an instrument or its proceeds on behalf of one who was not the true owner is not liable in conversion or otherwise to the true owner beyond the amount of any proceeds remaining in his hands.

(4) An intermediary bank or payor bank which is not a depositary bank is not liable in conversion solely by reason of the fact that proceeds of an item endorsed restrictively (30-3-205 and 30-3-206) are not paid or applied consistently with the restrictive endorsement of an endorser other than its immediate transferor."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

DECISIONS UNDER U.C.C. AFTER 1991 REVISION

Applicability of Discovery Doctrine to Uniform Commercial Code Conversion Cases: Over a 2½-year period, one of plaintiff's employees forged signatures on more than 100 company checks and money orders, made them payable to herself, and deposited the proceeds in her personal account at defendant credit union. Plaintiff ultimately filed an action against the credit union, seeking damages in the amount of the checks and money orders and alleging unlawful conversion of negotiable instruments under this section and breach of transfer warranties under 30-4-207. The credit union moved for summary judgment on grounds that the conversion action was barred by the statutes of limitations in 30-3-417(4) and 30-4-207(5). However, the statutes of limitations in 30-3-417(4) and 30-4-207(5) apply only to breach of warranty actions, not to conversion actions. The credit union then asserted that the discovery doctrine should apply. The doctrine is an equitable exception to the general rule that the statute of limitations begins to run as soon as the cause of action accrues, allowing instead that the applicable statute of limitations begins to run once plaintiff knew or should have known that a cause of action existed. In a case of first impression, the Supreme Court declined to apply the discovery doctrine to the Uniform Commercial Code conversion claim. Conversion actions are subject to the statute of limitations in 30-3-122(7), which requires commencement of a conversion action within 3 years of the action's accrual. The public would be poorly served by a rule that shifts the responsibility for careful bookkeeping and employee supervision away from those in the best position to monitor accounts and employees. Although predictably harsh in some cases, the 3-year statute of limitations will be strictly applied as best serving the goals of the Uniform Commercial Code. The facts regarding the date of the conversion and the filing of plaintiff's complaint were not in dispute, so the credit union was entitled to judgment as a matter of law on the conversion claim. Yarbro, Ltd. v. Missoula Fed. Credit Union, 2002 MT 152, 310 M 346, 50 P3d 158 (2002).

Prior Adjudication of Common-Law Conversion as Collaterally Estopping Subsequent Claim of Statutory Conversion: Boyds contended that a previous action for common-law conversion did not collaterally estop subsequent litigation on a theory of statutory conversion. However, the prior litigation determined that Boyds had no interest in or right to checks deposited by the bank into the account of third-party defendants and that because the checks were correctly deposited, no conversion occurred. Because the subsequent cause depended on the same question of conversion that had already been determined, relitigation was properly barred by estoppel. Boyd v. First Interstate Bank of Kalispell, 253 M 214, 833 P2d 149, 49 St. Rep. 459 (1992), distinguishing Stapleton v. First Sec. Bank, 207 M 248, 675 P2d 83 (1983).

DECISIONS UNDER U.C.C. PRIOR TO 1991 REVISION

Unendorsed Check — Payment to Joint Payee Who Converts Proceeds — Liability: The District Court, on remand, properly followed the Supreme Court's directions in determining the wife's interest in two checks, wrongfully negotiated by the husband and converted by the defendant banks, to be the face amount of the checks. Based on the clear language of 30-3-419 and on expert testimony on statutory conversion, the findings and conclusions that the wife was entitled to the face amount were supported by ample authority. Stapleton v. First Sec. Bank, 219 M 323, 711 P2d 1364, 42 St. Rep. 2056 (1985), modifying Stapleton v. First Sec. Bank, 207 M 248, 675 P2d 83, 40 St. Rep. 2015 (1983).

Payment on a "forged endorsement", within the meaning of this section, includes payment on an unauthorized endorsement or payment when there is no endorsement at all. A person to whom an instrument is delivered, and who pays the instrument, is best able to prevent conversion by carefully checking endorsements. Therefore, where husband deposited in the bank two checks made out to him and his wife, neither of whom had endorsed the checks, the two drawee banks paid the checks, and husband withdrew the money, all without his wife's knowledge or consent, converted the money, and divorced his wife, all three banks were liable to wife for conversion of the checks. This section does not fix the extent of liability to a joint payee. To allow one of two joint payees to recover the face amount of an instrument would grant a windfall equal to half that amount, and each joint payee could recover the full face amount, requiring the defendant(s) to pay twice. The court held that the drawee banks were, under this section, absolutely liable for the face amount, since this section states the "liability is the face amount", but that payees' relative interests should be determined and a payee could recover only to the extent of his interest. The depositary bank was presumably liable for the full face amount under the wording of this section but could offer evidence to the contrary and must indemnify the drawee banks. The checks were in payment of the sale of property husband and wife jointly held, and wife was thus entitled to recover half the face amount of the checks absent proof to the contrary. Stapleton v. First Sec. Bank, 207 M 248, 675 P2d 83, 40 St. Rep. 2015 (1983), distinguished in Boyd v. First Interstate Bank of Kalispell, 253 M 214, 833 P2d 149, 49 St. Rep. 459 (1992).

Summary Judgment Proper — Improperly Endorsed Check Admittedly Negotiated by Bank: Plaintiff drew a check on her account at defendant bank payable to a building supply store to be used for supplies specifically listed on the face of the check and gave it to a contractor who was working for her. Contractor, unknown to plaintiff, endorsed the check "for exchange only" to the supply store. Based on this endorsement, defendant bank issued a new check payable to the supply store but without restriction on its face. Contractor applied the check to his own account with the supply store, rather than using it to buy materials for plaintiff. Several weeks later, the same thing was done with a check made payable to another building supply store. Plaintiff sued defendant bank for conversion. The Supreme Court reversed the District Court's denial of plaintiff's motion for summary judgment because the undisputed evidence showed that the defendant bank accepted and negotiated two checks that were not endorsed by the payees or by anyone clothed with apparent or actual authority to act for them. Eatinger v. First Nat'l Bank of Lewistown, 199 M 377, 649 P2d 1253, 39 St. Rep. 1465 (1982).

Plaintiff Estopped From Denying Ownership of Account: There was substantial evidence to support the District Court's conclusion that plaintiff was equitably estopped from denying his joint and beneficial ownership of a checking account by virtue of his acknowledgment and use of the account and the defendant-bank's reliance thereon in crediting a check to that account. The plaintiff could not complain that he lacked authority to draw checks on the account when he could have remedied that situation simply by signing the signature card. Beyer v. First Nat'l Bank of Dillon, 188 M 208, 612 P2d 1285, 37 St. Rep. 1035 (1980).

30-3-420. Employer responsibility for fraudulent indorsement by employee.

Official Comment

Source: Section 3-405, U.C.C.

Official Comment:

1. This section applies to instruments generally but normally the instrument will be a check. Section 3-405 [30-3-420] adopts the principle that the risk of loss for fraudulent indorsements by employees who are entrusted with responsibility with respect to checks should fall on the employer rather than the bank that takes the check or pays it, if the bank was not negligent in the transaction. If the bank failed to exercise ordinary care, subsection (b) [subsection (2) of this section] allows the employer to shift part of the loss to the bank to the extent the bank's failure to exercise ordinary care contributed to the loss. "Ordinary care" is defined in Section 3-103(a)(7)

[30-3-102(1)(g)]. Section 3-405 [30-3-420] is based on the belief that the employer is in a far better position to avoid the loss by care in choosing employees, in supervising them, and in adopting other measures to prevent forged indorsements on instruments payable to the employer or fraud in the issuance of instruments in the name of the employer. The provision applies regardless of whether the employer is negligent. Proposed Section 3-405 [30-3-420] governs cases that are covered by present Section 3-405(1)(c) [30-3-405(1)(c) prior to 1991 revision]. It also covers cases in which an entrusted employee forges the employer's signature as an indorsement and some cases not covered by present Section 3-405(1)(c) [30-3-405(1)(c) prior to 1991 revision] in which the entrusted employee makes a forged indorsement to a check drawn by the employer. An example is Case #6 in Comment 3. The latter cases are covered by present Section 3-406 [30-3-406 prior to 1991 revision], and under present law the employer takes the loss only if negligence of the employer can be proved. The proposed Section 3-405 [30-3-420] imposes the loss on the employer without proof of negligence. The definition of fraudulent indorsement covers the indorsement of the name of the payee on checks issued by the employer. These cases are covered by present Section 3-405(1)(c) [30-3-405(1)(c) prior to 1991 revision]. The result under proposed Section 3-405 [30-3-420] is similar, but the scope of proposed Section 3-405 [30-3-420] is somewhat wider. The scope is found in the definition of "responsibility" with respect to instruments, which includes some employees that may not be covered under present Section 3-405(1)(c) [30-3-405(1)(c) prior to 1991 revision]. This definition allows an employer to identify employees for whom the employer is responsible. An employer can insure this risk by bonding such employees.

2. With respect to cases governed by present Section 3-405(1)(c) [30-3-405(1)(c) prior to 1991 revision], proposed Section 3-405 [30-3-420] is more favorable to employers in one respect. Under present law, the bank is entitled to the preclusion provided by [present] Section 3-405(1)(c) [30-3-405(1)(c) prior to 1991 revision] if it took the check in good faith. The fact that the bank acted negligently does not shift the loss to the bank if the bank was acting in good faith. Under proposed Section 3-405 [30-3-420] part of the loss may be recovered from the bank according to the extent of the failure of the bank to exercise ordinary care.

3. Section 3-404(b) [30-3-405(2)] and Section 3-405 [30-3-420] both apply to cases of employee fraud. Section 3-404(b) [30-3-405(2)] is not limited to cases of employee fraud, but most of the cases to which it applies will be cases of employee fraud. The following cases illustrate the application of Section 3-405 [30-3-420]. In each case it is assumed that the bank that took the check acted in good faith and was not negligent.

Case #1. Janitor, an employee of Employer, breaks into Employer's safe and steals checks payable to Employer. Janitor forges Employer's indorsements on these checks. Since Janitor was not entrusted with "responsibility" with respect to the checks, Section 3-405 [30-3-420] does not make the indorsements effective. Section 3-406 [30-3-406] might apply to this case. The issue would be whether Employer was negligent in safeguarding the checks. If not, Employer could assert that the indorsements were forged and bring an action for conversion under Section 3-420 [30-3-419].

Case #2. X is Treasurer of Corporation and is authorized to write checks on behalf of Corporation by signing X's name as Treasurer. X draws a check in the name of Corporation and signs X's name as Treasurer. The check is payable to X. X then indorses the check and obtains payment. Assume that Corporation did not owe any money to X and did not authorize X to write the check. Although the writing of the check was not authorized, Corporation is bound as drawer of the check because X had authority to sign checks on behalf of Corporation. This result follows from agency law and Section 3-402(a) [30-3-403(1)]. Section 3-405 [30-3-420] is not needed in this case because there is no forged indorsement. X was payee of the check. Section 3-110(a) [30-3-126(1)].

Case #3. The duties of Employee, a bookkeeper, include posting the amounts of checks payable to Employer to the accounts of the drawers of the checks. Employee steals a check payable to Employer and forges Employer's indorsement. The check is deposited by Employee to an account in Depositary Bank which Employee opened in the same name as Employer, and the check is honored by the drawee bank. The indorsement is effective as Employer's indorsement because Employee's duties include processing checks for bookkeeping purposes. Thus, Employee is entrusted with "responsibility" with respect to the check. Neither Depositary Bank nor the drawee bank is liable to Employer for conversion of the check. The same result follows if Employee deposited the check in the account in Depositary Bank without indorsement. Under subsection (c) [subsection (3) of this section] deposit in a depositary bank in an account in a name substantially similar to that of Employer is the equivalent of an indorsement in the name of Employer.

Case #4. Employee's duties include stamping Employer's unrestricted blank indorsement on checks received by Employer and depositing them in Employer's bank account. After stamping Employer's unrestricted blank indorsement on a check, Employee steals the check and deposits it in Employee's personal bank account. Section 3-405 [30-3-420] doesn't apply because there is no forged indorsement. Employee is authorized by Employer to indorse Employer's checks. The fraud by Employee is not the indorsement but rather the theft of the check. Whether Employer has a cause of action against the bank in which the check was deposited is determined by whether the bank had notice of the breach of fiduciary duty by Employee. The issue is determined under Section 3-307 [30-3-308].

Case #5. The computer that controls Employer's check-writing machine was programmed to cause a check to be issued to Supplier Co. to which money was owed by Employer. The address of Supplier Co. was included in the information in the computer. Employee is an accounts payable clerk whose duties include entering information into the computer. Employee fraudulently changed the address of Supplier Co. in the computer data bank to an address of Employee. The check was subsequently produced by the check-writing machine and mailed to the address that Employee had entered into the computer. Employee obtained possession of the check, indorsed it in the name of Supplier Co, and deposited it to an account in Depositary Bank which Employee opened in the name "Supplier Co." The check was honored by the drawee bank. The indorsement is effective under Section 3-405(b) [30-3-420(2)] because Employee's duties allowed Employee to supply information determining the address of the payee of the check. An employee that has the ability to determine the address to which a check is to be sent controls the disposition of the check and facilitates forgery of the indorsement. The employer is held responsible. The drawee may debit the account of Employer for the amount of the check. There is no breach of warranty by Depositary Bank under Section 3-417(a)(1) [30-3-424(1)(a)].

Case #6. Treasurer is authorized to draw checks in behalf of Corporation. Treasurer draws a check of Corporation payable to Supplier Co., a company that sold goods to Corporation. The check was issued to pay the price of these goods. At the time the check was signed Treasurer had no intention of stealing the check. Later, Treasurer stole the check, indorsed it in the name "Supplier Co." and obtained payment by depositing it to an account in Depositary Bank which Treasurer opened in the name "Supplier Co.". The indorsement is effective under Section 3-405(b) [30-3-420(2)]. Section 3-404(b) [30-3-405(2)] does not apply to this case.

Case #7. Checks of Corporation are signed by Treasurer in behalf of Corporation or drawer. Clerk's duties include the preparation of checks for issue by Corporation. Clerk prepares a check payable to the order of Supplier Co. for Treasurer's signature. Clerk fraudulently informs Treasurer that the check is needed to pay a debt owed to Supplier Co, a company that does business with Corporation. No money is owed to Supplier Co. and Clerk intends to steal the check. Treasurer signs it and returns it to Clerk for mailing. Clerk does not indorse the check but deposits it to an account in Depositary Bank which Clerk opened in the name "Supplier Co.". The check is honored by the drawee bank. Section 3-404(b)(i) [30-3-405(2)(part)] does not apply to this case because Clerk, under Section 3-110(a) [30-3-126(1)], is not the person whose intent determines to whom the check is payable. But Section 3-405 [30-3-420] does apply and it treats the deposit by Clerk as an effective indorsement by Clerk because Clerk was entrusted with responsibility with respect to the check. If Supplier Co. is a fictitious person Section 3-404(b)(ii) [30-3-405(2)(part)] applies. But the result is the same. Clerk's deposit is treated as an effective indorsement of the check whether Supplier Co. is a fictitious or a real person or whether money was or was not owing to Supplier Co. The drawee bank may debit the account of Corporation for the amount of the check and there is no breach of warranty by Depositary Bank under Section 3-417(1)(a) [30-3-424(1)(a)].

4. The last sentence of subsection (b) [subsection (2) of this section] is similar to subsection (d) of Section 3-404 [30-3-405(4)] which is discussed in Comment 3 to Section 3-404 [30-3-405]. For example, in Case #5, Case #6, or Case #7 the depositary bank may have failed to exercise ordinary care when it allowed the employee to open an account in the name "Supplier Co." and to deposit checks payable to "Supplier Co." in that account. If the trier of fact finds that there was such a failure and that the failure substantially contributed to loss, it could find the depositary bank liable to the extent the failure contributed to the loss.

Case Notes

Employer Responsible for Employee's Fraudulent Endorsement of Instrument Absent Evidence of Lack of Ordinary Care by Party Taking Instrument for Value — Breach of Warranty Claim Properly Dismissed: Over a 2½-year period, one of plaintiff's employees forged signatures on more than 100 company checks and money orders, made them payable to herself, and deposited the proceeds in her personal account at defendant credit union. Plaintiff ultimately filed an action against the credit union, seeking damages in the amount of the checks and money orders and alleging breach of transfer warranties under 30-4-207. After finding that plaintiff produced no evidence to refute the credit union's assertion that the employee was entrusted with responsibility for processing instruments and that the credit union had exercised ordinary care in accepting the instruments for payment, the District Court entered summary judgment for the credit union on the breach of warranty claim. The Supreme Court affirmed. Plaintiff was not considered a transferee under the terms of 30-4-207. Plaintiff received no instrument or transfer warranty from the credit union, so plaintiff was not entitled to claim a breach of the warranty against the credit union. Plaintiff was responsible for the employee's actions under this section. Yarbro, Ltd. v. Missoula Fed. Credit Union, 2002 MT 152, 310 M 346, 50 P3d 158 (2002).

30-3-421. Refusal to pay cashier's checks, teller's checks, and certified checks.

Official Comment

Source: Section 3-411, U.C.C.

Official Comment:

In some cases a creditor may require that the debt be paid by an obligation of a bank. The debtor may comply by obtaining certification of the debtor's check, but more frequently the debtor buys from a bank a cashier's check or teller's check payable to the creditor. The check is taken by the creditor as a cash equivalent on the assumption that the bank will pay the check. Sometimes, the debtor wants to retract payment by inducing the obligated bank not to pay. That bank is the bank that certifies the debtor's check or the bank from which the debtor bought the cashier's check or teller's check. The typical case involves a dispute between the parties to the transaction in which the check is given in payment. In the case of a certified check or cashier's check, the bank can safely pay the holder of the check despite notice that there may be an adverse claim to the check (Section 3-602 [30-3-603]). It is also clear that the bank that sells a teller's check has no duty to order the bank on which it is drawn not to pay it. A debtor using any of these types of checks has no right to stop payment. Nevertheless, some banks will refuse payment as an accommodation to a customer. Section 3-411 [30-3-421] is designed to discourage this practice.

The term "obligated bank" refers to the issuer of the cashier's check, the acceptor of the certified check, and the drawer of the teller's check. If the obligated bank wrongfully refuses to pay, it is liable to pay for expenses and loss of interest resulting from the refusal to pay. There is no express provision for attorney's fees, but attorney's fees are not meant to be necessarily excluded. They could be granted because they fit within the language "expenses . . . resulting from the nonpayment." In addition the bank may be liable to pay consequential damages if it has notice of the particular circumstances giving rise to the damages.

Subsection (c) [subsection (3) of this section] provides that expenses or consequential damages are not recoverable if the refusal to pay is because of the reasons stated. The purpose is to limit that recovery to cases in which the bank refuses to pay even though its obligation to pay is clear and it is able to pay. Subsection (b) [subsection (2) of this section] applies only if the refusal to honor the check is wrongful. If the bank is not obliged to pay there is no recovery. The bank may assert any claim or defense that it has, but normally the bank would not have a claim or defense. In the usual case it is a remitter that is asserting a claim to the check on the basis of a rescission of negotiation to the payee under Section 3-202 [30-3-209]. See Section 3-201(a) [30-3-202(1)] and Comment to Section 3-201 [30-3-202]. The bank can assert that claim if there is compliance with Section 3-305(c) [30-3-305(3)], but the bank is not protected from damages under subsection (b) [subsection (2) of this section] if the claim of the remitter is not upheld. In that case, the bank is insulated from damages only if payment is enjoined under Section 3-603(b)(1) [30-3-604(2)(a)]. Subsection (c)(iii) [subsection (3)(c) of this section] refers to cases in which the bank may have a reasonable doubt about the identity of the person demanding payment. For example, a cashier's check is payable to "Supplier Co." The person in possession of the check presents it for payment over the counter and claims to be an officer of Supplier Co. The bank may refuse payment until it has been given adequate proof that the presentment in fact is being made for Supplier Co., the person entitled to enforce the check.

30-3-422. Obligation of acceptor.

Official Comment

Source: Section 3-413, U.C.C.

Official Comment:

Subsection (a) [subsection (1) of this section] is consistent with present Section 3-413(1) [30-3-413(1) prior to 1991 revision]. Subsection (b) [subsection (2) of this section] has primary importance with respect to certified checks. It protects the holder in due course of a certified check that was altered after certification and before negotiation to the holder in due course. A bank can avoid liability for the altered amount by stating on the check the amount the bank agrees to pay. The subsection applies to other accepted drafts as well.

30-3-423. Obligation of drawer.

Official Comment

Source: Section 3-414, U.C.C.

Official Comment:

1. Subsection (a) [subsection (1) of this section] relates to the obligation of the drawer on an unaccepted draft. It replaces present Section 3-413(2) [30-3-413(2) prior to 1991 revision]. The requirement in present law of notice of dishonor or protest has been eliminated. Notice of dishonor is necessary only with respect to indorser's liability. The liability of the drawer of an unaccepted draft is treated as a primary liability. The effect of a draft drawn without recourse is stated in subsection (d) [subsection (4) of this section].

2. Subsection (b) [subsection (2) of this section] relieves the drawer of liability on a draft accepted before or after issue or negotiation of the draft if the acceptor is a bank. This changes present law. Under present Section 3-411(1) [30-3-411, now repealed] the drawer is discharged only if the holder obtains certification. Holders that have a bank obligation do not normally rely on the drawer to guarantee the bank's solvency. A holder can obtain protection against the insolvency of a bank acceptor by a specific guaranty of payment by the drawer or by obtaining an indorsement by the drawer. See Section 3-205(d) [30-3-204(4)].

3. Subsection (c) [subsection (3) of this section] concerns the liability of the drawer if a draft is accepted by a drawee other than a bank and the acceptor dishonors. The drawer of an unaccepted draft is the party primarily liable on the instrument. The drawee has no liability on the draft. When the draft is accepted, the obligations change. The drawee, as acceptor, becomes primarily liable and the drawer's liability is that of a person secondarily liable. The drawer's liability is identical to that of an indorser, and subsection (c) [subsection (3) of this section] states the drawer's liability that way. The drawer is liable to pay the person entitled to enforce the draft or any indorser that pays pursuant to Section 3-415 [30-3-414]. The drawer in this case is discharged if notice of dishonor is required by Section 3-503 [30-3-508] and is not given in compliance with that section. A drawer that pays has a right of recourse against the acceptor. Section 3-413(a) [30-3-422(1)].

4. Subsection (d) [subsection (4) of this section] does not permit the drawer of a check to avoid liability under subsection (a) [subsection (1) of this section] by drawing the check without recourse. There is no legitimate purpose served by issuing a check on which nobody is liable. Drawing without recourse is effective to disclaim liability of the drawer if the draft is not a check. For example, in a documentary sale, Seller draws a draft on Buyer for the price of goods shipped to Buyer. The draft is payable upon delivery of an order bill of lading covering the goods. Seller delivers the draft with the bill of lading to Finance Company that is named as payee of the draft. If Seller draws without recourse Finance Company takes the risk that Buyer will dishonor. If Buyer dishonors, Finance Company has no recourse against Seller but it can obtain reimbursement by selling the goods which it controls through the bill of lading.

5. Subsection (e) [subsection (5) of this section] is derived from present Section 3-502(1)(b) [30-3-502, now repealed]. It is designed to protect the drawer of a check against loss resulting from suspension of payments by the drawee bank when the holder of the check delays collection of the check. For example, X writes a check payable to Y for $1,000. The check is covered by funds in X's account in the drawee bank. Y delays initiation of collection of the check for more than 30 days after the date of the check. The drawee bank suspends payments after the 30-day period and before the check is presented for payment. If the $1,000 of funds in X's account have not been withdrawn, X has a claim for those funds against the drawee bank and, if subsection (e) [subsection (5) of this section] were not in effect, X would be liable to Y on the check because the check was dishonored. Section 3-502(e) [30-3-512(5)]. If the suspension of payments by the drawee bank will result in payment to X of less than the full amount of the $1,000 in the account or if there is a significant delay in payment to X, X will suffer a loss which would not have been suffered if Y had promptly initiated collection of the check. In most cases, X will not suffer any loss because of the existence of federal bank deposit insurance that covers accounts up to $100,000. Thus, subsection (e) [subsection (5) of this section] has relatively little importance. There might be some cases, however, in which the account is not fully insured because it exceeds $100,000 or because the account doesn't qualify for deposit insurance. Subsection (e) [subsection (5) of

this section] retains the phrase "deprived of funds maintained with the drawee" appearing in present Section 3-502(1)(b) [30-3-502, now repealed]. The quoted phrase applies if the suspension of payments by the drawee prevents the drawer from receiving the benefit of funds which would have paid the check if the holder had been timely in initiating collection. Thus, any significant delay in obtaining full payment of the funds is a deprivation of funds. The drawer can discharge drawer's liability by assigning rights against the drawee with respect to the funds to the holder.

30-3-424. Presentment warranties.

Official Comment

Source: Section 3-417, U.C.C.

Official Comment:

1. This section replaces subsection (1) of present Section 3-417 [30-3-417(1) prior to 1991 revision]. The present provision is difficult to understand because it purports to state in one subsection all warranties given to any person paying any instrument. The result is a provision that is replete with exceptions that cannot be readily understood except after close scrutiny of the language. Proposed Section 3-417 [30-3-424] covers presentment warranties made to the drawee of an unaccepted draft, to the acceptor of an accepted draft and to the maker of a note. Warranties made to drawees of uncertified checks and other unaccepted drafts are covered in subsection (a) [subsection (1) of this section].

2. Subsection (a) [subsection (1) of this section] states three warranties. Subsection (a)(1) [subsection (1)(a) of this section] in effect is a warranty that there are no unauthorized or missing indorsements. "Person entitled to enforce" is defined in Section 3-301 [30-3-301]. Subsection (a)(2) [subsection (1)(b) of this section] is a warranty that there is no alteration. Subsection (a)(3) [subsection (1)(c) of this section] is a warranty of no knowledge that there is a forged drawer's signature. Subsection (a) [subsection (1) of this section] states that the warranties are made to the drawee and subsections (b) and (c) [subsections (2) and (3) of this section] identify the drawee as the person entitled to recover for breach of warranty. There is no warranty made to the drawer under subsection (a) [subsection (1) of this section] when presentment is made to the drawee. Warranty to the drawer is governed by subsection (d) [subsection (4) of this section] and that applies only when presentment for payment is made to the drawer with respect to a dishonored draft. In Sun 'N Sand, Inc. v. United California Bank, 582 P.2d 920 (Cal. 1978), the court held that a warranty is made to the drawer of a check when the check is presented to the drawee for payment. The result in this case is rejected by Section 3-417 [30-3-424].

3. Subsection (a)(1) [subsection (1)(a) of this section] retains the rule that the drawee does not admit the authenticity of indorsements and subsection (a)(3) [subsection (1)(c) of this section] retains the rule of Price v. Neal, 3 Burr. 1354 (1762), that the drawee takes the risk that the drawer's signature is unauthorized unless the person presenting the draft has knowledge that the drawer's signature is unauthorized. Under subsection (a)(3) [subsection (1)(c) of this section] the warranty of no knowledge that the drawer's signature is unauthorized is also given by prior transferors of the draft.

4. Subsection (d) [subsection (4) of this section] applies to presentment for payment in all cases not covered by subsection (a) [subsection (1) of this section]. It applies to presentment of notes and accepted drafts to any party obliged to pay the instrument, including an indorser, and to presentment of dishonored drafts if made to the drawer or an indorser. In cases covered by subsection (d) [subsection (4) of this section], there is only one warranty and it is the same as that stated in subsection (a)(1) [subsection (1)(a) of this section]. There are no warranties comparable to subsections (a)(2) and (a)(3) [subsections (1)(b) and (1)(c) of this section] because they are appropriate only in the case of presentment to the drawee. If presentment is made to the drawer or maker, there is no necessity for a warranty concerning the signature of that person or with respect to alteration. If presentment is made to an indorser, the indorser had itself warranted authenticity of signatures and that the instrument was not altered. Section 3-416(a)(2) and (3) [30-3-417(1)(b) and (1)(c)].

5. The measure of damages for breach of warranty under subsection (a) [subsection (1) of this section] is stated in subsection (b) [subsection (2) of this section]. There is no express provision for attorney's fees, but attorney's fees are not meant to be necessarily excluded. They could be granted because they fit within the language "expenses . . . resulting from the breach." See Comment 2 to Section 3-416 [30-3-417]. Subsection (b) [subsection (2) of this section] provides that the right of the drawee to recover for breach of warranty is not affected by a failure of the drawee to exercise ordinary care in paying the draft. This provision follows the result reached in Hartford Accident & Indemnity Co. v. First Pennsylvania Bank, 859 F.2d 295 (3d Cir. 1988).

6. Subsection (c) [subsection (3) of this section] applies to checks and other unaccepted drafts. It gives to the warrantor the benefit of rights that the drawee has against the drawer under Section 3-404 [30-3-405], Section 3-405 [30-3-420], Section 3-406 [30-3-406], and Section 4-406 [30-4-406]. If the drawer's conduct contributed to a loss from forgery or alteration, the drawee should not be allowed to shift the loss to the warrantor.

7. The first sentence of subsection (e) [subsection (5) of this section] recognizes that checks are normally paid by automated means and that payor banks rely on warranties in making payment. Thus, it is not appropriate to allow disclaimer of warranties appearing on checks that normally will not be examined by the payor bank. The second sentence requires a breach of warranty claim to be asserted within 30 days after the drawee learns of the breach and the identity of the warrantor.

30-3-425. Payment or acceptance by mistake.

Official Comment

Source: Section 3-418, U.C.C.

Official Comment:

1. This section covers payment or acceptance by mistake and replaces present Section 3-417 [30-3-417 prior to 1991 revision]. Under present law, the remedy of a drawee that pays or accepts a draft by mistake is based on the law of mistake and restitution which is referred to in Section 1-103 [30-1-103]. Present Section 3-418 [30-3-418, now repealed] is simply a limitation on this right of restitution which is not specifically stated in present Article 3 [Title 30, chapter 3, prior to 1991 revision]. Proposed Section 3-418 [30-3-425] specifically states the right of restitution in subsection (a) and (b) [subsections (1) and (2) of this section]. Subsection (a) [subsection (1) of this section] applies to the most common cases in which the problem is presented. It covers payment or acceptance of forged checks, insufficient funds checks and checks on which the drawer has stopped payment. If the drawee acted under a mistaken belief that the check was not forged, had not been stopped or was not an insufficient funds check, the drawee is entitled to recover the funds paid or to revoke the acceptance whether or not the drawee acted negligently. But in each case, by virtue of subsection (c) [subsection (3) of this section], the drawee loses the remedy if the person receiving payment or acceptance was a person who took the check in good faith and for value. Subsection (a) and (c) [subsections (1) and (3) of this section] are consistent with present Section 3-418 [30-3-418, now repealed] and incorporate the rule of Price v. Neal. The result in the three cases covered by subsection (a) [subsection (1) of this section] is that the drawee in most cases will not have a remedy against the person paid because there is usually a person who took the check in good faith and for value.

The remedy of a drawee to recover funds paid on bad checks is principally found in Section 3-417 [30-3-424]. The drawee wins in forged indorsement cases (Section 3-417(a)(1) [30-3-424(1)(a)]) and in alteration cases (Section 3-417(a)(2) [30-3-424(1)(b)]) and loses in forged check cases unless the warrantor had knowledge of the forgery (Section 3-417(a)(3) [30-3-424(1)(c)]). Insufficient funds cases are of three types:

Case #1. The check is not covered by a credit balance in the customer's account and the drawee paid the check intending to honor an overdraft. This case is not covered by Section 3-418 [30-3-425] because no mistake was made by the drawee. The drawee intended to give credit to the drawer.

Case #2. The check is not covered by a credit balance and the check was paid because the bank neglected to verify the balance before paying. This case is covered by Section 3-418 [30-3-425].

Case #3. The check is covered by a credit balance but the balance does not represent funds that are available for withdrawal by the drawer under applicable law. Section 3-418 [30-3-425] applies if the bank mistakenly believed that the credit balance represented available funds. But if the check was covered by a credit balance available for withdrawal by the customer, Section 3-418 [30-3-425] doesn't apply even if the bank learns at a later date that the credit balance was subject to a charge-back because of a returned item. In that case there was no mistake of fact. The funds were available for withdrawal. The only remedy of the drawee bank is to recover from the drawer of the check by charge-back or otherwise.

2. Subsection (b) [subsection (2) of this section] covers cases of payment or acceptance by mistake that are not covered by subsection (a) [subsection (1) of this section]. It directs courts to deal with those cases under the law governing mistake and restitution. This subsection is also subject to subsection (c) [subsection (3) of this section].

3. The right of the drawee to recover a payment or to revoke an acceptance under Section 3-418 [30-3-425] is not affected by the rules under Article 4 [Title 30, chapter 4] that determine

when an item is paid. Even though a payor bank may have paid an item under proposed Section 4-215 [30-4-213], it may have a right to recover the payment under Section 3-418 [30-3-425]. National Savings & Trust Co. v. Park Corp. 722 F.2d 1303 (6th Cir. 1983), cert. denied, 466 U.S. 939 (1984), correctly states the present law on the issue.

Part 5
Presentment, Notice of Dishonor, and Protest

Part Case Notes

DECISIONS UNDER U.C.C. PRIOR TO 1991 REVISION

Supply of Presentment Date by Holder: The holder of a 160-day sight draft may supply a date of presentment when the drawee fails to provide his written acceptance or date thereof. Thus, the holder of the draft could in good faith treat the date on which the collecting bank acknowledged receipt of the draft as the date of acceptance and could properly treat the draft as dishonored when payment was received 162 days after the date the draft was received from the bank. Clawson v. Berklund, 188 M 48, 610 P2d 1168 (1980).

DECISIONS UNDER UNIFORM NEGOTIABLE INSTRUMENTS LAW

Interest Coupons in Effect Promissory Notes: Interest coupons are in effect promissory notes, and as to such commercial paper laches of the holder in failure promptly to make presentment for payment does not discharge the maker (in the instant case the district issuing the coupon bonds) from liability thereon; the maker (district) is primarily liable and presentment is unnecessary to preserve such liability. J. K. & C. S. Mullen Benev. Corp. v. School District, 99 M 388, 43 P2d 902 (1935).

Successive Endorsements: In an action against the drawer of a check to recover thereon, defendant pleading payment by reason of the delay of plaintiff in presenting it before the bank on which drawn closed its doors, the rule is that transfers to successive endorsees do not extend the time within which it must be presented, so far as defendant drawer is concerned, which, under section 55-1703, R.C.M. 1947 (now repealed), is within a reasonable time after its issue. Cellars v. Dwinnell, 87 M 73, 285 P 181 (1930).

Wrongful Refusal by Drawee to Pay: Under section 55-1703, R.C.M. 1947 (now repealed), the drawer of a check is discharged from liability thereon for delay in presenting it for payment only "to the extent of the loss caused by the delay"; hence where the endorsee of a check, drawn on a bank in another town, immediately upon its receipt 3 days after its issuance, mailed it to his bank, which in turn on the same day mailed it to the bank upon which drawn, which, while paying checks presented over the counter, refused to pay check presented by mail, of which fact the endorsee was ignorant, the loss sustained by the drawer was due to the wrongful act of the drawee bank and not to delay in presenting the check for payment. Cellars v. Dwinnell, 87 M 73, 285 P 181 (1930).

Maker's Liability Regardless of Presentment:

Demand upon the maker of a promissory note for payment or presentment to him, is not necessary before action against him thereon. Barrett v. Morton, 137 M 190, 351 P2d 601 (1960); Quickenden v. Hubert, 83 M 501, 272 P 994 (1928).

In an action to enforce a note against the maker, it is not necessary to prove presentment for payment; it is only persons secondarily liable that the law has reference to in specifying the time and manner in which presentment must be made, and, unless the Statute of Limitations bars a demand against the maker, he cannot say it was not made in time. U.S. Nat'l Bank of Red Lodge v. Shupak, 54 M 542, 172 P 324 (1918).

Presentment for payment is not necessary to charge the makers of a demand note payable at a particular place. U.S. Nat'l Bank of Red Lodge v. Shupak, 54 M 542, 172 P 324 (1918).

Delay in Giving Notice: The general rule is that unless the drawer of a check has sustained loss or damage by reason of delay in giving notice of dishonor or nonpayment, such delay is of no consequence; hence where, even if timely notice had been given, it could not have reached him and therefore not aided him in preventing loss, the delay was immaterial. Cellars v. Dwinnell, 87 M 73, 285 P 181 (1930).

Loss Required to Discharge Drawer: A check must be presented for payment within a reasonable time after its issuance, or the drawer will be discharged from liability thereon to the extent of the loss caused by the delay, but this result follows only on a showing of loss or injury by reason of delay. Blackwelder v. Fergus Motor Co., 80 M 374, 260 P 734 (1927).

Repeal of Prior Law: The effect of the repeal of section 5923, Revised Codes of 1907, by Ch. 82, L. 1909, which section provided that presentment of instrument payable at a bank must be made during banking hours, and substituting therefor section 55-706, R.C.M. 1947 (now repealed), which made no reference to the time when presentment must be made, was to make presentment for payment at any time proper, whether during banking hours or not. Clarke v. Nat'l Bank of Mont., 78 M 48, 252 P 373 (1926).

Failure to Prove Presentment: Where plaintiff in an action against the endorser of a promissory note contented himself with introducing the note in evidence, failing to show that defendant's liability had been fixed by presentment to and demand of payment thereof from the maker and notice of nonpayment to defendant, or facts excusing presentment, demand and notice, or a waiver thereof by defendant, judgment for defendant was proper. Morgan v. Huffman, 76 M 396, 247 P 326 (1926).

Re-Presentment After Dishonor: Where the Board of County Commissioners had wrongfully refused to issue an order for the payment of a warrant not represented for payment until after the 60-day period provided for in section 16-2609, R.C.M. 1947 (now repealed), had expired, and thereafter the bank in which its funds were deposited became insolvent, the county was not discharged from liability thereon under this section by the holder's neglect to make timely demand for payment, since the detriment suffered by it was traceable to its improper refusal and not to the holder's failure to act. State ex rel. Case v. Bolles, 74 M 54, 238 P 586 (1925).

Presentment to Bank Where Payable: Sending of a check direct to the drawee bank by a Federal Reserve Bank is a good presentment. Jensen v. Laurel Meat Co., 71 M 582, 230 P 1081 (1924).

Demand Note: The provision of section 55-701, R.C.M. 1947 (now repealed), that where a note is by its terms payable at a special place, and the maker is able and willing to pay it there at maturity, such ability and willingness are equivalent to a tender of payment by him, has no application to a demand note. U.S. Nat'l Bank of Red Lodge v. Shupak, 54 M 542, 172 P 324 (1918).

"Maturity" Defined: "Maturity" of a note, within the meaning of section 55-701, R.C.M. 1947 (now repealed), is the time when a note or bill becomes due. U.S. Nat'l Bank of Red Lodge v. Shupak, 54 M 542, 172 P 324 (1918).

Purpose of Presentment: Section 55-701, R.C.M. 1947 (now repealed), defined the purpose of presentment, and was not modified by subsequent sections. U.S. Nat'l Bank of Red Lodge v. Shupak, 54 M 542, 172 P 324 (1918).

30-3-504. Presentment.

Official Comment

Source: Section 3-501, U.C.C.

Prior Uniform Statutory Provision: Sections 72, 73, 77, 78 and 145, Uniform Negotiable Instruments Law.

Official Comment to 1991 Amendment:

Subsection (a) [subsection (1) of this section] restates present Section 3-504(1) [30-3-504(1) prior to 1991 revision]. Proposed Section 3-502 [30-3-512] states when presentment is a condition to dishonor. Subsection (b)(1) [subsection (2)(a) of this section] states the place and manner of presentment. Electronic presentment is authorized. The communication of the demand for payment or acceptance is effective when received. Subsection (b)(2)(ii), (iii), and (iv) [subsections (2)(b)(ii) through (2)(b)(iv) of this section] restate present Section 3-505 [30-3-505, now repealed]. Subsection (b)(2)(ii) [subsection (2)(b)(ii) of this section] allows the person to whom presentment is made to require exhibition of the instrument, unless the parties have agreed otherwise as in an electronic presentment agreement. Present Section 3-507(3) [30-3-507, now repealed] is the antecedent of subsection (b)(2)(v) [subsection (2)(b)(v) of this section]. Since a payor must decide whether to pay or accept on the day of presentment, subsection (b)(2)(i) [subsection (2)(b)(i) of this section] allows the payor to set a cut-off hour for receipt of instruments presented.

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "How presentment made. (1) Presentment is a demand for acceptance or payment made upon the maker, acceptor, drawee or other payor by or on behalf of the holder.

(2) Presentment may be made:

(a) by mail, in which event the time of presentment is determined by the time of receipt of the mail; or

(b) through a clearinghouse; or

(c) at the place of acceptance or payment specified in the instrument or if there be none at the place of business or residence of the party to accept or pay. If neither the party to accept or pay nor anyone authorized to act for him is present or accessible at such place presentment is excused.

(3) It may be made:

(a) to any one of two or more makers, acceptors, drawees or other payors; or

(b) to any person who has authority to make or refuse the acceptance or payment.

(4) A draft accepted or a note made payable at a bank in the United States must be presented at such bank.

(5) In the cases described in 30-4-210 presentment may be made in the manner and with the result stated in that section."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

DECISIONS UNDER U.C.C. PRIOR TO 1991 REVISION

"Demand Item" and "Presentment" Construed — Waiver of Midnight Deadline Rule: When defendant's, Nuernberger's, check was twice refused and returned for insufficient funds by the payor bank, First Bank of Billings (First Bank), an officer of the joint payee, Montana Livestock Production Credit Association (MLPCA) returned the check to First Bank with a written memo authorizing First Bank to "hold it for longer than the usual 24-hour period" and to pay when funds became available. The District Court granted summary judgment for the plaintiff (the other joint payee) and MLPCA and found First Bank strictly liable for the face amount of the check because of its failure to comply with the midnight deadline rule. The Supreme Court reversed and found that the midnight deadline rule did not apply, holding that the check was not a "demand item" because it was transmitted with the understanding it would be held for sufficient funds and that there had been no "presentment" by the plaintiff, but only by the joint payee, MLPCA. The Supreme Court further held that there had been a waiver of the midnight rule time requirements by MLPCA's memo. Iverson v. First Bank of Billings, 219 M 283, 712 P2d 1285, 42 St. Rep. 2021 (1985).

Supply of Presentment Date by Holder: The holder of a 160-day sight draft may supply a date of presentment when the drawee fails to provide his written acceptance or date thereof. Thus, the holder of the draft could in good faith treat the date on which the collecting bank acknowledged receipt of the draft as the date of acceptance and could properly treat the draft as dishonored when payment was received 162 days after the date the draft was received from the bank. Clawson v. Berklund, 188 M 48, 610 P2d 1168 (1980).

30-3-508. Notice of dishonor.

Official Comment

Source: Section 3-503, U.C.C.

Prior Uniform Statutory Provision: Sections 90 through 108, Uniform Negotiable Instruments Law.

Official Comment to 1991 Amendment:

1. Subsection (a) [subsection (1) of this section] is based on present Section 3-501(2)(a) [30-3-501, now repealed]. However, as explained in Comment 1 to Section 3-414 [30-3-423], notice of dishonor is no longer relevant to the liability of a drawer except for the case of a draft accepted by an acceptor other than a bank. There is no reason why drawers should be discharged on instruments they draw until payment or acceptance. They are entitled to have the instrument presented to the drawee and dishonored (Section 3-414(1) [30-3-423(1)]) before they are liable to pay, but no formal notice of dishonor need be made to them as a condition of liability. Subsection (b) [subsection (2) of this section], which states how notice of dishonor is given, is based on present Section 3-508(3) [30-3-508(3) prior to 1991 revision].

2. The second sentence of subsection (c) [subsection (3) of this section] is based on present Section 3-508(2) [30-3-508(2) prior to 1991 revision]. It differs from that section in that it provides a longer time for a person who is not a collecting bank to give notice of dishonor than the three-day period allowed in the present statute. Delay in giving notice of dishonor may be excused under Section 3-504(d) [30-3-513(4)].

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "(1) Notice of dishonor may be given to any person who may be liable on the instrument by or on behalf of the holder or any party who has himself received notice, or any other party who can be compelled to pay the instrument. In addition an agent or bank in whose hands the instrument is dishonored may give notice to his principal or customer or to another agent or bank from which the instrument was received.

(2) Any necessary notice must be given by a bank before its midnight deadline and by any other person before midnight of the third business day after dishonor or receipt of notice of dishonor.

(3) Notice may be given in any reasonable manner. It may be oral or written and in any terms which identify the instrument and state that it has been dishonored. A misdescription which does not mislead the party notified does not vitiate the notice. Sending the instrument bearing a stamp, ticket or writing stating that acceptance or payment has been refused or sending a notice of debit with respect to the instrument is sufficient.

(4) Written notice is given when sent although it is not received.

(5) Notice to one partner is notice to each although the firm has been dissolved.

(6) When any party is in insolvency proceedings instituted after the issue of the instrument notice may be given either to the party or to the representative of his estate.

(7) When any party is dead or incompetent notice may be sent to his last known address or given to his personal representative.

(8) Notice operates for the benefit of all parties who have rights on the instrument against the party notified."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

DECISIONS UNDER U.C.C. PRIOR TO 1991 REVISION

Oral Notice of Dishonor Insufficient Under Circumstances: Oral notice of dishonor of check was insufficient to release payor bank from strict liability rule under 30-4-302 where bank president told payee that, although it would take time, checks would clear because things were looking better but checks were never paid and bank made withdrawals from drawer's account to apply against loans not in default. Sun River Cattle Co., Inc. v. Miners Bank of Mont., 164 M 237, 521 P2d 679 (1974).

DECISIONS UNDER UNIFORM NEGOTIABLE INSTRUMENTS LAW

Drawer's Whereabouts Unknown: Under sections 55-824 and 55-825, R.C.M. 1947 (now repealed), where the drawer of a check was out of the state at the time of its dishonor and despite the efforts of the holder to ascertain his whereabouts could not be reached until the bank upon which drawn had closed its doors, a finding exculpating the holder for failure to give notice sooner was warranted. Cellars v. Dwinnell, 87 M 73, 285 P 181 (1930).

Attorney General's Opinions

"Banking Day": Saturday should not be considered a banking day for the purposes of this section for banks open on Saturday for limited teller transactions. 36 A.G. Op. 91 (1976).

30-3-510. Evidence of dishonor.

Official Comment

Source: Section 3-505, U.C.C.

Official Comment to 1991 Amendment:

Protest is no longer mandatory but must be requested by the holder. Even if requested, protest is not a condition to the liability of indorsers or drawers. Protest is a service provided by the banking system to establish that dishonor has occurred. Like other services provided by the banking system, it will be available if market incentives, interbank agreements, or governmental regulations require it, but liabilities of parties no longer rest on it.

Compiler's Comments

1991 Amendment: At end of catchline deleted "and notice of dishonor"; in (1)(a), before "purports", substituted "subsection (2) that" for "the preceding section which"; in (1)(b), after "refused", inserted "unless reasons for the refusal are stated and the" and after "reasons" inserted "are not"; inserted (2) concerning protest made by certain persons; and made minor changes in style.

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

DECISIONS UNDER U.C.C. PRIOR TO 1991 REVISION

Promissory Note — Undue Influence in Making: A promissory note was executed to appellant by the deceased with whom he had a close confidential relationship. The decedent's age caused her to rely quite heavily on appellant in running her farm and made her more susceptible to his influence. The amount of the note was also quite large in relation to the alleged consideration. Under the five-factor test enumerated in Cameron v. Cameron, 179 M 219, 587 P2d 939 (1978), there was substantial evidence to support a finding of undue influence in the creation of the note. Heintz v. Vestal, 185 M 233, 605 P2d 606 (1980).

30-3-512. Dishonor.

Official Comment

Source: Section 3-502, U.C.C.

Official Comment:

1. Section 3-415 [30-3-414] provides that indorsers are obliged to pay an instrument if the instrument is dishonored and are discharged if they are entitled to notice of dishonor and notice is not given. Under Section 3-414 [30-3-423], the drawer is obliged to pay an unaccepted draft if it is dishonored. The drawer, however, is not entitled to notice of dishonor except to the extent required in a case governed by Section 3-414(c) [30-3-423(3)]. Part 5 tells when an instrument is dishonored (Section 3-502 [30-3-512]) and what it means to give notice of dishonor (Section 3-503 [30-3-508]). Often dishonor does not occur until presentment (Section 3-501 [30-3-504]), and frequently presentment and notice of dishonor are excused (Section 3-504 [30-3-513]).

2. In the great majority of cases presentment and notice of dishonor are waived with respect to notes. In most cases a formal demand for payment from the maker of the note is not contemplated. Rather, the maker is expected to send payment to the holder of the note on the date or dates on which payment is due. If payment is not made when due, the holder usually makes a demand for payment, but in the normal case in which presentment is waived, demand is irrelevant and the holder can proceed against indorsers when payment is not received. In the small minority of cases in which presentment and dishonor are not waived with respect to notes, the present law discharges the indorser from liability (proposed Section 3-502(1)(a) [30-3-512(1)(a)]) unless the holder makes formal presentment to the maker on the exact day the note is due (proposed Section 3-503(1)(c) [30-3-508(1)(c)]) and gives notice of dishonor to the indorser before midnight of the third business day after dishonor (proposed Section 3-508(2) [30-3-508(2)]).

The present procedure is unnecessarily technical and outmoded. Proposed Section 3-502 [30-3-512] is a change in the law that would recognize and accommodate modern methods of doing business. Under both present Section 3-413 [30-3-413 prior to 1991 revision] and proposed Section 3-412 [30-3-413], the obligation of the maker of a note to pay the note does not depend upon presentment and dishonor. Moreover, there is no reason to require a formal presentment to the maker to hold the indorser unless the note is payable on demand, presentment is required by the terms of the note, or the note is payable at or through a bank.

3. Subsection (a) [subsection (1) of this section] applies to notes. Subsection (a)(1) [subsection (1)(a) of this section] applies to notes payable on demand. Dishonor requires presentment, and dishonor occurs if payment is not made on the day of presentment. There is no change in present law. Subsection (a)(2) [subsection (1)(b) of this section] applies to notes payable at a definite time if the note is payable at or through a bank or, by its terms, presentment is required. Dishonor requires presentment and dishonor occurs if payment is not made on the due date or the day of presentment if presentment is made after the due date. Subsection (a)(3) [subsection (1)(c) of this section] applies to all other notes. If the note is not paid on its due date it is dishonored. This allows holders to collect notes in ways that make sense commercially without having to be concerned about a formal presentment on a given day.

4. Subsection (b) [subsection (2) of this section] applies to unaccepted drafts other than documentary drafts. Subsection (b)(1) [subsection (2)(a) of this section] applies to checks. Except for checks presented for immediate payment over the counter, which are covered by subsection (b)(2) [subsection (2)(b) of this section], dishonor occurs according to rules stated in Article 4 [Title 30, chapter 4]. When a check is presented for payment through the check-collection system, the drawee bank normally makes a provisional settlement, i.e. provisional payment, for the amount of the check to the presenting bank. Under Section 4-301 [30-4-301] the drawee bank may revoke this settlement if it returns the check within its midnight deadline (Section 4-104 [30-4-104]). In that case the check is not paid and dishonor occurs under Section 3-502(b)(1) [30-3-512(2)(a)]. If the drawee bank does not return the check or give notice of dishonor or nonpayment within the

midnight deadline, the provisional settlement becomes final payment of the check. Section 4-215 [30-4-213]. Thus, no dishonor occurs regardless of whether the check is retained or is returned after the midnight deadline. In some cases the drawee bank might not settle for the check when it is received. Under Section 4-302 [30-4-302] if the drawee bank retains the check without settling for it beyond midnight of the day it is presented for payment, the bank becomes "accountable" for the amount of the check, i.e. it is obliged to pay the amount of the check. In this case the check has not been paid and, under Section 3-502(b)(1) [30-3-512(2)(a)], the check is dishonored. The fact that the bank is obliged to pay the check does not mean that the check has been paid. When a check is presented for payment, the person presenting the check is entitled to payment not just the obligation of the drawee to pay. Until that payment is made, the check is dishonored. To say that the drawee bank is obliged to pay the check necessarily means that the check has not been paid. If the check is eventually paid, the drawee bank no longer is accountable.

Subsection (b)(2) [subsection (2)(b) of this section] applies to demand drafts other than those governed by subsection (b)(1) [subsection (2)(a) of this section]. It covers checks presented for immediate payment over the counter and demand drafts other than checks. Dishonor occurs if presentment for payment is made and payment is not made on the day of presentment.

Subsection (b)(3) and (4) [subsections (2)(c) and (2)(d) of this section] applies to time drafts. An unaccepted time draft differs from a time note. The maker of a note knows that the note has been issued, but the drawee of a draft may not know that a draft has been drawn on it. Thus, with respect to drafts, presentment for payment or acceptance is required. Subsection (b)(3) [subsection (2)(c) of this section] applies to drafts payable on a date stated in the draft. Dishonor occurs if presentment for payment is made and payment is not made on the day the draft becomes payable or the day of presentment if presentment is made after the due date. The holder of an unaccepted draft payable on a stated date has the option of presenting the draft for acceptance before the day the draft becomes payable to establish whether the drawee is willing to assume liability by accepting. Under subsection (b)(3)(ii) [subsection (2)(c)(ii) of this section] dishonor occurs when the draft is presented and not accepted. Subsection (b)(4) [subsection (2)(d) of this section] applies to unaccepted drafts payable on elapse of a period of time after sight or acceptance. If the draft is payable 30 days after sight, the draft must be presented for acceptance to start the running of the 30-day period. Dishonor occurs if it is not accepted. The rules in subsection (b)(3) and (4) [subsections (2)(c) and (2)(d) of this section] follow present Section 3-501(1)(a) [30-3-501, now repealed].

5. Subsection (c) [subsection (3) of this section] gives drawees an extended period to pay documentary drafts because of the time that may be needed to examine the documents. The period prescribed is that given by Section 5-112 [30-5-112, now repealed] in cases in which a letter of credit is involved.

6. Subsection (d) [subsection (4) of this section] governs accepted drafts. If the acceptor's obligation is to pay on demand the rule, stated in subsection (d)(1) [subsection (4)(a) of this section], [i]s the same as for that of a demand note stated in subsection (a)(1) [subsection (1)(a) of this section]. If the acceptor's obligation is to pay at a definite time the rule, stated in subsection (d)(2) [subsection (4)(b) of this section], is the same as that of a time note payable at a bank stated in subsection (b)(2) [subsection (2)(b) of this section].

7. Subsection (e) [subsection (5) of this section] is a limitation on subsection (a)(1) and (2), subsection (b), subsection (c), and subsection (d) [subsections (1)(a), (1)(b), and (2) through (4) of this section]. Each of those provisions states dishonor as occurring after presentment. If presentment is excused under Section 3-504 [30-3-513], dishonor occurs under those provisions without presentment if the instrument is not duly accepted or paid.

8. Under subsection (b)(3)(ii) and (4) [subsections (2)(c)(ii) and (2)(d) of this section] if a draft is presented for acceptance and the draft is not accepted on the day of presentment, there is dishonor. But after dishonor, the holder may consent to late acceptance. In that case, under subsection (f) [subsection (6) of this section], the late acceptance cures the dishonor. The draft is treated as never having been dishonored. If the draft is subsequently presented for payment and payment is refused dishonor occurs at that time.

Case Notes

DECISIONS UNDER U.C.C. PRIOR TO 1991 REVISION

Dishonor of Sight Draft — Absence of Date of Acceptance: When the holder of a 160-day sight draft, upon which the drawee had failed to provide written acceptance or date thereof, supplied a date of presentment as provided under 30-3-410, the payee was entitled to treat the draft as dishonored when he did not receive payment within 160 days of the date he had supplied. Clawson v. Berklund, 188 M 48, 610 P2d 1168 (1980).

Promissory Note — Undue Influence in Making: A promissory note was executed to appellant by the deceased with whom he had a close confidential relationship. The decedent's age caused her to rely quite heavily on appellant in running her farm and made her more susceptible to his influence. The amount of the note was also quite large in relation to the alleged consideration. Under the five-factor test enumerated in Cameron v. Cameron, 179 M 219, 587 P2d 939 (1978), there was substantial evidence to support a finding of undue influence in the creation of the note. Heintz v. Vestal, 185 M 233, 605 P2d 606 (1980).

30-3-513. Excused presentment and notice of dishonor.

Official Comment

Source: Section 3-504, U.C.C.

Official Comment:

Section 3-504 [30-3-513] is largely a restatement of present Section 3-511 [30-3-511, now repealed]. Subsection (4) of present Section 3-511 [30-3-511, now repealed] is found in proposed Section 3-502(f) [30-3-512(6)].

Case Notes

DECISIONS UNDER U.C.C. PRIOR TO 1991 REVISION

Applicability: Subsection (4) does not apply to demand items. Payor bank was not excused from failure to comply with "midnight deadline" rule of 30-4-302 by subsection (4) of this section where checks presented by payees were demand items. Sun River Cattle Co., Inc. v. Miners Bank of Mont., 164 M 237, 521 P2d 679 (1974).

DECISIONS UNDER UNIFORM NEGOTIABLE INSTRUMENTS LAW

Burden of Proof: In the absence of proof showing the length of time for which the check in this action was held by the bank upon which drawn before returning it dishonored, the contention of defendant drawer that the bank having held it for more than 24 hours, his obligation thereon was discharged under section 55-1106, R.C.M. 1947 (now repealed), may not be sustained; the burden of proving payment in this manner having been upon him. Cellars v. Dwinnell, 87 M 73, 285 P 181 (1930).

Drawer's Whereabouts Unknown: Under sections 55-824 and 55-825, R.C.M. 1947 (now repealed), where the drawer of a check was out of the state at the time of its dishonor and despite efforts of the holder to ascertain his whereabouts could not be reached until the bank upon which drawn had closed its doors, a finding exculpating the holder for failure to give notice sooner was warranted. Cellars v. Dwinnell, 87 M 73, 285 P 181 (1930).

Application to Checks: The provisions of sections 55-1105 and 55-1106, R.C.M. 1947 (now repealed), that the drawee of a bill of exchange is allowed 24 hours after presentment in which to decide whether he will or will not accept it, and will be deemed to have accepted it if he fails to return it within that time, are applicable to a check which, under section 55-1702, R.C.M. 1947 (now repealed), is declared to be a bill of exchange drawn on a bank. Blackwelder v. Fergus Motor Co., 80 M 374, 260 P 734 (1927); Clarke v. Nat'l Bank of Mont., 78 M 48, 252 P 373 (1926).

Payment of Interest: Payment of interest by an endorser after maturity waives notice of dishonor. Morgan v. Huffman, 76 M 396, 247 P 326 (1926).

Part 6
Discharge

30-3-601. Discharge and effect of discharge.

Official Comment

Source: Section 3-601, U.C.C.

Prior Uniform Statutory Provision: Sections 119, 120 and 121, Uniform Negotiable Instruments Law.

Official Comment to 1991 Amendment:

Subsection (a) [subsection (1) of this section] restates subsections (1) and (2) of present Section 3-601 [30-3-601(1) and (2) prior to 1991 revision]. Subsection (b) [subsection (2) of this section] restates present Section 3-602 [30-3-602, now repealed]. Notice of discharge is not treated as notice of a defense that prevents holder in due course status. Section 3-302(b) [30-3-302(2)]. Discharge is effective against a holder in due course only if the holder had notice of the discharge when holder in due course status was acquired. For example, if an instrument bearing a canceled indorsement is taken by a holder, the holder has notice that the indorser has been discharged. Thus, the discharge is effective against the holder even if the holder is a holder in due course.

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "Discharge of parties. (1) The extent of the discharge of any party from liability on an instrument is governed by the sections on:

(a) payment or satisfaction (30-3-603); or
(b) tender of payment (30-3-604); or
(c) cancellation or renunciation (30-3-605); or
(d) impairment of right of recourse or of collateral (30-3-606); or
(e) reacquisition of the instrument by a prior party (30-3-208); or
(f) fraudulent and material alteration (30-3-407); or
(g) certification of a check (30-3-411); or
(h) acceptance varying a draft (30-3-412); or
(i) unexcused delay in presentment or notice of dishonor or protest (30-3-502).

(2) Any party is also discharged from his liability on an instrument to another party by any other act or agreement with such party which would discharge his simple contract for the payment of money.

(3) The liability of all parties is discharged when any party who has himself no right of action or recourse on the instrument:

(a) reacquires the instrument in his own right; or
(b) is discharged under any provision of this chapter, except as otherwise provided with respect to discharge for impairment of recourse or of collateral (30-3-606)."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

DECISIONS UNDER UNIFORM NEGOTIABLE INSTRUMENTS LAW

Exoneration by Death of Surety: Where deceased had previously cosigned a promissory note for the purpose of lending his name to another party, he became an accommodation maker. As such he is primarily responsible for the payment of the note, without necessity of resort to the principal, and it was error for the District Court to disallow the holder's claim against the deceased's estate. In re Estate of Harbaugh, 196 M 274, 639 P2d 495, 39 St. Rep. 84 (1982).

Existing Indebtedness: The execution of new notes and mortgage security therefor on surrender and cancellation of the first notes does not extinguish the existing indebtedness, and the only effect thereon is to extend the time of payment. White v. Hulls, 59 M 98, 195 P 850 (1921).

Construction: Section 55-901, R.C.M. 1947 (now repealed), relates only to a discharge of the instrument and not to a discharge of the parties. Merchants' Nat'l Bank of Billings v. Smith, 59 M 280, 196 P 523, 15 ALR 430 (1921).

Check or Draft: A check is merely an order for money, and in the absence of any agreement to the contrary its acceptance in discharge of an indebtedness is conditioned upon its payment. U.S. Nat'l Bank of Red Lodge v. Shupak, 54 M 542, 172 P 324 (1918). See also Advance-Rumely Thresher Co., Inc. v. Hess, 85 M 293, 279 P 236 (1929).

Renewal Instrument: The giving of a renewal note does not operate as a payment or discharge in the absence of an agreement to that effect. Stamping the note "paid" does not change this rule. First St. Bank of Hilger v. Lang, 55 M 146, 174 P 597, 9 ALR 1139 (1918).

30-3-603. Payment.

Official Comment

Source: Section 3-602, U.C.C.

Prior Uniform Statutory Provision: Sections 51, 88, 119, 121 and 171-177, Uniform Negotiable Instruments Law.

Official Comment to 1991 Amendment:

This section is based on present Section 3-603(1) [30-3-603(1) prior to 1991 revision]. "Claims to an instrument" is defined in Section 3-306 [30-3-306] to mean a claim of ownership or possession and not a claim in recoupment. Subsection (b)(1)(ii) [subsection (2)(a)(ii) of this section] is added to conform to Section 3-411 [30-3-421]. Payment of a cashier's check, teller's check, or certified check discharges the obligor even though indemnity has been given by the person asserting the claim. The obligor is not discharged if payment is made in violation of an injunction against payment.

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "Payment or satisfaction. (1) The liability of any party is discharged to the extent of his payment or satisfaction to the holder even though it is made with knowledge of a claim of another person to the instrument unless prior to such payment or satisfaction the person making the claim either supplies indemnity deemed adequate by the party seeking the discharge or enjoins payment or satisfaction by order of a court of competent jurisdiction in an action in which the adverse claimant and the holder are parties. This subsection does not, however, result in the discharge of the liability:

(a) of a party who in bad faith pays or satisfies a holder who acquired the instrument by theft or who (unless having the rights of a holder in due course) holds through one who so acquired it; or

(b) of a party (other than an intermediary bank or a payor bank which is not a depositary bank) who pays or satisfies the holder of an instrument which has been restrictively endorsed in a manner not consistent with the terms of such restrictive endorsement.

(2) Payment or satisfaction may be made with the consent of the holder by any person including a stranger to the instrument. Surrender of the instrument to such a person gives him the rights of a transferee (30-3-201)."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

DECISIONS UNDER U.C.C. PRIOR TO 1991 REVISION

Foreclosure of Mortgage Securing Note — Payment to Holder Required: The Dahls executed a note to Sythe and also executed a real estate mortgage in Sythe's favor. The note was placed in an escrow account in the Culbertson State Bank, and the bank was designated as the place where payment was to be made. Sythe assigned the note to the bank as security for a note obtained by him. Sythe later gave the bank a written assignment of the mortgage. Defendant Dahl was given written notice of this assignment. The bank did not receive any payments from Sythe on his notes or from Dahl on the note assigned to the bank. The bank brought an action for the foreclosure of the mortgage against Dahl. Dahl contended that the note was discharged because it was paid in full, with payments being made to Sythe. The bank was never able to make service of process on Sythe. The bank was a "holder" of the note since it was in possession of the note endorsed by Sythe. As a holder and having produced the note, the bank was entitled to recover unless the defendant established a defense. Defendant's sole defense was that he had paid the note to Sythe. The defense of payment only discharges the maker's liability on the instrument if payment is made to the holder. Defendant never attempted to prove payment to the holder. Since the bank was the holder of the note and a valid assignee of the mortgage securing the note, it was entitled to a decree of foreclosure. Culbertson St. Bank v. Dahl, 190 M 33, 617 P2d 1295, 37 St. Rep. 1752 (1980).

DECISIONS UNDER UNIFORM NEGOTIABLE INSTRUMENTS LAW

Pleading Payment: The defense of payment is new matter and a special affirmative defense and if relied on must be pleaded specially. Jensen v. Franklin, 135 M 341, 340 P2d 832 (1959).

Presumption of Payee's Ownership: In payee's action on notes, formal allegation in complaint that payee is still owner and holder was unnecessary where execution and delivery of the instrument and default of the maker or acceptor was alleged, since payee's ownership will be presumed from such facts. Parkinson v. Diefenderfer, 128 M 547, 280 P2d 424 (1955).

Evidence Required to Prove Payment: In order to justify a verdict for defendant under a plea of payment, defendant must introduce sufficient evidence to rebut the prima facie case made out by the plaintiff's possession of the note, and also outweigh any other evidence of nonpayment. Vesel v. Polich Trading Co., 96 M 118, 28 P2d 858 (1934).

Possession by Maker: Possession of a note by the maker is prima facie evidence of its payment. Anderson v. Border, 87 M 4, 285 P 174 (1930).

Sale and Payment Distinguished: Where the holder of a promissory note endorsed it and delivered it to a bank as collateral to secure his note to it, and a stranger to the transaction paid the latter note, the bank neither endorsing nor assigning it to him but simply surrendering it to him together with the note given as collateral, there was no sale of either note but the transaction resulted in a voluntary payment of the note so paid, and the maker was entitled to a return of the collateral. Watterson v. Hill, 84 M 549, 276 P 948 (1929), distinguished in Kennedy v. Conrad, 91 M 356, 9 P2d 1075 (1932).

Voluntary Payment by Another: Payment by one of the debt of another with full knowledge of the facts, or without the latter's request or promise to repay, is voluntary; by it the obligation is discharged and the volunteer cannot compel reimbursement. Watterson v. Hill, 84 M 549, 276 P 948 (1929).

Parol Evidence: Parol evidence is not admissible to show that a note containing an absolute promise to pay a specified amount of money at a stated time was by agreement of the parties to be paid out of a particular fund. Swan v. LeClair, 77 M 422, 251 P 155 (1926).

Payment on New Note: Payment on the new note is to be credited to the payor in an action on old note retained as collateral. Swan v. LeClair, 77 M 422, 251 P 155 (1926).

Bank as Agent: The bank at which a note is made payable is the agent of the payee to receive payment. Dehnert v. Union Cent. Life Ins. Co., 74 M 104, 239 P 773 (1925).

Accommodation Maker: An accommodation maker is not released by any act which releases the sureties. Merchants' Nat'l Bank of Billings v. Smith, 59 M 280, 196 P 523, 15 ALR 430 (1921).

Acceptance by Agent: An agent has no implied authority to accept payment in anything but money. U. S. Nat'l Bank of Red Lodge v. Shupak, 54 M 542, 172 P 324 (1918). See also First St. Bank of Hilger v. Lang, 55 M 146, 174 P 597, 9 ALR 1139 (1918).

Release of Comaker: Where a note is joint and several, payment by one of the makers extinguishes the liability of all. First Nat'l Bank of Butte v. Silver, 45 M 231, 122 P 584 (1912).

Complaint: In an action on a note, an allegation of nonpayment is material and essential. First Nat'l Bank of Butte v. Silver, 45 M 231, 122 P 584 (1912).

Possession by Person Other Than Maker: The possession of an uncanceled note by a person other than the maker is prima facie evidence that the debt evidenced thereby is unpaid. McCauley v. Darrow, 36 M 13, 91 P 1059 (1907).

30-3-604. Tender of payment.

Official Comment

Source: Section 3-603, U.C.C.

Prior Uniform Statutory Provision: Sections 70 and 120, Uniform Negotiable Instruments Law.

Official Comment to 1991 Amendment:

Section 3-603 [30-3-604] replaces present Section 3-604 [30-3-604 prior to 1991 revision]. Proposed subsection (a) [subsection (1) of this section] generally incorporates the law of tender of payment applicable to simple contracts. Subsections (b) and (c) [subsections (2) and (3) of this section] state particular rules. Subsection (b) [subsection (2) of this section] restates present Section 3-604(2) [30-3-604(2) prior to 1991 revision]. Under subsection (b) [subsection (2) of this section] refusal of a tender of payment discharges any indorser or accommodation party having a right of recourse against the party making the tender. Subsection (c) [subsection (3) of this section] restates present Section 3-604(1) and (3) [30-3-604(1) and (3) prior to 1991 revision].

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "(1) Any party making tender of full payment to a holder when or after it is due is discharged to the extent of all subsequent liability for interest, costs and attorney's fees.

(2) The holder's refusal of such tender wholly discharges any party who has a right of recourse against the party making the tender.

(3) Where the maker or acceptor of an instrument payable otherwise than on demand is able and ready to pay at every place of payment specified in the instrument when it is due, it is equivalent to tender."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

DECISIONS UNDER U.C.C. PRIOR TO 1991 REVISION

No Default When Agreement Made to Accept Full Payment: The defendant requested payment on a promissory note and was notified of plaintiff's intention to pay off the entire amount due. Defendant agreed by phone to accept full payment by mail, and plaintiff sent a check for the balance. Defendant later argued that plaintiff had defaulted on the note. The District Court found that plaintiff was not in default. On appeal, the Supreme Court affirmed, noting that under 30-3-604 any party making tender of full payment to a holder when or after it is due is discharged to the extent of all subsequent liability for interest, costs, and attorney fees. Rauch v. Michel, 221 M 1, 716 P2d 617, 43 St. Rep. 587 (1986).

30-3-605. Discharge by cancellation or renunciation.

Official Comment

Source: Section 3-604, U.C.C.

Prior Uniform Statutory Provision: Sections 48, 119(3), 120(2), 122 and 123, Uniform Negotiable Instruments Law.

Official Comment to 1991 Amendment:

Proposed Section 3-604 [30-3-605] restates present Section 3-605 [30-3-605 prior to 1991 revision].

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "Cancellation and renunciation. (1) The holder of an instrument may even without consideration discharge any party:

(a) in any manner apparent on the face of the instrument or the endorsement, as by intentionally canceling the instrument or the party's signature by destruction or mutilation, or by striking out the party's signature; or

(b) by renouncing his rights by a writing signed and delivered or by surrender of the instrument to the party to be discharged.

(2) Neither cancellation nor renunciation without surrender of the instrument affects the title thereto."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

DECISIONS UNDER UNIFORM NEGOTIABLE INSTRUMENTS LAW

Sufficiency of Cancellation: Where a note payable at a bank was deposited by the holder with another bank as collateral security and the maker paid the note at the place of payment named therein and that bank remitted to the holder of the note the full amount of the payee's debt to it, the note was paid, the strict rule as to payment in absence of the note not being applicable where there was no loss. Union Bank & Trust Co. v. Lynn, 73 M 473, 237 P 490 (1925).

Rescinded Contract: Section 55-904, R.C.M. 1947 (now repealed), providing that the holder of a promissory note may in writing renounce his rights under it, was inapplicable to an action by the payee against the maker where the contract under which it was given was rescinded by mutual consent. Hollingsworth v. Ruckman, 72 M 147, 232 P 180 (1924).

30-3-607. Discharge of indorsers and accommodation parties.

Official Comment

Source: Section 3-605, U.C.C.

Official Comment:

1. A person who needs credit may not be able to obtain it unless some other person is willing to incur liability to pay the debt if the credit is granted. In the typical case a note represents the debt. For example, Bank lends $10,000 to Borrower who signs a note under which Borrower is obliged to pay $10,000 to Bank on a due date stated in the note. Bank insists, however, that Accommodation Party also become liable to pay the note. Accommodation Party can incur this liability by signing the note as a co-maker or by indorsing the note. In either case the note is signed for accommodation and Borrower is the accommodated party. Rights and obligations of Accommodation Party in this case are stated in Section 3-419 [30-3-415]. Suppose that after the note is signed, Bank agrees to a modification of the rights and obligations between Bank and Borrower. For example, Bank agrees that Borrower may pay the note at some date after the due date, or that Borrower may discharge Borrower's $10,000 obligation to pay the note by paying Bank $3,000, or that Bank releases collateral given by Borrower to secure the note. Under the law of suretyship a surety or guarantor of a debt, such as Accommodation Party in our example, can be discharged under certain circumstances if changes of this kind are made by Bank without the consent of Accommodation Party. Rights of the surety to discharge in such cases are commonly referred to as suretyship defenses. Section 3-605 [30-3-607] is concerned with this kind of problem in the context of a negotiable instrument to which the principal debtor and the surety are parties. But Section 3-605 [30-3-607] has a wider scope. It also applies to indorsers who are not accommodation parties. For example, if Bank in our hypothetical case indorsed the note and transferred it to Bank #2, Bank has rights given to an indorser under Section 3-605 [30-3-607] if it is Bank #2 that modifies rights and obligations of Borrower. The scope of Section 3-605 [30-3-607] is also widened by subsection (f) [subsection (6) of this section]

which deals with rights of a person such as a co-maker of a note who is not an accommodation party when collateral is impaired.

2. The importance of suretyship defenses is greatly diminished by the fact that they can be waived. The waiver is usually made by a provision in the note or other writing that represents the obligation of the principal debtor. It is standard practice to include a waiver of suretyship defenses in notes given to financial institutions or other commercial creditors. Section 3-605(g) [30-3-607(7)] also allows waiver. Thus, Section 3-605 [30-3-607] applies to the occasional case in which the creditor did not include a waiver clause in the instrument or in which the creditor did not obtain the permission of the surety to take the action that triggers the suretyship defense.

3. Subsection (b) [subsection (2) of this section] addresses the effect of discharge under Section 3-604 [30-3-605] of the principal debtor. In the hypothetical case stated in Comment 1, release of Borrower by Bank does not release Accommodation Party. As a practical matter, Bank will not gratuitously release Borrower. Discharge will arise in the context of a settlement with a debtor who is insolvent or in financial difficulty. If Borrower is unable to pay all creditors, it may be prudent for a creditor to take partial payment, but Borrower will normally insist on a release of the obligation. If Bank takes $3,000 and releases Borrower from the $10,000 debt, Accommodation Party is not injured. To the extent of the payment Accommodation Party's obligation to Bank is reduced. The release of Borrower by Bank does not affect the right of Accommodation Party to obtain reimbursement from Borrower if Accommodation Party pays Bank. Section 3-419(e) [30-3-415(5)]. Subsection (b) [subsection (2) of this section] is designed to allow a creditor to settle with the principal debtor without risk of losing rights against the accommodation party or indorser. Settlement is in the interest of secondary parties as well as the creditor. Subsection (b) [subsection (2) of this section] changes the law, but the change relates largely to formalities rather than substance. Under the present law, Bank can settle with and release Borrower without releasing Accommodation Party, but to accomplish that result Bank has to either obtain the consent of Accommodation Party or make an express reservation of rights against Accommodation Party at the time it releases Borrower. The hoary doctrine of reservation of rights has very little to recommend it. The reservation of rights is made in the agreement between Bank and Borrower by which the release of Borrower is made and is binding on Accommodation Party even though Accommodation Party has no knowledge of it. There is no requirement in present Section 3-606 [30-3-606, now repealed] that any notice be given to Accommodation Party. The reservation of rights doctrine is abolished in proposed Section 3-605 [30-3-607] with respect to rights on instruments.

4. Subsection (c) [subsection (3) of this section] relates to material modifications of the obligation of the principal debtor, including an extension of the due date of the instrument. In most cases an extension of time to pay a note is a benefit to both the principal debtor and parties having recourse against the debtor, but in some cases the extension may cause loss to the party having recourse by reducing the amount that the accommodation party or indorser will be able to recover on its right of recourse when default occurs. Present Section 3-606(1)(a) [30-3-606, now repealed] does not take into account the presence or absence of loss to the surety. For example, if the instrument is an installment note and the principal debtor is temporarily short of funds to pay a monthly installment, the payee may agree to extend the due date of the installment for a month or two to allow the debtor to pay when funds are available. Under present Section 3-606 [30-3-606, now repealed] an accommodation party or indorser is released if consent is not given unless the payee expressly reserves rights against the secondary party. It does not matter that the extension of time is a trivial change in the guaranteed obligation and that there is no evidence that the secondary party will suffer any loss because of the extension. Wilmington Trust Co. v. Gesullo, 29 U.C.C. Rep. 144 (Del. Super. Ct. 1980). On the other hand if the extension is for a long period of time the risk of the accommodation party may be substantially increased and loss may occur if there is a deterioration in the financial condition of the principal debtor that causes the debtor to be unable to pay during the period of extension.

Subsection (c) [subsection (3) of this section] changes the law in several respects. Present Section 3-606 [30-3-606, now repealed] applies to extensions of time but not to other modifications of the obligation of the principal debtor. There is no apparent reason why present Section 3-606 [30-3-606, now repealed] does not follow general suretyship law in covering both. Proposed Section 3-605(c) [30-3-607(3)] relates to both, but it distinguishes between extensions or other modifications that cause loss to the accommodation party or indorser and those that don't. Under subsection (c) [subsection (3) of this section] a material modification of the obligation of a party to an instrument will result in discharge of an indorser or accommodation party having a right of recourse against the obligor, unless the person enforcing the instrument proves lack of loss to the indorser or accommodation party. Loss refers to impairment of the value of the right of recourse. The issue will be presented when an action is brought to enforce the obligation of the indorser or accommodation party. The indorser or accommodation party that pays has a right of recourse against the principal debtor. If the person seeking enforcement can prove that the modification did not reduce the value of the right of recourse, there is no discharge. If the proof is that the modification caused only a partial reduction in the value of the right to recourse, discharge is limited to the amount of the reduction. For example, suppose the amount of an unsecured note is $10,000 and the original due date is April 1, 1988. In 1987 the payee of the note agrees to extend the due date to October 1, 1988. On October 1, 1988 the principal debtor has no assets and is in default on the note. Thus, the right of recourse of the accommodation party has no value on the extended due date. The accommodation party will lose $10,000 if required to pay the note. The payee brings an action against the accommodation party for $10,000, the amount of the note. If no proof is made with respect to loss caused by the modification, the accommodation party is discharged. But if the payee proves that the principal debtor did not have any assets on the original due date, there is no discharge because the extension of the due date did not cause loss. The accommodation party's loss would have been $10,000 even if no extension had occurred. If the payee proves that the principal debtor was insolvent on the original due date but that there were sufficient assets to allow debts to be paid 50 ¼ on the dollar, discharge is limited to $5,000, the amount of loss resulting from the extension.

The first sentence of subsection (g) [subsection (7) of this section] provides that an accommodation party is not discharged under subsection (c) [subsection (3) of this section] unless the person agreeing to the modification knows of the accommodation or has notice that the instrument was signed for accommodation in the case of an anomalous indorsement or a signature accompanied by words of guaranty. Section 3-419(c) [30-3-415(3)].

5. Subsection (d) [subsection (4) of this section] deals with discharge of indorsers or accommodation parties by impairment of collateral. It generally conforms to present Section 3-606(1)(b) [30-3-606, now repealed]. Subsection (f) [subsection (6) of this section] states in detail what is meant by impairment. The indorser or accommodation party is discharged to the extent the indorser or accommodation party proves that impairment was caused by a person entitled to enforce the instrument. For example, suppose the payee of a secured note fails to perfect the security interest. The collateral is owned by the principal debtor who subsequently files in bankruptcy. As a result of the failure to perfect, the security interest is not enforceable in bankruptcy. If the payee obtains payment from an accommodation party, the accommodation party is subrogated to the payee's security interest in the collateral. In this case the value of the security interest is impaired completely because the security interest is unenforceable. If the value of the collateral is as much or more than the amount of the note there is a complete discharge. The first sentence of subsection (g) [subsection (7) of this section] also applies to subsection (d) [subsection (4) of this section]. An accommodation party is not discharged unless the person causing the impairment knows of the accommodation or has notice of it. See the last paragraph to Comment 4.

In some states a real property grantee who assumes the obligation of the grantor as maker of a note secured by the real property becomes by operation of law a principal debtor and the grantor becomes a surety. The meager case authority is split on whether present Section 3-606 [30-3-606, now repealed] applies to release the grantor if the holder releases or extends the obligation of the grantee. Proposed Article 3 [Title 30, chapter 3] takes no position on the effect of the release of the grantor in this case. Proposed Section 3-605 [30-3-607] does not apply because the holder has not discharged the obligation of "a party to the instrument." The assuming grantee is not a party to the instrument.

6. Subsection (e) [subsection (5) of this section] is illustrated by the following case. X and Y sign a note for $1,000 as co-makers. Neither is an accommodation party. X grants a security interest in X's property to secure the note. The collateral is worth more than $1,000. Payee fails to perfect the security interest in X's property before X files in bankruptcy. As a result the security interest is not enforceable in bankruptcy. Had Payee perfected the security interest, Y could have paid the note and gained rights to X's collateral by subrogation. If the security interest had been perfected, Y could have realized on the collateral to the extent of $500 to satisfy its right of contribution against X. Payee's failure to perfect deprived Y of the benefit of the collateral. Subsection (e) [subsection (5) of this section] discharges Y to the extent of its loss. If there are no assets in the bankruptcy for unsecured claims, the loss is $500, the amount of Y's contribution claim against X which now has a zero value. If some amount is payable on unsecured claims, the loss is reduced by the amount receivable by Y. The same result follows if Y is an

accommodation party but Payee has no knowledge of the accommodation or notice under Section 3-419(c) [30-3-415(3)]. In that event Y is not discharged under subsection (d) [subsection (4) of this section], but subsection (e) [subsection (5) of this section] applies because X and Y are jointly and severally liable on the note. Under subsection (e) [subsection (5) of this section], Y is treated as a co-maker with a right of contribution rather than an accommodation party with a right of reimbursement. Y is discharged to the extent of $500. If Y is the principal debtor and X is the accommodation party subsection (f) [subsection (6) of this section] doesn't apply. Y, as principal debtor, is not injured by the impairment of collateral because Y would have been obliged to reimburse X for the entire $1,000 even if Payee had obtained payment from sale of the collateral.

7. The second sentence of subsection (g) [subsection (7) of this section] is a continuation of present law which allows suretyship defenses to be waived.

Case Notes

DECISIONS UNDER U.C.C. AFTER 1991 REVISION

No Impairment of Collateral Used to Secure Loan — No Exoneration of Surety: Plaintiff read and signed a promissory note to secure a small business loan for a friend who subsequently went bankrupt. The promissory note provided that plaintiff would secure the friend's loan with logging equipment that plaintiff had used to secure his loan. After defendant bank foreclosed on the logging equipment, plaintiff claimed that the bank improperly impaired the collateral and improperly subordinated plaintiff's loan to his friend's loan without plaintiff's knowledge, thereby relieving plaintiff, as surety, of the obligation to repay the loan. The bank contended that plaintiff was fully informed of the loan structure and the requirement that plaintiff's loan was junior to the friend's small business loan. The trial court weighed the conflicting evidence and agreed that the bank had explained to plaintiff that proceeds from the sale of the collateral would be applied to the small business loan first and that plaintiff's loan was structured to limit plaintiff's potential exposure while ensuring that plaintiff would not have to provide cash up front to help the friend secure the small business loan. On appeal, the Supreme Court declined to second-guess the trial court's findings regarding the conflicting testimony, and the trial court was affirmed. Denton v. First Interstate Bank of Commerce, 2006 MT 193, 333 M 169, 142 P3d 797 (2006).

Promissory Note Not Considered Contract of Adhesion: Plaintiff read and signed a promissory note to secure a loan for a friend who subsequently went bankrupt. The promissory note provided that plaintiff waived the right to rely on the defense of impairment. Nevertheless, after defendant bank foreclosed on the property that plaintiff used to secure the loan, plaintiff claimed impairment, arguing that the waiver constituted a contract of adhesion that was unenforceable. The District Court disagreed, and plaintiff appealed. The Supreme Court noted that a contract of adhesion is a contract whose terms are dictated by one party to another who has no voice in the contract's formulation and that the contract is unenforceable if it is not within the expectations of the weaker party or if the contract terms are unduly oppressive, unconscionable, or against public policy. Plaintiff was a sophisticated businessman who did not attempt to negotiate the contract terms and who studied the contract prior to signing and thus could not later claim that he was unaware of the waiver provision and that it was not within his reasonable expectations. Although the bank prepared the contract, the transaction was entered solely at plaintiff's behest, and plaintiff voluntarily waived the defense of collateral impairment under this section. Therefore, the Supreme Court concluded that the promissory note was not a contract of adhesion, nor were the contract's general provisions outside of plaintiff's reasonable expectations. The District Court was affirmed. Denton v. First Interstate Bank of Commerce, 2006 MT 193, 333 M 169, 142 P3d 797 (2006), following Kloss v. Edward D. Jones & Co., 2002 MT 129, 310 M 123, 54 P3d 1 (2002).

DECISIONS UNDER U.C.C. PRIOR TO 1991 REVISION

Clear Language of Surety Agreement Binds Surety — Impairment of Collateral: Plaintiff contended that he was entitled to discharge from his surety agreement under Montana statutes on the remedies and rights of a surety. He claimed that the creditor bank's unconsented release of collateral, which exposed plaintiff to increased liability, discharged him from the surety agreement. The Supreme Court held that plaintiff is not entitled to be discharged as an original obligor because the clear language of the surety agreement makes him liable and allows the creditor bank to realize on any collateral it held without obtaining plaintiff's consent. Mont. Bank of Livingston v. Old Saloon, Inc., 235 M 244, 766 P2d 878, 45 St. Rep. 2354 (1988).

DECISIONS UNDER UNIFORM NEGOTIABLE INSTRUMENTS LAW

Impairment of Collateral — Defenses of Accommodation Maker: A Shaklee distributor negotiated with Storms Trust for a $10,000 loan to increase his inventory. Trustee Storms drafted a promissory note but refused to approve the loan until the distributor's wife had signed the note. The agreement granted Storms a security interest in the purchased inventory, yet Storms failed to record the security agreement. The distributor subsequently secured a second loan from a bank, which filed a financing statement on the inventory. The distributor defaulted on both loans. Storms took possession of the inventory but relinquished possession upon the bank's demand. Storms obtained a judgment against both the distributor and his wife. Wife appealed a District Court judgment for the full balance due on the promissory note and contract, contending she was discharged from liability on the note because Storms failed to perfect a security interest in the inventory, causing an impairment of collateral. Storms argued the wife was primarily liable as co-maker without benefit of defenses. The court stated that the law discharges all parties who occupy the position of a surety, including accommodation makers, endorsers, and acceptors. At the note signing, Storms had notice that the wife signed merely to aid her husband in obtaining the loan. Therefore, the wife was an accommodation maker entitled to the benefit of the defense of discharge. Storms' failure to perfect his security interest resulted in its loss to another secured party and entitled the wife to a discharge to the extent of the collateral's value. El-Ce Storms Trust v. Svetahor, 223 M 113, 724 P2d 704, 43 St. Rep. 1575 (1986).

Failure to Act:

Even if former corporate officers who endorsed corporation's note to Small Business Administration to effect that they guaranteed payment were sureties rather than guarantors, they were not exonerated from liability on note by Administration's failure to insist that new officers comply with agreement former officers had made with plaintiff to furnish quarterly financial statements and monthly lists of accounts receivable. U.S. v. Helena Office Supply Co., 256 F. Supp. 53 (D.C. Mont. 1966).

Small Business Administration, which made loan to corporation whose former officers endorsed back of note to effect that they guaranteed repayment and which did not insist that new officers comply with agreement former officers had made with it to furnish quarterly financial statements and monthly lists of accounts receivable, was chargeable with nothing more than non-action, not with action that would exonerate former officers of liability on note. U.S. v. Helena Office Supply Co., 256 F. Supp. 53 (D.C. Mont. 1966).

CHAPTER 4
UNIFORM COMMERCIAL CODE
BANK DEPOSITS AND COLLECTIONS

Chapter Commission Notes

Official Comment:

This draft of Article 4 [Title 30, chapter 4] makes several changes in the draft reviewed by the Conference at its August 1989 Meeting. These revisions result in part from a statement made in February 1990 by representative of the Board of Governors of the Federal Reserve System that the Board would probably be willing to assume regulatory control over the forward collection of checks if deemed appropriate by the NCCUSL, but that in any event the Federal Reserve is proceeding with a proposal relating to settlement for forward collection of checks and may well consider other changes to forward collection rules in the future. An extension of regulatory control by the Board over the entire check collection process is explicitly authorized by the Expedited Funds Availability Act of 1987.

Until the announcement by the Board's representatives, the Drafting Committee had proposed a number of amendments to conform Article 4 [Title 30, chapter 4] to new concepts of interbank settlements for checks embodied in Regulation CC. Since any regulations proposed by the Board would preempt these provisions, the Drafting Committee has withdrawn these amendments and has largely returned to the original text of Article 4 [Title 30, chapter 4]. If the Board issues comprehensive regulations, the functions of Article 4 [Title 30, chapter 4] will be: (1) to afford a residual, safety-net body of law applying to the check collection and return process to the extent not preempted by the Board's new regulations; (2) to continue to be the major source of statutory law for customer-bank relations; and (3) to govern the collection process for noncheck items.

The amendments to the original text of Article 4 [Title 30, chapter 4] found in this draft are proposed both to conform provisions of Article 4 [Title 30, chapter 4] to the new Article 3 [Title 30, chapter 3] as well as to clarify and up-date Article 4 [Title 30, chapter 4] in a number of areas in which problems have arisen under the present Act [prior to 1991 revision]. Among the conforming amendments are Sections 4-207 [30-4-207] and 4-208 [30-4-215] which conform the transfer and presentment warranties provisions of Article 4 [Title 30, chapter 4] to those in Article 3 [Title 30, chapter 3]. Section 4-111 [30-4-112] adds a statute of limitations to Article 4 [Title 30, chapter 4] that conforms to Section 3-118(g) [30-3-122(7)]. The reference to restrictive indorsements in present Section 4-205(2) [30-4-205(2) prior to 1991 revision] is deleted in order to leave coverage of restrictive indorsements to Section 3-206 [30-3-205]. Section 4-406 [30-4-406] is amended to include the modified comparative fault approach to loss allocation found in Sections 3-404, 3-405 and 3-406 [30-3-405, 30-3-420, and 30-3-406]. In the present version of Article 3 [Title 30, chapter 3, prior to 1991 revision], Sections 3-120 and 3-121 [30-3-120 and 30-3-121, both now repealed] deal with instruments "payable through" and "payable at" banks. These provisions have been removed from Article 3 [Title 30, chapter 3] and are combined in Section 4-106 [30-4-110].

Several amendments are required by the trend toward automation and, ultimately, truncation in the collection process. The process-of-posting test to determine when an item is paid is rejected as inappropriate for an [sic] regime of automated collection or truncation. "Accordingly, present Section 4-109 [30-4-109, now repealed] is deleted and conforming amendments are made in Sections 4-215 and 4-303 [30-4-213 and 30-4-303]. Encoding and retention warranties are added by Section 4-209 [30-4-216]. A provision authorizing truncation agreements is added as Section 4-110 [30-4-111]. The incapacity of an automated check clearing system based on MICR line information to accommodate postdated checks is recognized by adding Section 4-401(3) [30-4-401(3)]. The time for determining the insufficiency of an account is established in Section 4-402 [30-4-402]. Section 4-406 [30-4-406] is revised to accommodate new patterns of payor bank check retention and truncation plans.

Other provisions significantly modified are those on depositary bank as holder of an unindorsed item (Section 4-205 [30-4-205]) and the medium and time of settlement (Section 4-213 [30-4-211]). A number of sections have been clarified or expanded. Among these are the definitions of "account" (Section 4-104(1)(a) [30-4-104(1(a)]), "documentary draft" (Section 4-104(1)(f) [30-4-104(1)(f)]), "item" (Section 4-104(1)(h) [30-4-104(1)(h)]), "bank" (Section 4-105(a) [30-4-105(1)]), and "payor bank" (Section 4-105(c) [30-4-105(3)]), as well as substantive provisions on delays (Section 4-109 [30-4-108]), right of charge-back or refund (Section 4-214 [30-4-212]), final payment of item by payor bank (Section 4-215 [30-4-213]), payor bank's responsibility for late return of item (Section 4-302 [30-4-302]), when bank may charge customer's account (Section 4-401 [30-4-401]), bank's liability to customer for wrongful dishonor (Section 4-402 [30-4-402]), and customer's right to stop payment (Section 4-403 [30-4-403]).

Chapter Compiler's Comments

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Montana Compiler Changes: Compiler has changed the Official Comments by changing "Article" to "Chapter" wherever it appears, and by prefacing section numbers with Title 30 so as to reflect Montana's codification of the U.C.C.

Chapter Case Notes

Death of Partner — Disposition of Property Held Jointly by Partners: Robert and William, brothers, opened a joint checking account in 1947, paid all ranch expenses through the account, put all ranch income in the account, and equally split net profits. All cattle were branded with either of two brands, each of which was registered in the name of "William Palmer or Robert Palmer". The brothers were also joint tenants in a commodity brokerage account. The Supreme Court held that the cattle and both accounts were partnership property not held in joint tenancy and remained so upon Robert's death. Thus, they did not pass to William as the surviving joint tenant; rather, they remained in the partnership for the purpose of winding up the partnership and paying its liabilities, after which William must account to Robert's survivor, his widow, for Robert's share of the partnership. By its very nature, partnership property must be treated differently than property of individuals, including property held by individuals as joint tenants but who are not in partnership. This rule applies regardless of the formal legal manner in which the property is held. This is a rule of equity developed over hundreds of years and codified in the Uniform Partnership Act. In re Estate of Palmer, 218 M 285, 708 P2d 242, 42 St. Rep. 1585 (1985), followed in Fiedler v. Fiedler, 266 M 133, 879 P2d 675, 51 St. Rep. 691 (1994).

Part 1
General Provisions and Definitions

Part Case Notes

Drawer and Payee Identical — Circuitous Accountability: Checks were drawn on the account of Capital Preservation Fund, Inc., maintained with First National Bank of Great Falls, Montana, by John Bennett, an authorized signatory on the account. The checks were endorsed and deposited by Bennett in another account he maintained with the Ashford Bank of Houston, Texas. Ashford Bank sent the checks through normal banking channels and extended cash to Bennett in reliance on the checks. The checks, however, were dishonored by First National Bank. Ashford then charged back the account of Bennett but alleged that it sustained a loss of $500,000. An affidavit from the Federal Reserve Bank established that First National had timely returned the checks in advance of the "midnight deadline". Bennett contended that payment became final prior to dishonor because First National had completed the process of posting. Section 30-4-213 provides that "final" payment by a drawee bank is the point at which all "provisional" settlements as allowed by 30-4-104(1)(j) in the bank collection chain became "final" settlements. Typically, provisional credits given through a clearinghouse or mutual bank account are made final upon payment of the item by completion of the process of posting the drawer's account. The agency relationships established under 30-4-201 are thereby transformed into a series of debtor-creditor relationships ending with the depository bank indebted to its customer for the amount of the item. The right of a collecting bank under 30-4-212(1) to charge back the account of its customer for any credit given for an item terminates when payment on the item becomes final. Section 30-4-213 holds a "payor" bank accountable for an item once "final" payment has been rendered. The "payor" bank must act in a timely manner in either dishonoring or paying the instrument. Timely dishonor was established. Bennett in this instance had the roles of both a "drawer" and the "payee". To allow Bennett to allege that payment by First National, the "payor" bank, was final would result in circuitous accountability. First National would simply charge the account on which the checks were drawn, Capital Preservation Fund, Inc., in order to recoup the amount paid. Capital Preservation Fund, Inc., would in turn have a cause of action against Bennett for recovery of the money. Any litigation emanating from this unique factual situation properly was between Capital Preservation Fund, Inc., and Bennett. The cause of action against First National Bank was found to be illusory, and it was granted summary judgment. Ashford Bank v. Capital Preservation Fund, Inc., 544 F. Supp. 26, 39 St. Rep. 1385 (D.C. Mont. 1982).

Deposit of Check Made to Another — When No Customer Warranties Breached — When Settlement of Check Final: A bank initiated an action against a customer to recover the amount of a check she deposited. The check was a paycheck made out to her former husband. She had deposited his paychecks for a time, and the Supreme Court found an agency relationship in the situation. On the occasion leading to this action, the appellant had deposited the check unsigned to her checking account. The bank stamped the check "deposited to the credit of" and filled in the name of the former husband. Meanwhile, the former husband told the check's issuer his ex-wife had forged his name on the check and deposited it. The issuer completed necessary documents and issued a new check. The former husband then disappeared, being suspected of embezzlement. Whether the customer breached her warranties under the U.C.C. depended on whether the settlement on the check became final. The Supreme Court overruled the trial court and held the settlement had become final. The return of the check occurred after the posting. The bank where the check was deposited was not entitled to a refund under 30-4-212. The customer warranties issue was decided by the principle that an agency could not be denied by a principal accepting its benefits. Because the appellant was not in breach of customer warranties, the bank's remedy, if any, was against the maker or the payee, the appellant's former husband. First Nat'l Bank v. Nunn, 192 M 483, 628 P2d 1110, 38 St. Rep. 869 (1981).

30-4-101. Short title.

Official Comment

Source: Section 4-101, U.C.C.

Official Comment:

The tremendous number of checks handled by banks and the country-wide nature of the bank collection process require uniformity in the law of bank collections. Individual Federal Reserve banks process as many as 1,000,000 items a day; large metropolitan banks average 300,000 a day; banks with less than $5,000,000 on deposit handle from 1,000 to 2,000 daily. There is needed a uniform statement of the principal rules of the bank collection process with ample provision for flexibility to meet the needs of the large volume handled and the changing needs and conditions that are bound to come with the years.

The American Bankers Association Bank Collection Code, enacted in eighteen states, has stated many of the bank collection rules that have developed, and more recently Deferred Posting statutes have developed and varied further rules. With items flowing in great volume not only in and around metropolitan and smaller centers but also continuously across state lines and back and forth across the entire country, a proper situation exists for uniform rules that will state in modern concepts at least some of the rights of the parties and in addition aid this flow and not interfere with its progress.

This Chapter adopts many of the rules of the American Bankers Association Code that are still in current operation, the principles and rules of the Deferred Posting and other statutes, codifies some rules established by court decisions and in addition states certain patterns and procedures that exist even though not heretofore covered by statute.

30-4-102. Applicability.

Official Comment

Source: Section 4-102, U.C.C.

Purposes:

1. The rules governing negotiable instruments, their transfer, and the contracts of the parties thereto apply to the items collected through banking channels wherever no specific provision is found in this Chapter. In the case of conflict, this Chapter governs. See Section 30-3-103(2) [now repealed].

Bonds and like instruments constituting investment securities under Chapter 8 may also be handled by banks for collection purposes. Various sections of Chapter 8 prescribe rules of transfer some of which (see Sections 30-8-304 and 30-8-306, both repealed) may conflict with provisions of this Chapter (Sections 30-4-205 and 30-4-207). In the case of conflict, Chapter 8 governs.

Section 30-4-208 deals specifically with overlapping problems and possible conflicts between this Chapter and Chapter 9A. However, similar reconciling provisions are not necessary in the case of Chapters 5 and 7. Sections 30-4-301 and 30-4-302 are consistent with Section 30-5-112 [now repealed]. In the case of Chapter 7 documents of title frequently accompany items but they are not themselves items. See Section 30-4-104(g).

2. Subsection (2) is designed to state a workable rule for the solution of otherwise vexatious problems of the conflicts of laws:

a. The routine and mechanical nature of bank collections makes it imperative that one law govern the activities of one office of a bank. The requirement found in some cases that to hold an indorser notice must be given in accordance with the law of the place of indorsement, since that method of notice became an implied term of the indorser's contract, is more theoretical than practical.

b. Adoption of what is in essence a tort theory of the conflict of laws is consistent with the general theory of this Chapter that the basic duty of a collecting bank is one of good faith and the exercise of ordinary care. Justification lies in the fact that, in using an ambulatory instrument, the drawer, payee, and indorsers must know that action will be taken with respect to it in other jurisdictions. This is especially pertinent with respect to the law of the place of payment.

c. The phrase "action or nonaction with respect to any item handled by it for purposes of presentment, payment or collection" is intended to make the conflicts rule of subsection (2) apply from the inception of the collection process of an item through all phases of deposit, forwarding, presentment, payment and remittance or credit of proceeds. Specifically the subsection applies to the initial act of a depositary bank in receiving an item and to the incidents of such receipt. The conflicts rule of Weissman v. Banque de Bruxelles, 254 N.Y. 488, 173 N.E. 835 (1930), is rejected. The subsection applies to questions of possible vicarious liability of a bank for action or non-action of sub-agents (see Section 30-4-202(3)) and tests these questions by the law of the state of the location of the bank which uses the sub-agent. The conflicts rule of St. Nicholas Bank of New York v. State Nat. Bank, 128 N.Y. 26, 27 N.E. 849, 13 L.R.A. 241 (1891), is rejected. The subsection applies to action or non-action of a payor bank in connection with handling an item (see Sections 30-4-213(1), 30-4-301, 30-4-302, 30-4-303) as well as action or non-action of a collecting bank (Sections 30-4-201 through 30-4-214); to action or non-action of a bank which suspends payment or is affected by another bank suspending payment (Section 30-4-214); to action or non-action of a bank with respect to an item under the rules of Part 4 of Chapter 4.

d. Where subsection (2) makes this Chapter applicable, Section 30-4-103(1) leaves open the possibility of an agreement with respect to applicable law. Such freedom of agreement follows the general policy of Section 30-1-105 [now repealed].

Official Comment to 1991 Amendment:

This section is changed to indicate that in case of conflict the provisions of Article 5 [Title 30, chapter 5], as well as those of Article 8 [Title 30, chapter 8], govern those of Article 4 [Title 30, chapter 4].

Compiler's Comments

1991 Amendment: In (1), in two places, inserted reference to chapter 5; and made minor changes in style.

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

30-4-103. Variation by agreement — measure of damages — action constituting ordinary care.

Official Comment

Source: Section 4-103, U.C.C.

Prior Uniform Statutory Provision: See Sections 5 and 6 of the American Bankers Association Bank Collection Code.

Purposes:

1. Section 30-1-102 states the general principles and rules for variation of the effect of this Act by agreement and the limitations to this power. Section 30-4-103 states the specific rules for variation of Chapter 4 by agreement and also certain standards of ordinary care. In view of the technical complexity of the field of bank collections, the enormous number of items handled by banks, the certainty that there will be variations from the normal in each day's work in each bank, the certainty of changing conditions and the possibility of developing improved methods of collection to speed the process, it would be unwise to freeze present methods of operation by mandatory statutory rules. This section, therefore, permits within wide limits variation of provisions of the Chapter by agreement.

2. Subsection (1) confers blanket power to vary all provisions of the Chapter by agreements of the ordinary kind. The agreements may not disclaim a bank's responsibility for its own lack of good faith or failure to exercise ordinary care and may not limit the measure of damages for such lack or failure, but this subsection like Section 30-1-102(3) approves the practice of parties determining by agreement the standards by which such responsibility is to be measured. In the absence of a showing that the standards manifestly are unreasonable, the agreement controls. Owners of items and other interested parties are not affected by agreements under this subsection unless they are parties to the agreement or are bound by adoption, ratification, estoppel or the like.

As here used "agreement" has the meaning given to it by Section 30-1-201(3). The agreement may be direct, as between the owner and the depositary bank; or indirect, as where the owner authorizes a particular type of procedure and any bank in the collection chain acts pursuant to such authorization. It may be with respect to a single item; or to all items handled for a particular customer, e.g., a general agreement between the depositary bank and the customer at the time a deposit account is opened. Legends on deposit tickets, collection letters and acknowledgments of items, coupled with action by the affected party constituting acceptance, adoption, ratification, estoppel or the like, are agreements if they meet the tests of the definition of "agreement". See Section 30-1-201(3). First Nat. Bank of Denver v. Federal Reserve Bank, 6 F.2d 339 (8th Cir.1925) (deposit slip); Jefferson County Bldg. Ass'n v. Southern Bank & Trust Co., 225 Ala. 25, 142 So. 66 (1932) (signature card and deposit slip); Semingson v. Stock Yards Nat. Bank, 162 Minn. 424, 203 N.W. 412 (1925) (passbook); Farmers State Bank v. Union Nat. Bank, 42 N.D. 449, 454, 173 N.W. 789, 790 (1919) (acknowledgment of receipt of item).

3. Subsection (1) (subject to its limitations with respect to good faith and ordinary care) goes far to meet the requirements of flexibility. However, it does not by itself confer fully effective flexibility. When it is recognized that banks handle probably 25,000,000 items every business day and that the parties interested in each item include the owner of the item, the drawer (if it is a check), all non-bank indorsers, the payor bank and from one to five or more collecting banks, it is obvious that it is impossible, practically, to obtain direct agreements from all of these parties on all items. *En masse*, the interested parties constitute virtually every adult person and business organization in the United States. On the other hand they may become bound to agreements on the principle that collecting banks acting as agents have authority to make binding agreements with respect to items being handled. This conclusion was assumed but was not flatly decided in

Federal Reserve Bank of Richmond v. Malloy, 264 U.S. 160, at 167, 44 S.Ct. 296, at 298, 68 L.Ed. 617, 31 A.L.R. 1261 (1924).

To meet this problem subsection (2) provides that official or quasi-official rules of collection, that is Federal Reserve regulations and operating letters, clearing house rules, and the like, have the effect of agreements under subsection (1), whether or not specifically assented to by all parties interested in items handled. Consequently, such official or quasi-official rules may, standing by themselves but subject to the good faith and ordinary care limitations, vary the effect of the provisions of Chapter 4.

Federal Reserve regulations. Various sections of the Federal Reserve Act (12 U.S.C.A. § 221 et seq.) authorize the Board of Governors of the Federal Reserve System to direct the Federal Reserve banks to exercise bank collection functions. For example, Section 16 (12 U.S.C.A. § 248(o)) authorizes the Board to require each Federal Reserve bank to exercise the functions of a clearing house for its members and Section 13 (12 U.S.C.A. § 342) authorizes each Federal Reserve bank to receive deposits from non-member banks solely for the purposes of exchange or of collection. Under this statutory authorization the Board has issued Regulation J (Check Clearing and Collection), which has been infrequently amended over the many years during which it has been in force. (Regulation G, issued under comparable statutory authority, covers the handling of "non-cash items"). Where regulations issued by the Board in pursuance of its statutory mandate may be said to have some force of law and constitute an effective means of maintaining flexibility, it is appropriate to provide that such regulations may vary this Chapter even though not specifically assented to by all parties interested in items handled.

Federal Reserve operating letters. The regulations of the Federal Reserve Board authorize the Federal Reserve banks to promulgate rules covering operating details. Regulation J, for example, provides that each bank may promulgate rules "not inconsistent with the terms of the law or of this regulation governing the sorting, listing, packaging and transmission of items and other details of its check clearing and collection operation. Such rules . . . shall be set forth . . . in . . . letters of instructions to . . . member and non-member clearing banks." The term "operating letters" means these "letters of instructions", sometimes called "operating circulars", issued by the Federal Reserve banks under appropriate regulation of the Board. This Chapter recognizes such "operating letters" issued pursuant to the regulations and concerned with operating details as appropriate means, within their proper sphere, to vary the effect of the Chapter.

Clearing House Rules. Local clearing houses have long issued rules governing the details of clearing; hours of clearing, media of remittance, time for return of mis-sent items and the like. The case law has recognized such rules, within their proper sphere, as binding on affected parties and as appropriate sources for the courts to look to in filling out details of bank collection law. Subsection (2) in recognizing clearing house rules as a means of preserving flexibility continues the sensible approach indicated in the cases. Included in the term "clearing houses" are county and regional clearing houses as well as those within a single city or town. There is, of course, no intention of authorizing a local clearing house or a group of clearing houses to rewrite the basic law generally. The term "clearing house rules" should be understood in the light of functions the clearing houses have exercised in the past.

And the like. This phrase is to be construed in the light of the foregoing. "Federal Reserve regulations and operating letters" cover rules and regulations issued by public or quasi-public agencies under statutory authority. "Clearing house rules" cover rules issued by a group of banks which have associated themselves to perform through a clearing house some of their collection, payment and clearing functions. Other such agencies or associations may be established in the future whose rules and regulations could be appropriately looked on as constituting means of avoiding absolute statutory rigidity. The phrase "and the like" leaves open such possibilities of future development. An agreement between a number of banks or even all the banks in an area simply because they are banks, would not of itself, by virtue of the phrase "and the like," meet the purposes and objectives of subsection (2).

4. Under this Chapter banks come under the general obligations of the use of good faith and the exercise of ordinary care. "Good faith" is defined in this Act (Section 30-1-201(19)) as "honesty in fact in the conduct or transaction concerned." The term "ordinary care" is not defined and is here used with its normal tort meaning and not in any special sense relating to bank collections. No attempt is made in the Chapter to define *in toto* what constitutes ordinary care or lack of it. Section 30-4-202 states respects in which collecting banks must use ordinary care. Subsection (3) of 30-4-103 provides that action or non-action approved by the Chapter or pursuant to Federal Reserve regulations or operating letters constitutes the exercise of ordinary care. Where Federal Reserve regulations and operating letters are issued pursuant to statutory mandate as indicated

above, they constitute an affirmative standard of ordinary care equally with the provisions of Chapter 4 itself.

Subsection (3) further provides that, absent special instructions, action or non-action consistent with clearing house rules and the like or with a general banking usage not disapproved by the Chapter, prima facie constitutes the exercise of ordinary care. Clearing house rules and the phrase "and the like" have the significance set forth above in these Comments. The term "general banking usage" is not defined but should be taken to mean a general usage common to banks in the area concerned. See Section 30-1-205(2). Where the adjective "general" is used, the intention is to require a usage broader than a mere practice between two or three banks but it is not intended to require anything as broad as a country-wide usage. A usage followed generally throughout a state, a substantial portion of a state, a metropolitan area or the like would certainly be sufficient. Consistently with the principle of Section 30-1-205(3), action or non-action consistent with clearing house rules or the like or with such banking usages prima facie constitutes the exercise of ordinary care. However, the phrase "in the absence of special instructions" affords owners of items an opportunity to prescribe other standards and where there may be no direct supervision or control of clearing houses or banking usages by official supervisory authorities, the confirmation of ordinary care by compliance with these standards is *prima facie* only, thus conferring on the courts the ultimate power to determine ordinary care in any case where it should appear desirable to do so. The *prima facie* rule does, however, impose on the party contesting the standards to establish that they are unreasonable, arbitrary or unfair.

5. Subsection (4), in line with the flexible approach required for the bank collection process is designed to make clear that a novel procedure adopted by a bank is not to be considered unreasonable merely because that procedure is not specifically contemplated by this Chapter or by agreement, or because it has not yet been generally accepted as a bank usage. Changing conditions constantly call for new procedures and someone has to use the new procedure first. If such a procedure when called in question is found to be reasonable under the circumstances, provided, of course, that it is not inconsistent with any provision of the Chapter or other law or agreement, the bank which has followed the new procedure should not be found to have failed in the exercise of ordinary care.

6. Subsection (5) sets forth a rule for determining the measure of damages which, under subsection (1), cannot be limited by agreement. In the absence of bad faith the maximum recovery is the amount of the item concerned. When it is established that some part or all of the item could not have been collected even by the use of ordinary care the recovery is reduced by the amount which would have been in any event uncollectible. This limitation on recovery follows the case law. Finally, when bad faith is established the rule opens to allow the recovery of other damages, whose "proximateness" is to be tested by the ordinary rules applied in comparable cases. Of course, it continues to be as necessary under subsection (5) as it has been under ordinary common law principles that, before the damage rule of the subsection becomes operative, liability of the bank and some loss to the customer or owner must be established.

Official Comment to 1991 Amendment:

Operating "circular" is current usage. The Expedited Funds Availability Act, 12 U.S.C. Section 4007(b) provides that the Act and Regulation CC, 12 CFR 229, supersede "any provision of the law of any State, including the Uniform Commercial Code as in effect in such State, which is inconsistent with this chapter or such regulations." Operating circulars vary the UCC pursuant to Section 4-103(2) [30-4-103(2)]. Regulations and operating circulars of other federal agencies may also have an impact on provisions of the UCC.

In Clearfield Trust Co. v. United States, 318 U.S. 363 (1943), the Court held that if the federal government is a party to an instrument, its rights and duties are governed by federal law. However, in United States v. Kimbell Foods, Inc., 440 U.S. 715 (1979), the court evidenced a willingness to adopt the priorities rules of UCC Article 9 [Title 30, chapter 9A] in the absence of federal law on the subject.

Compiler's Comments

1991 Amendment: In (2) and (3) substituted "circulars" for "letters"; and made minor changes in style.

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

Bank to Exercise Ordinary Care in Settling Checks — Common Law That Bank Exercise Ordinary Care in Processing Checks Preempted by Uniform Commercial Code: Hughes brought common-law claims against a bank for failing to exercise ordinary care in processing checks and for communications that the bank made regarding check processing. A bank that receives a check from a depositor must use ordinary care, as defined in the Uniform Commercial Code (U.C.C.), in settling those checks. However, when a check is processed by automated means, reasonable commercial standards do not require the bank to examine the check, subject to certain exceptions. To the extent that common-law claims relate to processing checks, the specific provisions of the U.C.C. prevail, so Hughes' claims regarding the propriety of the bank's check processing were preempted. However, because the U.C.C. does not address misrepresentation in communications, Hughes' common-law and equitable claims for negligence were not preempted by the U.C.C., and the District Court committed reversible error by failing to consider whether common-law and equitable principles supplement the U.C.C.-defined duty of ordinary care with respect to the bank's representations about the check settlement process. Valley Bank of Ronan v. Hughes, 2006 MT 285, 334 M 335, 147 P3d 185 (2006).

Forgery — Damages Limited to Face Amount of Check: When substantial credible evidence existed by which the jury could reject plaintiffs' claim that defendant bank's action in cashing a forged check and its checking account practices proximately caused plaintiffs' additional damages, the bank could not be held liable for any amount beyond the face value of the check. Ahmann v. Am. Fed. S&L Ass'n, 235 M 184, 766 P2d 853, 45 St. Rep. 2305 (1988).

"Demand Item" and "Presentment" Construed — Waiver of Midnight Deadline Rule: When defendant's, Nuernberger's, check was twice refused and returned for insufficient funds by the payor bank, First Bank of Billings (First Bank), an officer of the joint payee, Montana Livestock Production Credit Association (MLPCA) returned the check to First Bank with a written memo authorizing First Bank to "hold it for longer than the usual 24-hour period" and to pay when funds became available. The District Court granted summary judgment for the plaintiff (the other joint payee) and MLPCA and found First Bank strictly liable for the face amount of the check because of its failure to comply with the midnight deadline rule. The Supreme Court reversed and found that the midnight deadline rule did not apply, holding that the check was not a "demand item" because it was transmitted with the understanding it would be held for sufficient funds and that there had been no "presentment" by the plaintiff, but only by the joint payee, MLPCA. The Supreme Court further held that there had been a waiver of the midnight rule time requirements by MLPCA's memo. Iverson v. First Bank of Billings, 219 M 283, 712 P2d 1285, 42 St. Rep. 2021 (1985).

Agreement Excusing Payor Bank from Noncompliance with "Midnight Rule": There was no agreement between payor bank and payees excepting bank from strict liability for noncompliance with "midnight rule" of 30-4-302 in its failure to give timely notice of dishonor of checks since: (1) bank's holding and paying of one check as to each of two of the payees was not sufficient to form "a sequence of previous conduct" necessary to establish a course of dealing from which an agreement excusing noncompliance with "midnight rule" could be implied under 30-1-201(3) and 30-1-205(1); and (2) alleged understanding with one payee's agent would not be considered an agreement in view of bank's unique position as drawer's creditor. Sun River Cattle Co., Inc. v. Miners Bank of Mont., 164 M 237, 521 P2d 679 (1974).

Custom and Practice: Custom and practice are relevant under subsection (3), if at all, only with respect to establishment of what standard constitutes ordinary care; where payor bank was subject to higher standard of care because of its status as creditor of drawer of checks, its failure to comply with "midnight rule" of 30-4-302 in handling checks for collection could not be excused on ground that established custom and practice of Montana banking industry was to hold such checks for an arbitrary length of time in absence of special instructions and writing. Sun River Cattle Co., Inc. v. Miners Bank of Mont., 164 M 237, 521 P2d 679 (1974).

Interest on Judgment: Determination by the court that the bank was liable for payment of dishonored checks was based on contract law of negotiable instruments, and the provisions of this statute for damages for negligence or bad faith do not apply. Sun River Cattle Co. v. Miners Bank of Mont., 164 M 479, 525 P2d 19 (1974).

30-4-104. Definitions and index of definitions.

Official Comment

[*Corresponding U.C.C. Section:* Section 4-104, U.C.C.]

Source: Section 4-104, U.C.C.

Purposes:

1. Subsection (1)(c): "Banking Day". Under this definition that part of a business day when a bank is open only for limited functions, e.g., on Saturday evenings to receive deposits and cash checks, but with loan, bookkeeping and other departments closed, is not part of a banking day.

2. Subsection (1)(d): "Clearing House". Occasionally express companies, governmental agencies and other non-banks deal directly with a clearing house; hence the definition does not limit the term to an association of banks.

3. Subsection (1)(e): "Customer". It is to be noted that this term includes a bank carrying an account with another bank as well as the more typical non-bank customer or depositor.

4. Paragraph (a)(6) [subsection (1)(f)]: "Documentary draft" applies even though the documents do not accompany the draft but are to be received by the drawee or other payor before acceptance or payment of the draft. Documents may be either in electronic or tangible form. See Article 5, Section 5-102 [30-5-102], Comment 2 and Article 1, Section 1-201 [30-1-201] (definition of "document of title").

5. Subsection (1)(h): The word "item" is chosen because it is "banking language" and includes non-negotiable as well as negotiable paper calling for money and also similar paper governed by the Chapter on Investment Securities (Chapter 8) as well as that governed by the Chapter on Commercial Paper (Chapter 3).

6. Subsection (1)(i): "Midnight Deadline". The use of this phrase is an example of the more mechanical approach used in this Chapter. Midnight is selected as a termination point or time limit to obtain greater uniformity and definiteness than would be possible from other possible termination points, such as the close of the banking day or business day.

7. Subsection (1)(j): The term "settle" is a new term in bank collection language that has substantial importance throughout Chapter 4. In the American Bankers Association Bank Collection Code, in deferred posting statutes, in Federal Reserve regulations and operating letters, in clearing house rules, in agreements between banks and customers and in legends on deposit tickets and collection letters, there is repeated reference to "conditional" or "provisional" credits or payments. Tied in with this concept of credits or payments being in some way tentative, has been a related but somewhat different problem as to when an item is "paid" or "finally paid" either to determine the relative priority of the item as against attachments, stop payment orders and the like or in insolvency situations. There has been extensive litigation in the various states on these problems. To a substantial extent the confusion, the litigation and even the resulting court decisions fail to take into account that in the collection process some debits or credits are provisional or tentative and others are final and that very many debits or credits are provisional for awhile but later become final. Similarly, some cases fail to recognize that within a single bank, particularly a payor bank, each item goes through a series of processes and that in a payor bank most of these processes are preliminary to the basic act of payment or "final payment".

The term "settle" is used as a convenient term to characterize a broad variety of conditional, provisional, tentative and also final payments of items. Such a comprehensive term is needed because it is frequently difficult or unnecessary to determine whether a particular action is tentative or final or when a particular credit shifts from the tentative class to the final class. Therefore, its use throughout the Chapter indicates that in that particular context it is unnecessary or unwise to determine whether the debit or the credit or the payment is tentative or final. However, when qualified by the adjective "provisional" its tentative nature is intended, and when qualified by the adjective "final" its permanent nature is intended.

Examples of the various types of settlement contemplated by the term include payments in cash; the efficient but somewhat complicated process of payment through the adjustment and off-setting of balances through clearing houses; debit or credit entries in accounts between banks; the forwarding of various types of remittance instruments, sometimes to cover a particular item but more frequently to cover an entire group of items received on a particular day.

8. Subsection (1)(k): "Suspends payments". This term is designed to afford an objective test to determine when a bank is no longer operating as a part of the banking system.

Official Comment to 1991 Amendment:

1. "Account" is defined to include both asset accounts in which a customer has deposited money and accounts from which a customer may draw on a line of credit. The limiting factor is that the account must be in a bank.

2. "Documentary draft" is amended to recognize the existence of uncertificated securities. The reference to "accompanying" documents is deleted as obsolete.

3. "Draft" is defined in Section 3-104 [30-3-104] as a form of instrument. Since Article 4 [Title 30, chapter 4] applies to items that may not fall within the definition of instrument, the term is defined here to include an item that is a written order to pay money, even though the item may not qualify as an instrument. The term "order" is defined in Section 3-103 [30-3-102].

4. "Item" is defined broadly to include an instrument, as defined in Section 3-104 [30-3-104], as well as promises or orders that may not be within the definition of "instrument". The terms

"promise" and "order" are defined in Section 3-103 [30-3-102]. A promise is a written undertaking to pay money. An order is a written instruction to pay money. The functional limitation on the meaning of this term is the willingness of the banking system to handle the instrument or obligation for collection or payment.

5. In present Article 4 [Title 30, chapter 4, prior to 1991 revision] there is no affirmative definition of the term "properly payable." Present Section 4-104(1)(i) [now deleted] merely implies that if the customer's account is insufficient to pay the item the item is not properly payable. The term is defined in proposed Section 4-401(1) [30-4-401(1)] in terms of the items being authorized by the customer and being in accordance with the bank-customer agreement. This is done to give meaning to "properly payable" in Sections 4-401(1) and 4-402(1) [30-4-401(1) and 30-4-402(1)]. The latter provision makes clear that a bank that fails to pay an overdraft has not wrongfully dishonored unless it had agreed to pay the overdraft.

Compiler's Comments

2005 Amendment: Chapter 575 in (3) in list inserted reference to control. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

1997 Amendment: Chapter 536 in definition of documentary draft substituted "certificated securities (30-8-112) or instructions for uncertificated securities (30-8-112)" for "certificated securities or transfer statements for uncertificated securities".

1991 Amendment: In (1), in definition of account after "any", inserted "deposit or credit" and at end substituted "demand, time, savings, passbook, share draft, or like account, other than an account evidenced by a certificate of deposit" for "a checking, time, interest or savings account"; in definition of customer, before "an account", substituted "maintaining" for "carrying"; substituted definition of documentary draft for former definition that read: ""Documentary draft" means any negotiable or nonnegotiable draft with accompanying documents, securities or other papers to be delivered against honor of the draft"; inserted definition of draft; substituted definition of item for former definition that read: ""Item" means any instrument for the payment of money even though it is not negotiable but does not include money"; deleted former (1)(i) that read: "(i) "Properly payable" includes the availability of funds for payment at the time of decision to pay or dishonor"; in definition of settle, at end of first sentence, substituted "agreed" for "instructed"; in (2) inserted references to bank and presentment notice and deleted ""Remitting bank. 30-4-105"; in (3) inserted references to alteration, cashier's check, certified check, drawee, good faith, instrument, order, ordinary care, person entitled to enforce, promise, prove, teller's check, and unauthorized signature and deleted ""Certification". 30-3-411", ""Draft". 30-3-104", ""Protest". 30-3-509", and ""Secondary party". 30-3-102"; and made minor changes in style.

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

"Customer" Construed: Defendant whose husband was incarcerated cashed VA checks payable to her husband by endorsing them with her husband's name and her own. The husband objected, and the VA requested reimbursement from the bank. The bank then filed suit against plaintiff, contending that as a customer she had warranted that she had title to the checks. Because defendant neither had an account with the bank nor authorized the bank to collect items for her, she was not a customer of the bank. As a noncustomer she had not warranted title to the checks. First Nat'l Bank in Eureka v. Giles, 225 M 467, 733 P2d 357, 44 St. Rep. 407 (1987).

Drawer and Payee Identical — Circuitous Accountability: Checks were drawn on the account of Capital Preservation Fund, Inc., maintained with First National Bank of Great Falls, Montana, by John Bennett, an authorized signatory on the account. The checks were endorsed and deposited by Bennett in another account he maintained with the Ashford Bank of Houston, Texas. Ashford Bank sent the checks through normal banking channels and extended cash to Bennett in reliance on the checks. The checks, however, were dishonored by First National Bank. Ashford then charged back the account of Bennett but alleged that it sustained a loss of $500,000. An affidavit from the Federal Reserve Bank established that First National had timely returned the checks in advance of the "midnight deadline". Bennett contended that payment became final prior to dishonor because First National had completed the process of posting. Section 30-4-213 provides that "final" payment by a drawee bank is the point at which all "provisional" settlements as allowed by 30-4-104(1)(j) in the bank collection chain became "final" settlements. Typically, provisional credits given through a clearinghouse or mutual bank account are made final upon payment of the item by completion of the process of posting the drawer's account. The agency relationships established under 30-4-201 are thereby transformed into a series of debtor-creditor relationships ending with the depository bank indebted to its customer for the amount of the item. The right of a collecting bank under 30-4-212(1) to charge back the account of its customer for any credit given for an item terminates when payment on the item becomes final. Section 30-4-213 holds a "payor" bank accountable for an item once "final" payment has been rendered. The "payor" bank must act in a timely manner in either dishonoring or paying the instrument. Timely dishonor was established. Bennett in this instance had the roles of both a "drawer" and the "payee". To allow Bennett to allege that payment by First National, the "payor" bank, was final would result in circuitous accountability. First National would simply charge the account on which the checks were drawn, Capital Preservation Fund, Inc., in order to recoup the amount paid. Capital Preservation Fund, Inc., would in turn have a cause of action against Bennett for recovery of the money. Any litigation emanating from this unique factual situation properly was between Capital Preservation Fund, Inc., and Bennett. The cause of action against First National Bank was found to be illusory, and it was granted summary judgment. Ashford Bank v. Capital Preservation Fund, Inc., 544 F. Supp. 26, 39 St. Rep. 1385 (D.C. Mont. 1982).

Prompt Payment of Time Draft by Collecting Bank: A time draft was payable on or before June 24, 1980. Since the "time for taking action" commenced on that date, a collecting bank had until midnight on June 25, 1980, to mail a cashier's check to the owner of the draft. Miske v. Stirling, 199 M 32, 647 P2d 841, 39 St. Rep. 1186 (1982).

Attorney General's Opinions

"Banking Day": Saturday should not be considered a banking day for the purposes of this section for banks open on Saturday for limited teller transactions. 36 A.G. Op. 91 (1976).

30-4-105. "Bank" — "depositary bank" — "intermediary bank" — "collecting bank" — "payor bank" — "presenting bank".

Official Comment

Source: Section 4-105, U.C.C.

Purposes:

1. The definitions in general exclude a bank to which an item is issued, as such bank does not take by transfer except in the particular case covered where the item is issued to a payee for collection, as where a corporation is transferring balances from one account to another. Thus, the definition of "depositary bank" does not include the bank to which a check is made payable where a check is given in payment of a mortgage. Such a bank has the status of a payee under Chapter 3 on Commercial Paper and not that of a collecting bank.

2. The term payor bank includes a drawee bank and also a bank at which an item is payable if the item constitutes an order on the bank to pay, for it is then "payable by" the bank. If the "at" item is not an order in the particular state (See Section 30-3-121 [now repealed]), then the bank is not a payor, but will be a presenting or collecting bank.

3. Items are sometimes drawn or accepted "payable through" a particular bank. Under this Section and Section 30-3-120 [now repealed] the "payable through" bank (if it in fact handles the item) will be a collecting (and often a presenting) bank; it is not a "payor bank."

4. The term intermediary bank includes the last bank in the collection process where the payor is not a bank. Usually the last bank is also a presenting bank.

Official Comment to 1991 Amendment:

1. "Bank" is defined in Section 1-201(4) [30-1-201(4)] as meaning "any person engaged in the business of banking." This broad definition is modified by the words in the preamble to Section 1-201 [30-1-201] "unless the context otherwise requires." The definition in subsection (a) [subsection (1) of this section] makes clear that "bank" includes savings banks, savings and loan associations, credit unions and trust companies, in addition to the commercial banks commonly denoted by use of the term "bank."

2. A bank that takes an "on us" item for collection, for application to a customer's loan, or first handles the item for other reasons is a depositary bank even though it is also the payor bank. However, if the holder presents such an item for immediate payment over the counter, the payor bank is not a depositary bank.

3. The definition of "payor bank" is clarified by use of the term "drawee." That term is defined in Section 3-103 [30-3-102] as meaning "a person ordered in a draft to make payment." The definition of "drawee" is brought into Article 4 [Title 30, chapter 4] by proposed Section 4-104(3) [30-4-104(3)]. An "order" is defined in Section 3-103 [30-3-102] as meaning "a written instruction to pay money ... . An authorization to pay is not an order unless the person authorized to pay is also instructed to pay." The definition of order is also incorporated into Article 4 [Title 30, chapter 4] by proposed Section 4-104(3) [30-4-104(3)]. Thus a payor bank is one instructed to pay in the item. A bank does not become a payor bank by being merely authorized to pay or by being given an instruction to pay not contained in the item.

4. The term "remitting bank" is not used in Article 4 [Title 30, chapter 4] and is deleted.

Compiler's Comments

1991 Amendment: In catchline, at beginning, inserted "Bank" and at end deleted "remitting bank"; inserted definition of bank; in definition of depositary bank, after item, deleted "is transferred for collection" and at end inserted "unless the item is presented for immediate payment over the counter"; in definition of payor bank, at end, substituted "that is the drawee of a draft" for "by which an item is payable as drawn or accepted"; deleted definition of remitting bank that read: ""Remitting bank" means any payor or intermediary bank remitting for an item"; and made minor changes in style.

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

"Collecting Bank" — Time Draft: A time draft from the defendant oil company and payable to the plaintiff landowner bore the legend "collect directly through First Citizens Bank". The landowner deposited the draft in his local bank, which then forwarded the draft to First Citizens Bank. First Citizens Bank received the oil company's check for payment of the draft, deposited the check in the oil company's account, and made out a cashier's check to the landowner. First Citizens Bank was a "collecting bank" within the meaning of this section. Miske v. Stirling, 199 M 32, 647 P2d 841, 39 St. Rep. 1186 (1982).

30-4-106. Separate office of a bank.

Official Comment

Source: Section 4-107, U.C.C.

Prior Uniform Statutory Provision: See Section 1, American Bankers Association Bank Collection Code.

Purposes:

1. A rule with respect to the status of a branch or separate office of a bank as a part of any statute on bank collections is highly desirable if not absolutely necessary. However, practices in the operations of branches and separate offices vary substantially in the different states and it has not been possible to find any single rule that is logically correct, fair in all situations and workable under all different types of practices.

2. In many states and for many purposes a branch or separate office of the bank needs to be treated as a separate bank. Many branches function as separate banks in the handling and payment of items and require time for doing so similar to that of a separate bank. This is particularly true where branch banking is permitted throughout a state or in different towns and cities. Similarly, where there is this separate functioning a particular branch or separate office is the only proper place for various types of action to be taken or orders or notices to be given. Examples include the drawing of a check on a particular branch by a customer whose account is carried at that branch; the presentment of that same check at that branch; the issuance of an order to the branch to stop payment on the check.

3. Section 1 of the American Bankers Association Bank Collection Code provides simply: "A branch or office of any such bank shall be deemed a bank." Although this rule appears to be brief and simple, as applied to particular sections of the ABA Code it produces illogical and, in some cases, unreasonable results. For example, under Section 11 of the ABA Code it seems anomalous for one branch of a bank to have charged an item to the account of the drawer and another branch to have the power to elect to treat the item as dishonored. Similar logical problems would flow from applying the same rule to Chapter 4. Warranties by one branch to another branch under Section 30-4-207 (each considered a separate bank) do not make sense.

4. Assuming that it is not desirable to make each branch a separate bank for all purposes, this Section provides that a branch or separate office is a separate bank for certain purposes. In so doing the single legal entity of the bank as a whole is preserved, thereby carrying with it the liability of the institution as a whole on such obligations as it may be under. On the other

hand, where the Chapter provides a number of time limits for different types of action by banks, if a branch functions as a separate bank, it should have the time limits available to a separate bank. Similarly if in its relations to customers a branch functions as a separate bank, notices and orders with respect to accounts of customers of the branch should be given at the branch. For example, whether a branch has notice sufficient to affect its status as a holder in due course of an item taken by it should depend upon what notice that branch has received with respect to the item. Similarly the receipt of a stop payment order at one branch should not be notice to another branch so as to impair the right of the second branch to be a holder in due course of the item, although in circumstances in which ordinary care requires the communication of a notice or order to the proper branch of a bank, such notice or order would be effective at such proper branch from the time it was or should have been received. See Section 30-1-201(27).

5. Whether a branch functions as a separate bank may vary depending upon the type of activity taking place and upon practices in the different states. If the activity is that of a payor bank paying items, a branch will usually function as a separate bank if it maintains its own deposit ledgers. Similarly whether a branch functions as a separate bank in the collection of items usually depends also on whether it maintains its own deposit ledgers. Conversely, if a particular bank having branches does all of its bookkeeping at its head office, the branches of that bank do not usually function as separate banks either in the payment or collection of items.

On the other hand, in its relations to customers a branch may function as a separate bank regardless of whether it maintains its own deposit ledgers. Checks may be drawn on a particular branch and notices and stop orders delivered to that branch even though all the bookkeeping is done at the head office or another branch.

Compiler's Comments

1991 Amendment: Made minor changes in style.

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Optional Language: Montana has not adopted the optional language proposed in this section, which would require a branch to maintain its own deposit ledgers in order to be considered a separate bank for certain purposes under chapter 4.

30-4-107. Time of receipt of items.

Official Comment

Source: Section 4-108, U.C.C.

Purposes:

1. After an item has been received by a bank it goes through a series of processes varying with the type of item that it is. It moves from the teller's window, branch office, or mail desk at which it is received through settlement and proving departments until it is forwarded or presented to a clearing house or another bank, if it is a transit item, or until it reaches the bookkeeping department, if the bank receiving it is the payor bank. In addition, in order that the books of the bank always remain in balance while items are moving through it, the amount of each item is included in lists or proofs of debits or credits several times as it progresses through the bank. The running of proofs, the making of debit and credit entries in subsidiary and general ledgers and the striking of a general balance for each day requires a considerable amount of time. If these processes are to be completed on any particular day during normal working hours without the employment of night forces, a number of banks have found it necessary to establish a "cut-off hour" to allow time to obtain final figures to be incorporated into the bank's position for the day. Subsection (1) approves the cut-off hour of this type provided it is not earlier than 2 P.M. Subsection (2) provides that if such a cut-off hour is fixed, items received after the cut-off hour may be treated as being received at the opening of the next banking day. Where the number of items received either through the mail or over the counter tends to taper off radically as the afternoon hours progress, a 2 P.M. cut-off hour does not involve a large portion of the items received but at the same time permits a bank using such a cut-off hour to leave its doors open later in the afternoon without forcing into the evening the completion of its settling and proving process.

2. The alternative provision in Subsection (2) that items or deposits received after the close of the banking day may be treated as received at the opening of the next banking day is important in cases where a bank closes at twelve or one o'clock, e.g., on a Saturday, but continues to receive some items by mail or over the counter if, for example, it opens Saturday evening for the limited purpose of receiving deposits and cashing checks.

30-4-108. Delays.

Official Comment

Source: Section 4-109, U.C.C.

Purposes:

1. Sections 30-4-202(2), 30-4-212, 30-4-301 and 30-4-302 prescribe various time limits for the handling of items. These are the limits of time within which a bank, in fulfillment of its obligation to exercise ordinary care, must handle items entrusted to it for collection or payment. Under Section 30-4-103 they may be varied by agreement or by Federal Reserve regulations or operating letters, clearing house rules, or the like.

2. Subsection (1) of this section permits a limited extension of these time limits in special cases. It permits collecting banks to grant, within a rather narrow field, an additional banking day and to do so with or without the approval of any interested party. Such one-day extension can only be granted in a good faith effort to secure payment and only with respect to specific items. It cannot be exercised if the customer instructs otherwise. Thus limited the escape provision should afford a limited degree of flexibility in special cases but should not interfere with the overall requirement and objective of speedy collections.

3. Notice that an extension granted under Subsection (1) is "without discharge of secondary parties". It therefore extends also the times for presentment or payment, as the case may be, specified in Chapter 3. See Sections 30-3-503 [now repealed] and 30-3-506 [now repealed]. Where this Chapter and Chapter 3 conflict, this Chapter controls. See Sections 30-3-103(2) [now repealed] and 30-4-102(1).

4. Subsection (2) is another escape clause from time limits. This clause operates not only with respect to time limits imposed by the chapter itself but also time limits imposed by special instructions, by agreement or by Federal Reserve regulations or operating letters, clearing house rules or the like. The latter time limits are "permitted" by the Code. This clause operates, however, only in the types of situation specified. Examples of these situations include blizzards, floods, or hurricanes, and other "Act of God" events or conditions, and wrecks or disasters, interfering with mails; suspension of payments by another bank; abnormal operating conditions such as substantial increased volume or substantial shortage of personnel during war or emergency situations. When delay is sought to be excused under the subsection the bank must "exercise such diligence as the circumstances require" and it has the burden of proof. See Section 30-4-202(2).

Official Comment to 1991 Amendment:

1. The amendment to subsection (1) authorizes a collecting bank to take additional time in attempting to collect drafts drawn on nonbank payors. The right of a collecting bank to waive time limits under subsection (1) does not apply to checks. The term "secondary parties" is no longer defined in Article 3 [Title 30, chapter 3]. Hence, it is deleted here and replaced by the parties included in the definition in present Section 3-102(1)(d) [30-4-102(1)(d) prior to 1991 revision].

2. A payor bank that fails to make timely return of a dishonored item may be accountable for the amount of the item. The amendments in subsection (2) excuse the bank from this liability when its failure to meet its midnight deadline resulted from, for example, a computer breakdown that was beyond the control of the bank, so long as the bank exercised the degree of diligence that the circumstances required. In Port City State Bank v. American National Bank, 486 F.2d 196 (10th Cir. 1973), the court held that a bank exercised sufficient diligence to be excused under Section 4-108(2) [30-4-107(2)]. The subsection is consistent with Regulation CC Section 229.38(e).

Compiler's Comments

1991 Amendment: In (1), after "specific item", inserted "drawn on a payor other than a bank" and after "period not" substituted "exceeding 2 additional banking days without discharge of drawers or indorsers" for "in excess of an additional banking day without discharge of secondary parties and without"; in (2)(a), at beginning, inserted "the delay is", after "communication" inserted "or computer", and after "conditions" inserted "failure of equipment"; at beginning of (2)(b) inserted "the bank"; and made minor changes in style.

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

Construction: Effect of subsection (2) of this section is to excuse a payor bank from the standard of strict accountability of 30-4-302 and to hold it to a standard of "diligence as the circumstances require"; under subsection (2) there must be a showing that the circumstances were beyond the control of the bank and that the bank exercised such diligence as the circumstances required; the burden of proof is on the bank. Sun River Cattle Co., Inc. v. Miners Bank of Mont., 164 M 237, 521 P2d 679 (1974).

Degree of Diligence Required: Degree of diligence required of payor bank attempting to come under "escape clause" provisions of subsection (2) was greater than it otherwise would have been where bank financed and refinanced drawers of checks and refinancing loans had not yet been completely repaid; showing of diligence required more than testimony as to normal operating procedures; evidence that armored car which delivered checks to clearinghouse broke down on day checks were presented by payees and that clearinghouse's computer malfunctioned after checks were received by it the next day was insufficient to meet bank's burden of proof of excuse for violation of "midnight deadline" where there was no testimony as to what happened on day after checks were initially received by bank. The bank was therefore liable for face amount of checks under strict accountability rule of 30-4-302. Sun River Cattle Co., Inc. v. Miners Bank of Mont., 164 M 237, 521 P2d 679 (1974).

30-4-110. Payable through or payable at bank — collecting bank.

Official Comment

Source: Section 4-106, U.C.C.

Official Comment:

1. This section replaces present Sections 3-120 and 3-121 [30-3-120 and 30-3-121, both now repealed]. Some items are made "payable through" a particular bank. Subsection (1) states that such language makes the bank a collecting bank and not a payor bank. An item identifying a "payable through" bank can be presented for payment only to the drawee by the "payable through" bank. Such an item cannot be presented to the drawee over the counter for immediate payment or by a collecting bank other than the "payable through" bank.

2. Subsection (2) retains the alternative approach of the present law [prior to 1991 revision]. Under Alternative A a "payable at" bank is a payor bank and the midnight deadline provisions of Sections 4-301 and 4-302 [30-4-301 and 30-4-302] apply. Under Alternative B a "payable at" bank is in the same position as a "payable through" bank under subsection (1).

3. Subsection (3) rejects the view of some cases that a bank named below the name of a drawee is itself a drawee. The commercial understanding is that such a bank is a collecting bank and is not accountable under proposed Section 4-302(2) [30-4-302(2)] for holding an item beyond a deadline for dishonor. The liability of the bank is governed by Sections 4-202(1) and 4-103(5) [30-4-202(1) and 30-4-103(5)].

30-4-111. Truncation.

Official Comment

Source: Section 4-110, U.C.C.

Official Comment:

1. "Truncation agreement" refers to an agreement under which presentment may be made to a payor bank by a presentment notice rather than by presentment of the item. Under imaging technology now under development, the presentment notice might be an image of the item. The truncation agreement may provide that the item may be retained by a depositary bank, other collecting bank, or even a customer of the depositary bank. "Truncation agreement" does not refer to the common case of retention of items by payor banks because the item itself is presented to the payor bank in these cases. Payor bank check retention is a matter of agreement between payor banks and their customers. Provisions on payor bank check retention are found in Section 4-406(2) [30-4-406(2)].

2. The assumptions under which the truncation amendments are based are as follows: No bank will participate in a truncation program without an agreement. These agreements may be either bilateral (Section 4-103(1) [30-4-103(1)]), under which two banks that frequently do business with each other may agree to depositary bank check retention, or multilateral (Section 4-103(2) [30-4-103(2)]), in which large segments of the banking industry may participate in such a program. In the latter case, federal or other uniform regulatory standards would likely supply the substance of the electronic presentment agreement, the application of which could be triggered by the use of some form of identifier on the item. Regulation CC Section 229.36(c) authorizes truncation agreements but forbids them from extending return times or otherwise varying requirements of the part of Regulation CC governing check collection without the agreement of all parties interested in the check. For instance, an extension of return time could damage a depositary bank which must make funds available to its customers under mandatory availability schedules. The Expedited Funds Availability Act, 12 U.S.C. Section 4008(b)(2), directs the Federal Reserve Board to consider requiring that banks provide for check truncation.

3. The parties affected by a truncation agreement, with the exception of the customer, can be expected to protect themselves in a regime of truncation. For example, the payor bank can probably be expected to limit its risk of loss from drawer forgery by limiting the dollar amount of eligible items (Federal Reserve program), by reconcilement agreements (ABA Safekeeping program), by insurance (credit union share draft program), or by other means. Because agreements will exist, only minimal amendments are needed to make clear that the UCC does not prohibit truncation.

4. Under truncation the presentment notice and not the item itself will be handled and received. Intermediary banks between the bank that retains the item and the payor bank will probably not be common. However, in case there are such banks, they cannot be holders because they do not have possession of the items. Subsection (3) gives such banks rights equivalent to those they would have enjoyed had they dealt with items themselves.

30-4-112. Statute of limitations.

Official Comment

Source: Section 4-111, U.C.C.

Official Comment:

Present Article 4 [Title 30, chapter 4, prior to 1991 revision] contains no statute of limitations. This section conforms to the period of limitations set by Section 3-118(g) [30-3-122(7)] for actions for breach of warranty and to enforce other obligations, duties or rights arising under Article 3 [Title 30, chapter 3].

Part 2
Collection of Items
Depositary and Collecting Banks

Part Case Notes

Deposit of Check Made to Another — When No Customer Warranties Breached — When Settlement of Check Final: A bank initiated an action against a customer to recover the amount of a check she deposited. The check was a paycheck made out to her former husband. She had deposited his paychecks for a time, and the Supreme Court found an agency relationship in the situation. On the occasion leading to this action, the appellant had deposited the check unsigned to her checking account. The bank stamped the check "deposited to the credit of" and filled in the name of the former husband. Meanwhile, the former husband told the check's issuer his ex-wife had forged his name on the check and deposited it. The issuer completed necessary documents and issued a new check. The former husband then disappeared, being suspected of embezzlement. Whether the customer breached her warranties under the U.C.C. depended on whether the settlement on the check became final. The Supreme Court overruled the trial court and held the settlement had become final. The return of the check occurred after the posting. The bank where the check was deposited was not entitled to a refund under 30-4-212. The customer warranties issue was decided by the principle that an agency could not be denied by a principal accepting its benefits. Because the appellant was not in breach of customer warranties, the bank's remedy, if any, was against the maker or the payee, the appellant's former husband. First Nat'l Bank v. Nunn, 192 M 487, 628 P2d 1110, 38 St. Rep. 869 (1981).

30-4-201. Presumption and duration of agency status of collecting banks and provisional status of credits — applicability of chapter — item endorsed "pay any bank".

Official Comment

Source: Section 4-201, U.C.C.

Prior Uniform Statutory Provision: See Sections 2 and 4 of the American Bankers Association Bank Collection Code.

Purposes:

1. This section states certain basic rules and presumptions of the bank collection process. One basic rule, appearing in the last sentence of subsection (1), is that, to the extent applicable, the provisions of the Chapter govern without regard to whether a bank handling an item owns the item or is an agent for collection. Historically, much time has been spent and effort expended in determining or attempting to determine whether a bank was a purchaser of an item or merely an agent for collection. See discussion of this subject and cases cited in 11 A.L.R. 1043, 16 A.L.R. 1084, 42 A.L.R. 492, 68 A.L.R. 725, 99 A.L.R. 486. See also Section 4 of the American Bankers Association Bank Collection Code. The general approach of Chapter 4, similar to that of other chapters, is to provide, within reasonable limits, rules or answers to major problems known to

exist in the bank collection process without regard to questions of status and ownership but to keep general principles such as status and ownership available to cover residual areas not covered by specific rules. In line with this approach, the last sentence of subsection (1) says in effect that Chapter 4 applies to practically every item moving through banks for the purpose of presentment, payment or collection.

2. Within this general rule of broad coverage, the first two sentences of subsection (1) state a rule of status in terms of a strong presumption. "Unless a contrary intent clearly appears" the status of a collecting bank is that of an agent or sub-agent for the owner of the item. Although as indicated in Comment 1 it is much less important under Chapter 4 to determine status than has been the case heretofore, such status may have importance in some residual areas not covered by specific rules. Further, where status has been considered so important in the past, to omit all reference to it might cause confusion. The presumption of agency "applies regardless of the form of indorsement or lack of indorsement and even though credit given for the item is subject to immediate withdrawal as of right or is in fact withdrawn". Thus questions heretofore litigated as to whether ordinary indorsements "for deposit", "for collection" or in blank have the effect of creating an agency status or a purchase, no longer have significance in varying the prima facie rule of agency. Similarly, the nature of the credit given for an item or whether it is subject to immediate withdrawal as of right or is in fact withdrawn, do not rebut the general presumption. See A.L.R. references supra in Comment 1.

A contrary intent can rebut the presumption but this must be clear. An example of a clear contrary intent would be if collateral papers established or the item bore a legend stating that the item was sold absolutely to the depositary bank.

3. The prima facie agency status of collecting banks is consistent with prevailing law and practice today. Section 2 of the American Bankers Association Bank Collection Code so provides. Legends on deposit tickets, collection letters and acknowledgments of items and Federal Reserve operating letters consistently so provide. The status is consistent with rights of charge-back (Section 30-4-212 and Section 11 of the ABA Code) and risk of loss in the event of insolvency (Section 30-4-214 and Section 13 of the ABA Code).

4. Affirmative statement of a prima facie agency status for collecting banks requires certain limitations and qualifications. Under current practices substantially all bank collections sooner or later merge into bank credits, at least if collection is effected. Usually, this takes place within a few days of the initiation of collection. An intermediary bank receives final collection and evidences the result of its collection by a "credit" on its books to the depositary bank. The depositary bank evidences the results of its collection by a "credit" in the account of its customer. As used in these instances the term "credit" clearly indicates a debtor-creditor relationship. At some stage in the bank collection process the agency status of a collecting bank changes to that of debtor, a debtor of its customer. Usually at about the same time it also becomes a creditor for the amount of the item, a creditor of some intermediary, payor or other bank. Thus the collection is completed, all agency aspects are terminated and the identity of the item has become completely merged in bank accounts, that of the customer with the depositary bank and that of one bank with another.

Although Section 30-4-213(1) provides that an item is finally paid when the payor bank takes certain action with respect to the item such final payment of the item may or may not result in the simultaneous *final settlement* for the item in the case of all prior parties. If a series of provisional debits and credits for the item have been entered in accounts between banks, the final payment of the item by the payor bank may result in the automatic firming up of all these provisional debits and credits under Section 30-4-213(2), and the consequent receipt of final settlement for the item by each collecting bank and the customer of the depositary bank simultaneously with such action of the payor bank. However, if the payor bank or some intermediary bank accounts for the item with a remittance draft, the next prior bank usually does not receive final settlement for the item until such remittance draft finally clears. See Section 30-4-211(3)(a). The first sentence of subsection (1) provides that the agency status of a collecting bank (whether intermediary or depositary) continues until the settlement *given by it for the item* is or becomes final, referring to Sections 30-4-211(3), 30-4-212, and 30-4-213. In the case of the series of provisional credits covered by Section 30-4-213(2), this could be simultaneously with the final payment of the item by the payor bank. In cases where remittance drafts are used or in straight non-cash collections, this would not be until the times specified in Sections 30-4-211(3) and 30-4-213(3).

A number of practical results flow from this rule continuing the agency status of a collecting bank until its settlement for the item is or becomes final, some of which are specifically set forth in this Chapter. One is that risk of loss continues in the owner of the item rather than the agent bank. See Section 30-4-212. Off-setting rights favorable to the owner are that pending such final settlement, the owner has the preference rights of Section 30-4-214 and the direct rights of Section 30-4-302 against the payor bank. It also follows from this rule that the dollar limitations of Federal Deposit Insurance are measured by the claim of the owner of the item rather than that of the collecting bank.

5. In those cases where some period of time elapses between the final payment of the item by the payor bank and the time that the settlement of the collecting bank is or becomes final, e.g., where the payor bank or an intermediary bank accounts for the item with a remittance draft or in straight non-cash collections, the continuance of the agency status of the collecting bank necessarily carries with it the continuance of the owner's status as principal. The second sentence of subsection (1) provides that whatever rights the owner has to proceeds of the item are subject to the rights of collecting banks for outstanding advances on the item and other valid rights, if any. The rule provides a sound rule to govern cases of attempted attachment of proceeds of a non-cash item in the hands of the payor bank as property of the absent owner. If a collecting bank has made an advance on an item which is still outstanding, its right to obtain reimbursement for this advance should be superior to the rights of the owner to the proceeds or to the rights of a creditor of the owner. The phrase "other valid rights, if any" is broad enough to cover legitimate rights of set-off of accounts between banks without attempting to provide that all set-offs may be valid. An intentional crediting of proceeds of an item to the account of a prior bank known to be insolvent, for the purpose of acquiring a right of set-off, would not produce a valid set-off. See 8 Zollman, Banks and Banking (1936) Sec. 5443.

6. This section and Chapter 4 as a whole represent an intentional abandonment of the approach to bank collection problems appearing in Section 4 of the American Bankers Association Bank Collection Code. Where the tremendous volume of items handled makes impossible the examination by all banks of all indorsements on all items and where in fact this examination is not made, except perhaps by depositary banks, it is unrealistic to base the rights and duties of all banks in the collection chain on variations in the form of indorsements. It is anomalous to provide throughout the ABA Code that the prima facie status of collecting banks is that of agent or sub-agent but in Section 4 to provide that subsequent holders (sub-agents) shall have the right to rely on the presumption that the bank of deposit (the primary agent) is the owner of the item. It is unrealistic, particularly in this background, to base rights and duties on status of agent or owner. This Section 30-4-201 makes the pertinent provisions of Chapter 4 applicable to substantially all items handled by banks for presentment, payment or collection, recognizes the prima facie status of most banks as agents, and then seeks to state appropriate limits and some attributes to the general rules and presumptions so expressed.

7. Subsection (2) protects the ownership rights with respect to an item indorsed "pay any bank or banker" or in similar terms of a customer initiating collection or of any bank acquiring a security interest under Section 30-4-208, in the event the item is subsequently acquired under improper circumstances by a person who is not a bank and transferred by that person to another person, whether or not a bank. Upon return to the customer initiating collection of an item so indorsed, the indorsement may be cancelled (Section 30-3-208). A bank holding an item so indorsed may transfer the item out of banking channels by special indorsement; however, under Section 30-4-103(5), such bank would be liable to the owner of the item for any loss resulting therefrom if the transfer had been made in bad faith or with lack of ordinary care. If briefer and more simple forms of bank indorsements are developed under Section 30-4-206 (e.g., the use of bank transit numbers in lieu of present lengthy forms of bank indorsements), a depositary bank having the transit number "X100" could make subsection (2) operative by indorsements such as "Pay any bank — X100".

Official Comment to 1991 Amendment:

The only changes of substance are to clarify in subsection (1) that rights of an owner of an item are subject to a bank's right to recoupment as well as setoff and that the last sentence applies if the item is handled for return as well as for forward collection. The reference to present Section 4-212 [30-4-212 prior to 1991 revision] is deleted from subsection (1) because it does not state when a settlement given by a collecting bank becomes final.

Compiler's Comments

1991 Amendment: In (1), in parenthetical, inserted references to 30-4-211(4) and subsections (2) and (3) of 30-4-213 and deleted reference to 30-4-212, after "the bank" inserted "with respect to the item", near end of second sentence, after "rights of", inserted "recoupment or", and in last sentence, after "collection", inserted "or return"; and made minor changes in style.

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

Payment to Collecting Bank — Equivalent to Payment to Owner: A time draft from the defendant oil company and payable to the plaintiff landowner bore the legend "collect directly through First Citizens Bank". The landowner deposited the draft in his local bank, which then forwarded the draft to First Citizens Bank. First Citizens Bank received the oil company's check for payment of the draft, deposited the check in the oil company's account, and made out a cashier's check to the landowner. Because First Citizens Bank as a collecting bank was acting as an agent for the landowner, its receipt of the oil company's check and dedication of the funds to the draft was the equivalent of payment to the landowner, its principal. The oil company was discharged. Miske v. Stirling, 199 M 32, 647 P2d 841, 39 St. Rep. 1186 (1982).

30-4-202. Responsibility for collection or return — when action timely.

Official Comment

Source: Section 4-202, U.C.C.

Prior Uniform Statutory Provision: See Sections 5 and 6, American Bankers Association Bank Collection Code.

Purposes:

1. Subsection (1) states the basic responsibilities of a collecting bank. Of course, under Section 30-1-203 a collecting bank is subject to the standard requirement of good faith. By subsection (1) it must also use ordinary care in the exercise of its basic collection tasks. By Section 30-4-103(1) neither requirement may be disclaimed.

2. If the bank makes presentment itself, subsection (1)(a) requires ordinary care with respect both to the time and manner of presentment. (Sections 30-3-503 [now repealed], 30-3-504, 30-4-210.) If it forwards the item to be presented the subsection requires ordinary care with respect to routing (Section 30-4-204), and also in the selection of intermediary banks or other agents.

3. Subsection (1) describes *types* of basic action with respect to which a collecting bank must use ordinary care. Subsection (2) deals with the *time* for taking action. It first prescribes the general standard for seasonable action, namely, for items received on Monday, proper action (such as forwarding or presenting) on Monday or Tuesday is seasonable. Although under current "production line" operations banks customarily move items along on regular schedules substantially briefer than two days, the subsection states an outside time within which a bank may know it has acted seasonably. To provide flexibility from this standard norm, the subsection further states that action within a reasonably longer time may be seasonable but the bank has the burden of proof. In the case of time items, action after the midnight deadline, but sufficiently in advance of maturity for proper presentation, is a clear example of a "reasonably longer time" that is seasonable. The standard of requiring action not later than Tuesday in the case of Monday items is also subject to possibilities of variation under the general provisions of Section 30-4-103, or under the special provisions regarding time of receipt of items (Section 30-4-107), and regarding delays (Section 30-4-108). This subsection (2) deals only with collecting banks. The time limits applicable to payor banks appear in Sections 30-4-301 and 30-4-302.

4. At common law the so-called New York collection rule subjected the initial collecting bank to liability for the actions of subsequent banks in the collection chain; the so-called Massachusetts rule was that each bank, subject to the duty of selecting proper intermediaries, was liable only for its own negligence. Subsection (3) adopts the Massachusetts rule. But since this is stated to be subject to subsection (1)(a) a collecting bank remains responsible for using ordinary care in selecting properly qualified intermediary banks and agents and in giving proper instructions to them.

Official Comment to 1991 Amendment:

1. Proposed Sections 4-214 and 4-301 [30-4-212 and 30-4-301] prescribe the party to whom an item is to be returned or notice given. There is no need to refer to the routing of returns in this subsection; hence the deletion in subsection (1)(b). The deletion of present subsection (1)(d) [now deleted] is made because there is no provision in Article 3 [Title 30, chapter 3] for a necessary protest.

2. Subsection (2) deals with when a collecting or returning bank is in exercise of ordinary care in forwarding an item, returning an item or giving notice of dishonor, and settling for an item when the bank receives settlement. It restates present subsection (2).

Compiler's Comments

1991 Amendment: In catchline, after "collection", inserted "or return" and at end substituted "timely" for "seasonable"; in (1)(b), after "transferor", deleted "or directly to the depositary bank under subsection (2) of 30-4-212"; deleted former (1)(d) that read: "(d) making or providing for any necessary protest"; near beginning of (2), after "bank", inserted "exercises ordinary care under subsection (1) by", at end of first sentence substituted "settlement" for "payment acts seasonably", and in second sentence, after "may", substituted "constitute the exercise of ordinary care" for "be seasonable"; and made minor changes in style.

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

30-4-203. Effect of instructions.

Official Comment

Source: Section 4-203, U.C.C.

Prior Uniform Statutory Provision: See Section 2 of the American Bankers Association Bank Collection Code.

Purposes:

This Section adopts a "chain of command" theory which renders it unnecessary for an intermediary or collecting bank to determine whether its transferor is "authorized" to give the instructions. Equally the bank is not put on notice of any "revocation of authority" or "lack of authority" by notice received from any other person. The desirability of speed in the collection process and the fact that, by reason of advances made, the transferor may have the paramount interest in the item requires the rule.

The Section is made subject to the provisions of Chapter 3 concerning conversion of instruments (Section 30-3-419) and other provisions of Chapter 3 and this Chapter concerning restrictive indorsements (Sections 30-3-205, 30-3-206 [now repealed], 30-3-419, 30-3-603, 30-4-205). Of course instructions from or an agreement with its transferor does not relieve a collecting bank of its general obligation to exercise good faith and ordinary care. See Section 30-4-103(1). If in any particular case a bank has exercised good faith and ordinary care and is relieved of responsibility by reason of instructions of or an agreement with its transferor, the owner of the item may still have a remedy for loss against the transferor (another bank) if such transferor has given wrongful instructions.

The rules of the Section are applied only to collecting banks. Payor banks always have the problem of making proper payment of an item; whether such payment is proper should be based upon all of the rules of Chapters 3 and 4 and all of the facts of any particular case, and should not be dependent exclusively upon instructions from or an agreement with a person presenting the item.

Official Comment to 1991 Amendment:

The references to restrictive indorsements have been deleted from Article 4 [Title 30, chapter 4] and incorporated into proposed Section 3-206 [30-3-205].

Compiler's Comments

1991 Amendment: Near beginning, after "(30-3-419) and" deleted "the provisions of both Chapter 3 and this chapter concerning" and after "endorsements" inserted "(30-3-205)"; and made minor changes in style.

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

30-4-204. Methods of sending and presenting — sending directly to payor bank.

Official Comment

Source: Section 4-204, U.C.C.

Prior Uniform Statutory Provision: See Section 6, American Bankers Association Bank Collection Code.

Purposes:

1. Subsection (1) prescribes the general standards applicable to proper sending or forwarding of items. Because of the many types of methods available and the desirability of preserving flexibility any attempt to prescribe limited or precise methods is avoided.

2. Subsection (2)(a) codifies the practice of direct mail, express, messenger or like presentment to payor banks. The practice is now country-wide and is justified by the need for speed, the general responsibility of banks, Federal Deposit Insurance protection and other reasons.

3. Full approval of the practice of direct sending is limited to cases where a bank is a payor. Where non-bank drawees or payors may be of unknown responsibility, substantial risks may be attached to placing in their hands the instruments calling for payments from them. This is obviously so in the case of documentary drafts. However, in some cities practices have long existed under clearing house procedures to forward certain types of items to certain non-bank payors. Examples include insurance loss drafts drawn by field agents on home offices. For the purpose of

leaving the door open to legitimate practices of this kind, subsection (2)(c) affirmatively approves direct sending of any item other than documentary drafts to any non-bank payor, if authorized by Federal Reserve regulation or operating letter, clearing house rule or the like.

On the other hand subsection (2)(b) approves sending any item direct to a non-bank payor if authorized by a collecting bank's transferor. This permits special instructions or agreements out of the norm and is consistent with the "chain of command" theory of Section 30-4-203. However, if a transferor other than the owner of the item, e.g., a prior collecting bank, authorizes a direct sending to a non-bank payor, such transferor assumes responsibility for the propriety or impropriety of such authorization.

4. Section 30-3-504 states how presentment is made and subsection (2) of that Section affirmatively approves three specific methods by which presentment may be made. The methods so specified are permissive and do not foreclose other possible methods. However, in view of the substantial increase in recent years of presentment at centralized bookkeeping centers and electronic processing centers maintained or used by payor banks, many of which are at locations other than the banks themselves, subsection (3) specifically approves presentment by a presenting bank at any place requested by the payor bank.

Official Comment to 1991 Amendment:

The change in subsection (3) makes clear that a nonbank payor may request that presentment be made at a particular place.

Compiler's Comments

1991 Amendment: In catchline and (2)(a) substituted "directly" for "direct"; in (2)(c), after "operating", substituted "circular" for "letter"; in (3), after "payor bank", inserted "or other payor"; and made minor changes in style.

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

Prompt Payment of Time Draft by Collecting Bank: A time draft was payable on or before June 24, 1980. Since, under 30-4-104, the "time for taking action" commenced on that date and the collecting bank had until midnight on June 25, 1980, to mail a cashier's check to the owner of the draft, the collecting bank acted in a reasonably prompt manner. Miske v. Stirling, 199 M 32, 647 P2d 841, 39 St. Rep. 1186 (1982).

30-4-205. Depositary bank holder of unindorsed item.

Official Comment

Source: Section 4-205, U.C.C.

Purposes:

1. Subsection (1) is designed to speed up collections by eliminating any necessity to return to a non-bank depositor any items he may have failed to indorse.

2. For the purpose of permitting items to move rapidly through banking channels, intermediary banks and payor banks which are not also depositary banks are permitted to ignore restrictive indorsements of any person except the bank's immediate transferor. However, depositary banks may not so ignore restrictive indorsements. If an owner of an item indorses it "for deposit" or "for collection" he usually does so in the belief such indorsement will guard against further negotiation of the item to a holder in due course by a finder or a thief. This belief is reasonably justified if at least one bank in any chain of banks collecting the item has a responsibility to act consistently with the indorsement.

Official Comment to 1991 Amendment:

Section 3-201(b) [30-3-202(2)] provides that negotiation of an instrument payable to order requires indorsement by the holder. The rule of present Section 4-205(1) [30-4-205(1) prior to 1991 revision] is that the depositary bank may supply a missing indorsement of its customer unless the item contains the words "payee's indorsement required" or the like. The cases have differed on the status of the depositary bank as a holder if it fails to supply its customer's indorsement. Marine Midland Bank, N.A. v. Price, Miller, Evans & Flowers, 446 N.Y.S.2d 797 (N.Y.App. Div.4th Dept. 1981), *rev'd*, 455 N.Y.S.2d 565 (N.Y. 1982). It is common practice for depositary banks to receive unindorsed checks under so-called "lock-box" agreements from customers who receive a high volume of checks. No function would be served by requiring a depositary bank to run these items through a machine that would supply the customer's indorsement except to afford the drawer and the subsequent banks evidence that the proceeds of the item reached the customer's account. Proposed Section 4-205 [30-4-205] provides that the depositary bank becomes a holder when it takes the item for deposit if the depositor is a holder. Whether it supplies the customer's indorsement is immaterial. This subsection satisfies the need for a receipt of funds by the depositary bank by imposing on that bank a warranty that it paid the customer or deposited the item to the customer's account. This warranty runs not only to collecting banks and to the payor bank or nonbank drawee but also to the drawer, affording protection to these parties that the depositary bank received the item and applied it to the benefit of the holder.

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "Supplying missing endorsement — no notice from prior endorsement. (1) A depositary bank which has taken an item for collection may supply any endorsement of the customer which is necessary to title unless the item contains the words "payee's endorsement required" or the like. In the absence of such a requirement a statement placed on the item by the depositary bank to the effect that the item was deposited by a customer or credited to his account is effective as the customer's endorsement.

(2) An intermediary bank, or payor bank which is not a depositary bank, is neither given notice nor otherwise affected by a restrictive endorsement of any person except the bank's immediate transferor."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

30-4-206. Transfer between banks.

Official Comment

Source: Section 4-206, U.C.C.

Purposes:

This section is designed to permit the simplest possible form of transfer from one bank to another, once an item gets in the bank collection chain, provided only identity of the transferor bank is preserved. This is important for tracing purposes and if recourse is necessary. However, since the responsibilities of the various banks appear in the Chapter it becomes unnecessary to have liability or responsibility depend on more formal indorsements. Simplicity in the form of transfer is conducive to speed. Where the transfer is between banks this section takes the place of the more formal requirements of Section 30-3-202.

Compiler's Comments

1991 Amendment: Made minor change in style.

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

30-4-207. Transfer warranties.

Official Comment

Source: Section 4-207, U.C.C.

Prior Uniform Statutory Provision: See American Bankers Association Bank Collection Code, Section 4.

Purposes:

1. Subject to certain exceptions peculiar to the bank collection process and except that they apply only to customers and collecting banks, the warranties and engagements to honor in this section are identical in substance with those provided in the Chapter on Commercial Paper (Chapter 3). See Sections 30-3-414, 30-3-417. For a more complete explanation of the purposes of these warranties and engagements see the Comments to Section 30-3-414 and 30-3-417.

2. In addition to imposing upon customers and collecting banks the warranties and engagements imposed by the original Sections 65 and 66 of the Uniform Negotiable Instruments Law and those of Sections 30-3-414 and 30-3-417 of Chapter 3, with some variations, this Section 30-4-207 is intended to give the effect presently obtained in bank collections by the words "prior indorsements guaranteed" in collection transfers and presentments between banks. The warranties and engagements arise automatically as a part of the bank collection process. Receipt of a settlement or other consideration by a customer or collecting bank is a requirement but any settlement is sufficient regardless of whether the settlement is concurrent with the transfer, as in the case of a cash item, or delayed, as in the case of a non-cash straight collection item. Further, the warranties and engagements run with the item with the result that a collecting bank may sue a remote prior collecting bank or a remote customer and thus avoid multiplicity of suits. This section is also intended to make it clear that the so-called equitable defense of "payment over" does not apply to a collecting bank and that no statute of frauds provision will defeat recovery. Subsections (2) and (3) indicate that these results are intended notwithstanding the absence of indorsement or words of guarantee or warranty in a transfer or presentment. Consequently, if for purposes of simplification or the speeding up of the bank collection process, banks desire to

cut down the length or size of indorsements (Section 30-4-206), they may do so and the standard warranties and engagements to honor still apply.

3. With respect to the exceptions to the warranties in favor of a holder in due course specified in sub-paragraphs (b) and (c) of subsection (1), collecting banks usually have holder in due course status (Sections 30-4-208, 30-4-209). However, if in any case there is a holder in due course but a subsequent collecting bank does not have holder in due course status (e.g., in a straight non-cash collection where no settlement of any kind is made until the bank itself receives final settlement) the bank still has the benefit of the exceptions (if it acts in good faith) under the shelter provisions of Section 30-3-201 [now repealed]. It is to be noted that these shelter provisions, by virtue of successive transfers, benefit not only the immediate transferee from a holder in due course but also subsequent transferees.

4. In this section as in Section 30-3-417, the (a), (b) and (c) warranties to transferees and collecting banks under subsection (2) are in general similar to the (a), (b) and (c) warranties to payors under subsection (1); but the warranties to payors are less inclusive because of exceptions reflecting the rule of Price v. Neal, 3 Burr. 1354 (1762), and related principles. See Comment to Section 30-3-417. Thus collecting banks are given not only all the warranties given to payors by subsection (1), without those exceptions, but also the (d) and (e) warranties of subsection (2).

5. The last sentence of subsection (3) provides that damages for breach of warranties or the engagement to honor shall not exceed the consideration received by the customer or collecting bank responsible "plus finance charges and expenses related to the item, if any". The "expenses" referred to in this phrase may be ordinary collecting expenses and in appropriate cases could also include such expenses as attorneys fees. "Finance charges" are also referred to because in some cases interest or a finance charge is charged by the collecting bank for the time that the bank's advance on the item is outstanding prior to receipt of proceeds of collection. An example of this type of case would be where a bank undertakes a foreign collection in South America or Europe and makes an advance on the item at the time of receipt but may not receive proceeds of the foreign collection for three months or more.

Official Comment to 1991 Amendment:

Except for subsection (2), this section conforms to Section 3-416 [30-3-417] and extends its coverage to items. The substance of this section is discussed in the comment to Section 3-416 [30-3-417]. Subsection (2) is based on the last sentence of subsection (2) of present Section 4-207 [30-4-207(2) prior to 1991 revision]. It provides that customers or collecting banks that transfer items, whether by indorsement or not, undertake to pay the item if the item is dishonored. This obligation cannot be disclaimed by a "without recourse" indorsement or otherwise.

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "Warranties of customer and collecting bank on transfer or presentment of items — time for claims. (1) Each customer or collecting bank who obtains payment or acceptance of an item and each prior customer and collecting bank warrants to the payor bank or other payor who in good faith pays or accepts the item that:

(a) he has a good title to the item or is authorized to obtain payment or acceptance on behalf of one who has a good title; and

(b) he has no knowledge that the signature of the maker or drawer is unauthorized, except that this warranty is not given by any customer or collecting bank that is a holder in due course and acts in good faith:

(i) to a maker with respect to the maker's own signature; or

(ii) to a drawer with respect to the drawer's own signature, whether or not the drawer is also the drawee; or

(iii) to an acceptor of an item if the holder in due course took the item after the acceptance or obtained the acceptance without knowledge that the drawer's signature was unauthorized; and

(c) the item has not been materially altered, except that this warranty is not given by any customer or collecting bank that is a holder in due course and acts in good faith:

(i) to the maker of a note; or

(ii) to the drawer of a draft whether or not the drawer is also the drawee; or

(iii) to the acceptor of an item with respect to an alteration made prior to the acceptance if the holder in due course took the item after the acceptance, even though the acceptance provided "payable as originally drawn" or equivalent terms; or

(iv) to the acceptor of an item with respect to an alteration made after the acceptance.

(2) Each customer and collecting bank who transfers an item and receives a settlement or other consideration for it warrants to his transferee and to any subsequent collecting bank who takes the item in good faith that:

(a) he has a good title to the item or is authorized to obtain payment or acceptance on behalf of one who has a good title and the transfer is otherwise rightful; and

(b) all signatures are genuine or authorized; and

(c) the item has not been materially altered; and

(d) no defense of any party is good against him; and

(e) he has no knowledge of any insolvency proceeding instituted with respect to the maker or acceptor or the drawer of an unaccepted item. In addition each customer and collecting bank so transferring an item and receiving a settlement or other consideration engages that upon dishonor and any necessary notice of dishonor and protest he will take up the item.

(3) The warranties and the engagement to honor set forth in the two preceding subsections arise notwithstanding the absence of endorsement or words of guaranty or warranty in the transfer or presentment and a collecting bank remains liable for their breach despite remittance to its transferor. Damages for breach of such warranties or engagement to honor shall not exceed the consideration received by the customer or collecting bank responsible plus finance charges and expenses related to the item, if any.

(4) Unless a claim for breach of warranty under this section is made within a reasonable time after the person claiming learns of the breach, the person liable is discharged to the extent of any loss caused by the delay in making claim."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

DECISIONS UNDER U.C.C. AFTER 1991 REVISION

Applicability of Discovery Doctrine to Uniform Commercial Code Conversion Cases: Over a 2½-year period, one of plaintiff's employees forged signatures on more than 100 company checks and money orders, made them payable to herself, and deposited the proceeds in her personal account at defendant credit union. Plaintiff ultimately filed an action against the credit union, seeking damages in the amount of the checks and money orders and alleging unlawful conversion of negotiable instruments under 30-3-419 and breach of transfer warranties under this section. The credit union moved for summary judgment on grounds that the conversion action was barred by the statutes of limitations in 30-3-417(4) and subsection (5) of this section. However, the statutes of limitations in 30-3-417(4) and subsection (5) of this section apply only to breach of warranty actions, not to conversion actions. The credit union then asserted that the discovery doctrine should apply. The doctrine is an equitable exception to the general rule that the statute of limitations begins to run as soon as the cause of action accrues, allowing instead that the applicable statute of limitations begins to run once plaintiff knew or should have known that a cause of action existed. In a case of first impression, the Supreme Court declined to apply the discovery doctrine to the Uniform Commercial Code conversion claim. Conversion actions are subject to the statute of limitations in 30-3-122(7), which requires commencement of a conversion action within 3 years of the action's accrual. The public would be poorly served by a rule that shifts the responsibility for careful bookkeeping and employee supervision away from those in the best position to monitor accounts and employees. Although predictably harsh in some cases, the 3-year statute of limitations will be strictly applied as best serving the goals of the Uniform Commercial Code. The facts regarding the date of the conversion and the filing of plaintiff's complaint were not in dispute, so the credit union was entitled to judgment as a matter of law on the conversion claim. Yarbro, Ltd. v. Missoula Fed. Credit Union, 2002 MT 152, 310 M 346, 50 P3d 158 (2002).

Employer Responsible for Employee's Fraudulent Endorsement of Instrument Absent Evidence of Lack of Ordinary Care by Party Taking Instrument for Value — Breach of Warranty Claim Properly Dismissed: Over a 2½-year period, one of plaintiff's employees forged signatures on more than 100 company checks and money orders, made them payable to herself, and deposited the proceeds in her personal account at defendant credit union. Plaintiff ultimately filed an action against the credit union, seeking damages in the amount of the checks and money orders and alleging breach of transfer warranties under this section. After finding that plaintiff produced no evidence to refute the credit union's assertion that the employee was entrusted with responsibility for processing instruments and that the credit union had exercised ordinary care in accepting the instruments for payment, the District Court entered summary judgment for the credit union on the breach of warranty claim. The Supreme Court affirmed. Plaintiff was not considered a transferee under the terms of this section. Plaintiff received no instrument or transfer warranty from the credit union, so plaintiff was not entitled to claim a breach of the warranty against the credit union. Plaintiff was responsible for the employee's actions under 30-3-420. Yarbro, Ltd. v. Missoula Fed. Credit Union, 2002 MT 152, 310 M 346, 50 P3d 158 (2002).

DECISIONS UNDER U.C.C. PRIOR TO 1991 REVISION

"Customer" Construed: Defendant whose husband was incarcerated cashed VA checks payable to her husband by endorsing them with her husband's name and her own. The husband objected, and the VA requested reimbursement from the bank. The bank then filed suit against plaintiff, contending that as a customer she had warranted that she had title to the checks. Because defendant neither had an account with the bank nor authorized the bank to collect items for her, she was not a customer of the bank. As a noncustomer she had not warranted title to the checks. First Nat'l Bank in Eureka v. Giles, 225 M 467, 733 P2d 357, 44 St. Rep. 407 (1987).

Question Whether Checks Cashed Without Authorization — Summary Judgment Improper: The District Court improperly granted summary judgment to bank when it assumed, absent evidence in the record, that checks were cashed by an unauthorized signer. The determination that the signature was unauthorized could not be made without dealing with the rights and liabilities between the signer and the person to whom the checks were originally made out. First Nat'l Bank in Eureka v. Giles, 225 M 467, 733 P2d 357, 44 St. Rep. 407 (1987).

Timing of Notification of Breach: Plaintiff notified defendant payor bank of irregularities in the endorsement of a check shortly after she received her monthly bank statement. Such notice was given within a reasonable time within the meaning of this section. Eatinger v. First Nat'l Bank of Lewistown, 199 M 377, 649 P2d 1253, 39 St. Rep. 1465 (1982).

Deposit of Check Made to Another — When No Customer Warranties Breached — When Settlement of Check Final: A bank initiated an action against a customer to recover the amount of a check she deposited. The check was a paycheck made out to her former husband. She had deposited his paychecks for a time, and the Supreme Court found an agency relationship in the situation. On the occasion leading to this action, the appellant had deposited the check unsigned to her checking account. The bank stamped the check "deposited to the credit of" and filled in the name of the former husband. Meanwhile, the former husband told the check's issuer his ex-wife had forged his name on the check and deposited it. The issuer completed necessary documents and issued a new check. The former husband then disappeared, being suspected of embezzlement. Whether the customer breached her warranties under the U.C.C. depended on whether the settlement on the check became final. The Supreme Court overruled the trial court and held the settlement had become final. The return of the check occurred after the posting. The bank where the check was deposited was not entitled to a refund under 30-4-212. The customer warranties issue was decided by the principle that an agency could not be denied by a principal accepting its benefits. Because the appellant was not in breach of customer warranties, the bank's remedy, if any, was against the maker or the payee, the appellant's former husband. First Nat'l Bank v. Nunn, 192 M 487, 628 P2d 1110, 38 St. Rep. 869 (1981).

30-4-208. Security interest of collecting bank in items, accompanying documents, and proceeds.

Official Comment

Source: Section 4-210, U.C.C.

Prior Uniform Statutory Provision: See American Bankers Association Bank Collection Code, Section 2.

Purposes:

1. Subsection (1) states a rational rule for the interest of a bank in an item. The customer of the depositary bank is normally the owner of the item and the several collecting banks are his agents (Section 30-4-201). A collecting agent may properly make advances on the security of paper held by him for collection, and when he does acquires at common law a possessory lien for his advances. Subsection (1) applies an analogous principle to a bank in the collection chain which extends credit on items in the course of collection. The bank has a security interest to the extent stated in this section. To the extent of its security interest it is a holder for value (Sections 30-3-303, 30-4-209) and a holder in due course if it satisfies the other requirements for that status (Section 30-3-302). Subsection (1) does not derogate from the banker's general common-law lien or right of set-off against indebtedness owing in deposit accounts. See Section 30-1-103. Rather subsection (1) specifically implements and extends the principle as a part of the bank collection process.

2. Subsection (2) spreads the security interest of the bank over all items in a single deposit or received under a single agreement and a single giving of credit. It also adopts the "first-in, first-out" rule.

3. Collection statistics establish that in excess of ninety-nine percent of items handled for collection are in fact collected. The first sentence of subsection (3) reflects the fact that in such normal case the bank's security interest is self-liquidating. The remainder of the subsection correlates the security interest with the provisions of Chapter 9A, particularly for use in the cases of non-collection where the security interest may be important.

Compiler's Comments

1999 Amendment: Chapter 305 at end of (3)(a) substituted "30-9-213(2)(c)(i)" (renumbered 30-9A-203(2)(c)(i)) for "30-9-203". Amendment effective July 1, 2001.

1991 Amendment: At beginning of (1), after "A", inserted "collecting"; and made minor changes in style.

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

1983 Amendment: In (3)(a), deleted "subsection (1)(b) of" before "30-9-203)".

Montana Changes: In subsection (3)(a), Montana omits the parenthetical reference to subsection (1)(b) of 30-9-203.

30-4-209. When bank gives value for purposes of holder in due course.

Official Comment

Source: Section 4-211, U.C.C.

Prior Uniform Statutory Provision: Negotiable Instruments Law, Section 27.

Purpose:

The section completes the thought of the previous section and makes clear that a security interest in an item is "value" for the purpose of determining the holder's status as a holder in due course. The provision is in accord with the prior law (N.I.L. Section 27) and with Chapter 3 (Section 30-3-303). The section does not prescribe a security interest under Section 30-4-208 as a test of "value" generally because the meaning of "value" under other Chapters is adequately defined in Section 30-1-201.

Compiler's Comments

1991 Amendment: Made minor changes in style.

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

30-4-210. Presentment by notice of item not payable by, through, or at a bank — liability of secondary parties.

Official Comment

Source: Section 4-212, U.C.C.

Purposes:

1. This section codifies a practice extensively followed in presentation of trade acceptances and documentary and other drafts drawn on non-bank payors. It imposes a duty on the payor to respond to the notice of the item if the item is not to be considered dishonored. Notice of such a dishonor charges parties secondarily liable. Presentment under this Section is good presentment under Chapter 3. See Section 30-3-504(5).

2. A drawee not receiving notice is not, of course, liable to the drawer for wrongful dishonor.

3. A bank so presenting an instrument must be sufficiently close to the drawee to be able to exhibit the instrument on the day it is requested to do so or the next business day at the latest.

Compiler's Comments

1991 Amendment: In (1) and (2) substituted "30-3-504" for "30-3-505"; in (2), after "neither", substituted "payment, acceptance" for "honor"; and made minor changes in style.

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

30-4-211. Medium and time of settlement by bank.

Official Comment

Source: Section 4-213, U.C.C.

Prior Uniform Statutory Provision: See Sections 9 and 10, American Bankers Association Bank Collection Code.

Official Comment to 1991 Amendment:

1. Subsection (1) sets forth the medium of settlement that the person receiving settlement must accept. In nearly all cases the medium of settlement will be determined by agreement or by Federal Reserve regulations and circulars, clearinghouse rules, and the like. In the absence of

regulations, rules or agreement the person receiving settlement must accept cash or credit in a Federal Reserve bank. If the person receiving settlement does not have an account in a Federal Reserve bank, it may specify the account of another bank in a Federal Reserve bank. In the unusual case in which there is no agreement on the medium of settlement and the bank making settlement tenders settlement other than cash or Federal Reserve bank credit, no settlement has occurred under subsection (2) unless the person receiving settlement accepts the settlement tendered. For example, if a payor bank, without agreement, tenders a teller's check, the bank receiving the settlement may reject the check and return it to the payor bank or it may accept the check as settlement. In general, unless regulations or agreements provide otherwise, no settlement becomes final unless a payor bank has provided the collecting bank with usable funds. If the settlement fails, no settlement has occurred and a payor bank may be accountable under Section 4-302 [30-4-302].

2. In several provisions of Article 4 [Title 30, chapter 4] the time that a settlement occurs is relevant. Subsection (1) sets out a general rule that the time of settlement, like the means of settlement, may be prescribed by agreement. In the absence of agreement, the time of settlement for tender of the common agreed media of settlement is that set out in subsection (1)(b). The time of settlement by cash, cashier's or teller's check or authority to charge an account is the time the cash, check or authority is sent, unless presentment is over the counter in which case settlement occurs upon delivery to the presenter. If there is no agreement on the time of settlement and the tender of settlement is not made by one of the media set out in subsection (1), under subsection (2) the time of settlement is the time the settlement is accepted by the person receiving settlement.

3. Subsections (3) and (4) continue the policy of present Section 4-211(3) [30-4-211(3) prior to 1991 revision] in making special provisions for settlement by remittance drafts and authority to charge an account in the bank receiving settlement. With respect to settlement by cashier's checks or teller's checks, the bank receiving settlement can keep the risk that the check will not be paid on the bank tendering the check in settlement by acting to initiate collection of the check within the midnight deadline of the bank receiving settlement. If the bank fails to initiate settlement before its midnight deadline, final settlement occurs at the midnight deadline, and the bank receiving settlement assumes the risk that the check will not be paid. If there is no agreement that permits the bank tendering settlement to tender a cashier's or teller's check, subsection (2) allows the bank receiving the check to reject it, and, if it does, no settlement occurs. However, if the bank accepts the check, settlement occurs and the time of final settlement is governed by subsection (3).

With respect to settlement by tender of authority to charge the account of the bank making settlement in the bank receiving settlement, subsection (4) provides that final settlement does not take place until the account charged has available funds to cover the amount of the item. If there is no agreement that permits the bank tendering settlement to tender an authority to charge an account as settlement, subsection (2) allows the bank receiving the tender to reject it. However, if the bank accepts the authority, settlement occurs and the time of final settlement is governed by subsection (4).

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "Media of remittance — provisional and final settlement in remittance cases. (1) A collecting bank may take in settlement of an item:

(a) a check of the remitting bank or of another bank on any bank except the remitting bank; or

(b) a cashier's check or similar primary obligation of a remitting bank which is a member of or clears through a member of the same clearinghouse or group as the collecting bank; or

(c) appropriate authority to charge an account of the remitting bank or of another bank with the collecting bank; or

(d) if the item is drawn upon or payable by a person other than a bank, a cashier's check, certified check or other bank check or obligation.

(2) If before its midnight deadline the collecting bank properly dishonors a remittance check or authorization to charge on itself or presents or forwards for collection a remittance instrument of or on another bank which is of a kind approved by subsection (1) or has not been authorized by it, the collecting bank is not liable to prior parties in the event of the dishonor of such check, instrument or authorization.

(3) A settlement for an item by means of a remittance instrument or authorization to charge is or becomes a final settlement as to both the person making and the person receiving the settlement:

(a) if the remittance instrument or authorization to charge is of a kind approved by subsection (1) or has not been authorized by the person receiving the settlement and in either case the person receiving the settlement acts seasonably before its midnight deadline in presenting, forwarding for collection or paying the instrument or authorization,—at the time the remittance instrument or authorization is finally paid by the payor by which it is payable;

(b) if the person receiving the settlement has authorized remittance by a nonbank check or obligation or by a cashier's check or similar primary obligation of or a check upon the payor or other remitting bank which is not of a kind approved by subsection (1)(b),—at the time of the receipt of such remittance check or obligation; or

(c) if in a case not covered by subparagraphs (a) or (b) the person receiving the settlement fails to seasonably present, forward for collection, pay or return a remittance instrument or authorization to it to charge before its midnight deadline,—at such midnight deadline."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

30-4-212. Right of charge-back or refund — liability of collecting bank — return of item.

Official Comment

Source: Section 4-214, U.C.C.

Prior Uniform Statutory Provision: See Sections 2 and 11, American Bankers Association Bank Collection Code.

Purposes:

1. Under current bank practice, in a major portion of cases banks make provisional settlement for items when they are first received and then await subsequent determination of whether the item will be finally paid. This is the principal characteristic of what are referred to in banking parlance as "cash items". Statistically, this practice of settling provisionally first and then awaiting final payment is justified because more than ninety-nine percent of such cash items are finally paid, with the result that in this great preponderance of cases it becomes unnecessary for the banks making the provisional settlements to make any further entries. In due course the provisional settlements become final simply with the lapse of time. However, in those cases where the item being collected is not finally paid or where for various reasons the bank making the provisional settlement does not itself receive final payment, under the American Bankers Association Bank Collection Code, under Federal Reserve Regulations and operating letters and under various types of agreements between banks and between customers and banks, provision is made for the reversal of the provisional settlements, charge-back of provisional credits and the right to obtain refund. Subsection (1) codifies and simplifies the statement of these rights.

2. Various causes of a bank not receiving final payment, with the resulting right of charge-back or refund, are stated or suggested in subsection (1). These include dishonor of the original item; dishonor of a remittance instrument given for it; reversal of a provisional credit for the item; suspension of payments by another bank. The causes stated are illustrative; the right of charge-back or refund is stated to exist whether the failure to receive final payment in ordinary course arises through one of them "or otherwise".

3. The right of charge-back or refund exists if a collecting bank has made a provisional settlement for an item with its customer but terminates if and when a settlement received by the bank for the item is or becomes final. If the bank fails to receive such a final settlement the right of charge-back or refund must be exercised promptly after the bank learns the facts. The right exists (if so promptly exercised) whether or not the bank is able to return the item.

4. Subsection (2) is an affirmative provision for so-called "direct returns". This is a new practice that is currently in the process of developing in a few sections of the country. Its purpose is to speed up the return of unpaid items by avoiding handling by one or more intermediate banks. The practice is not yet well established and some bankers and bank lawyers would prefer to let the practice develop by agreement. The contention is made that substantive rights between banks may be affected, e.g., available set-offs, but proponents contend advantages of direct returns outweigh possible detriments. The payor bank, unless it has been specifically directed otherwise, will have the right to make the decision whether it will return an unpaid item directly.

5. The rule of subsection (4) relating to charge-back (as distinguished from claim for refund) applies irrespective of the cause of the nonpayment, and of the person ultimately liable for nonpayment. Thus charge-back is permitted even where nonpayment results from the depositary bank's own negligence. Any other rule would result in litigation based upon a claim for wrongful dishonor of other checks of the customer, with potential damages far in excess of the amount of the item. Any other rule would require a bank to determine difficult questions of fact. The customer's

protection is found in the general obligation of good faith (Sections 30-1-203 and 30-4-103). If bad faith is established the customer's recovery "includes other damages, if any, suffered by the party as a proximate consequence" (Section 30-4-103(5); see also Section 30-4-402).

6. It is clear that the charge-back does not relieve the bank from any liability for failure to exercise ordinary care in handling the item. The measure of damages for such failure is stated in Section 30-4-103(5).

7. Subsection (6) states a rule fixing the time for determining the rate of exchange if there is a charge-back or refund of a credit given in dollars for an item payable in a foreign currency. Compare Section 30-3-107(2). Fixing such a rule is desirable to avoid disputes. If in any case the parties wish to fix a different time for determining the rate of exchange, they may do so by agreement.

Official Comment to 1991 Amendment:

1. The amendment to subsection (1) adopts the view of Appliance Buyers Credit Corp. v. Prospect National Bank, 708 F.2d 290 (7th Cir. 1983), that if the midnight deadline for returning an item or giving notice is not met, a collecting bank loses its rights only to the extent of damages for any loss resulting from the delay.

2. Present subsection (2) [subsection (2) prior to 1991 revision] is deleted because direct return of checks is governed by Regulation CC which preempts subsection (2) with respect to checks. Proposed subsection (2) states the rule that applies to the return of items other than checks.

Compiler's Comments

1991 Amendment: In catchline inserted "liability of collecting bank — return of item"; in (1) inserted second sentence concerning return beyond midnight deadline and at end, in parenthetical, inserted reference to 30-4-211(4); substituted (2) concerning return by collecting bank for former (2) that read: "(2) Within the time and manner prescribed by this section and 30-4-301, an intermediary or payor bank, as the case may be, may return an unpaid item directly to the depositary bank and may send for collection a draft on the depositary bank and obtain reimbursement. In such case, if the depositary bank has received provisional settlement for the item, it must reimburse the bank drawing the draft and any provisional credits for the item between banks shall become and remain final"; in (6), in two places, substituted "money" for "currency" and after "basis of the" substituted "bank-offered spot rate" for "buying sight rate"; and made minor changes in style.

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Optional Subsection: Montana has included subsection (2) which was bracketed in the proposed act, as direct returns were not established banking practice when the U.C.C. was proposed.

Case Notes

Bank's Charge-Back Right Terminated Only on Final Settlement of Check — Estoppel Verdict Inapplicable to Bank's Right to Charge Back Provisional Settlement Funds From Defendant's Account — Fees and Costs: Shupak sold a car to a buyer in Germany for $7,400. The German sent Shupak a check for $11,500 and asked Shupak to send the $4,100 difference to a "shipper" in Belgium. Because of the unusual nature of the check and the misspelling of Shupak's name on the check, Shupak inquired with plaintiff credit union before cashing the check, and plaintiff authorized cashing the check. Shupak placed $4,000 in his account, made a loan payment on a vehicle, and mailed $4,100 to Belgium. The check was subsequently returned as counterfeit and plaintiff charged back Shupak's account for $11,500, leaving the account overdrawn and the vehicle loan past due. After unsuccessful attempts to repossess Shupak's vehicles, plaintiff eventually sued Shupak to recover the outstanding balance, which at that point was $8,185.97. Shupak raised several defenses, including estoppel, and countersued for negligence, malicious prosecution, breach of the duty of good faith under the Uniform Commercial Code, breach of fair debt collection practices, and fraud. The District Court concluded that plaintiff had a statutory right to charge back the money given Shupak for the fraudulent check and granted plaintiff partial summary judgment on that issue, but reserved judgment against Shupak until the jury could determine whether Shupak was entitled to offset the amount because of plaintiff's alleged negligent misrepresentations regarding the validity of the check. The jury ultimately found that plaintiff was 77.5% negligent and Shupak was 22.5% negligent, that the negligence had caused $5,000 in damages, and that plaintiff was estopped from enforcing the provisions of its membership and loan liner agreements, but Shupak's fraud and punitive damage claims were rejected. Shupak was awarded $3,874 for plaintiff's negligence, which was subtracted from the $8,185.97 owed to plaintiff by reason of the charge-back right, resulting in a net judgment to plaintiff of $4,310.97. Both parties then sought attorney fees and costs. Shupak was determined to be the prevailing party because he had prevailed on the negligence claim, despite plaintiff prevailing on the charge-back issue and receiving a net judgment, and Shupak was awarded fees and costs of $49,918.65, for a net judgment of $44,606.88 in Shupak's favor. Plaintiff appealed. The Supreme Court, citing Valley Bank of Ronan v. Hughes, 2006 MT 285, 334 M 335, 147 P3d 185 (2006), concluded that plaintiff's charge-back right terminated only upon final settlement of the check, and the right was not affected by Shupak's use of the provisional settlement funds or by plaintiff's failure to exercise ordinary care in handling the check for settlement purposes. Until a check becomes final, a bank may charge back provisional settlement funds to the customer, and the risk of loss remains with the customer, so the charge-back right may not be equitably estopped. Additionally, the District Court erred in awarding Shupak's attorney fees and costs. Plaintiff was entitled to that portion of its attorney fees and costs related to enforcement of its statutory charge-back right as a matter of law. Because plaintiff prevailed on the charge-back claim and received a net judgment, plaintiff was considered the prevailing party and the award of attorney fees and costs to Shupak was reversed. Avanta Fed. Credit Union v. Shupak, 2009 MT 458, 354 M 372, 223 P3d 863 (2009), followed in Total Indus. Plant Serv., Inc. v. Turner Indus. Group, LLC, 2013 MT 5, 368 Mont. 189, 294 P.3d 363.

Bank to Exercise Ordinary Care in Settling Checks — Common Law That Bank Exercise Ordinary Care in Processing Checks Preempted by Uniform Commercial Code: Hughes brought common-law claims against a bank for failing to exercise ordinary care in processing checks and for communications that the bank made regarding check processing. A bank that receives a check from a depositor must use ordinary care, as defined in the Uniform Commercial Code (U.C.C.), in settling those checks. However, when a check is processed by automated means, reasonable commercial standards do not require the bank to examine the check, subject to certain exceptions. To the extent that common-law claims relate to processing checks, the specific provisions of the U.C.C. prevail, so Hughes' claims regarding the propriety of the bank's check processing were preempted. However, because the U.C.C. does not address misrepresentation in communications, Hughes' common-law and equitable claims for negligence were not preempted by the U.C.C., and the District Court committed reversible error by failing to consider whether common-law and equitable principles supplement the U.C.C.-defined duty of ordinary care with respect to the bank's representations about the check settlement process. Valley Bank of Ronan v. Hughes, 2006 MT 285, 334 M 335, 147 P3d 185 (2006).

Validity of Promissory Note Executed to Satisfy Charge-Back Liability in Nigerian Scam: Hughes executed a promissory note to satisfy a charge-back liability necessitated by Hughes' participation in a Nigerian scam. Hughes made the first payment on the note, but failed to make any more payments, and the bank that issued the note initiated an action for judicial foreclosure. The District Court granted summary judgment to the bank on the promissory note, and Hughes appealed. The Supreme Court considered Hughes' arguments regarding lack of consideration, menace, and undue influence. Hughes became liable under this section for satisfying the entire charge-back debt, so the note did not fail for lack of consideration. Hughes' first quarterly payment comprised a ratification of the contract, so the note did not fail for consent because of menace. Whatever influence the bank employee exerted over Hughes, it did not rise to the level of substituting the employee's will for that of Hughes, nor was there any indication that Hughes was in a mentally or physically weak state or in a confidential relationship with the employee, so the note did not fail for lack of consent as a result of undue influence. Based on the claims made and the facts asserted, summary judgment for the bank was affirmed. Valley Bank of Ronan v. Hughes, 2006 MT 285, 334 M 335, 147 P3d 185 (2006), following Averill Mach. Co. v. Taylor, 70 M 70, 223 P 918 (1924), and Heintz v. Vestal, 185 M 233, 605 P2d 606 (1980).

Drawer and Payee Identical — Circuitous Accountability: Checks were drawn on the account of Capital Preservation Fund, Inc., maintained with First National Bank of Great Falls, Montana, by John Bennett, an authorized signatory on the account. The checks were endorsed and deposited by Bennett in another account he maintained with the Ashford Bank of Houston, Texas. Ashford Bank sent the checks through normal banking channels and extended cash to Bennett in reliance on the checks. The checks, however, were dishonored by First National Bank. Ashford then charged back the account of Bennett but alleged that it sustained a loss of $500,000. An affidavit from the Federal Reserve Bank established that First National had timely returned the checks in advance of the "midnight deadline". Bennett contended that payment became final prior to dishonor because First National had completed the process of posting. Section 30-4-213 provides that "final" payment by a drawee bank is the point at which all "provisional" settlements as allowed by 30-4-104(1)(j) in the bank collection chain became "final" settlements. Typically, provisional credits given through a clearinghouse or mutual bank account are made final upon payment of the item by completion of the process of posting the drawer's account. The agency relationships established under 30-4-201 are thereby transformed into a series of debtor-creditor relationships ending with the depository bank indebted to its customer for the amount of the item. The right of a collecting bank under 30-4-212(1) to charge back the account of its customer for any credit given for an item terminates when payment on the item becomes final. Section 30-4-213 holds a "payor" bank accountable for an item once "final" payment has been rendered. The "payor" bank must act in a timely manner in either dishonoring or paying the instrument. Timely dishonor was established. Bennett in this instance had the roles of both a "drawer" and the "payee". To allow Bennett to allege that payment by First National, the "payor" bank, was final would result in circuitous accountability. First National would simply charge the account on which the checks were drawn, Capital Preservation Fund, Inc., in order to recoup the amount paid. Capital Preservation Fund, Inc., would in turn have a cause of action against Bennett for recovery of the money. Any litigation emanating from this unique factual situation properly was between Capital Preservation Fund, Inc., and Bennett. The cause of action against First National Bank was found to be illusory, and it was granted summary judgment. Ashford Bank v. Capital Preservation Fund, Inc., 544 F. Supp. 26, 39 St. Rep. 1385 (D.C. Mont. 1982).

Deposit of Check Made to Another — When No Customer Warranties Breached — When Settlement of Check Final: A bank initiated an action against a customer to recover the amount of a check she deposited. The check was a paycheck made out to her former husband. She had deposited his paychecks for a time, and the Supreme Court found an agency relationship in the situation. On the occasion leading to this action, the appellant had deposited the check unsigned to her checking account. The bank stamped the check "deposited to the credit of" and filled in the name of the former husband. Meanwhile, the former husband told the check's issuer his ex-wife had forged his name on the check and deposited it. The issuer completed necessary documents and issued a new check. The former husband then disappeared, being suspected of embezzlement. Whether the customer breached her warranties under the U.C.C. depended on whether the settlement on the check became final. The Supreme Court overruled the trial court and held the settlement had become final. The return of the check occurred after the posting. The bank where the check was deposited was not entitled to a refund under 30-4-212. The customer warranties issue was decided by the principle that an agency could not be denied by a principal accepting its benefits. Because the appellant was not in breach of customer warranties, the bank's remedy, if any, was against the maker or the payee, the appellant's former husband. First Nat'l Bank v. Nunn, 192 M 487, 628 P2d 1110, 38 St. Rep. 869 (1981).

30-4-213. Final payment of item by payor bank — when provisional debits and credits become final — when certain credits become available for withdrawal.

Official Comment

Source: Section 4-215, U.C.C.

Prior Uniform Statutory Provision: See Section 11, American Bankers Association Bank Collection Code.

Purposes:

1. By the definition and use of the term "settle" (Section 30-4-104(j)) this Chapter recognizes that various debits or credits, remittances, settlements or payments given for an item may be either provisional or final, that settlements sometimes are provisional and sometimes are final and sometimes are provisional for awhile but later become final. Subsection (1) of Section 30-4-213 defines when settlement for an item or other action with respect to it constitutes final payment.

Final payment of an item is important for a number of reasons. It is one of several factors determining the relative priorities between items and notices, stop-orders, legal process and set-offs (Section 30-4-303). It is the "end of the line" in the collection process and the "turn around" point commencing the return flow of proceeds. It is the point at which many provisional settlements become final. See Section 30-4-213(2). Final payment of an item by the payor bank fixes preferential rights under Section 30-4-214(1) and (2).

2. If an item being collected moves through several states, e.g., is deposited for collection in California, moves through two or three California banks to the Federal Reserve Bank of San Francisco, to the Federal Reserve Bank of Boston, to a payor bank in Maine, the collection process involves the eastward journey of the item from California to Maine and the westward journey of the proceeds from Maine to California. Subsection (1) adopts the basic policy that final payment occurs at some point in the processing of the item by the payor bank. This policy recognizes that final payment does not take place, in such hypothetical case, on the journey of the item eastward.

It also adopts the view that neither does final payment occur on the journey westward because what in fact is journeying westward are *proceeds* of the item. Because the true tests of final payment are the same in all cases and to avoid the confusion resulting from variable standards, the rule basing final payment exclusively on action of the payor bank is not affected by whether payment is made by a remittance draft or whether such draft is itself paid. Consequently, subsection (1) rejects those cases which base time of payment of the item in remittance cases on whether the remittance draft was *accepted* by the presenting bank; Page v. Holmes-Darst Coal Co. 269 Mich. 159, 256 N.W. 840 (1934); Tobiason v. First State Bank of Ashby, 173 Minn. 533, 217 N.W. 934 (1928); Bohlig v. First Nat. Bank in Wadena, 233 Minn. 523, 48 N.W.2d 445 (1951); Dewey v. Margolis & Brooks, 195 N.C. 307, 142 S.E. 22 (1928); Texas Electric Service Co. v. Clark, 47 S.W.2d 483 (Tex. Civ. App. 1932); cf. Ellis Way Drug Co. v. McLean, 176 Miss. 830, 170 So. 288 (1936); 2 Paton's Digest 1332; or whether the remittance draft was itself *paid*; Cleve v. Craven Chemical Co., 18 F.2d 711 (4th Cir. 1927); Holdingford Milling Co. V. Hillman Farmers' Cooperative Creamery, 181 Minn. 212, 231 N.W. 928 (1930); or upon an election of a collecting bank under Section 11 of the American Bankers Association Bank Collection Code; United States Pipe & Foundry Co. v. City of Hornell, 146 Misc. 812, 263 N.Y.S. 89 (1933); Jones v. Board of Education, 242 App. Div. 17, 272 N.Y.S. 5 (1934); Matter of State Bank of Binghamton, 156 Misc. 353, 281 N.Y.S. 706 (1935); cf. Malcolm, Inc. v. Burlington City Loan & Trust Co., 115 N.J. Eq. 227, 170 A. 32 (1934). Of course, the time of payment of the remittance draft will be governed by subsection (1) but payment or nonpayment of the remittance draft will not change the time of payment of the original item.

3. In fixing the point of time within the payor bank when an item is finally paid, subsection (1) recognizes and is framed on the basis that in a payor bank an item goes through a series of processes before its handling is completed. The item is received first from the clearing house or over the counter or through the mail. When received over the counter, the bank may receipt for it in some way by making a notation in the customer's passbook or by receipting a duplicate deposit slip. After the initial receipt the item moves to the sorting and proving departments. When sorted and proved it may be photographed. Still later it moves to the bookkeeping department where it is examined for form and signature and compared against the ledger account of the customer to whom it is to be charged. If it is in good form and there are funds to cover it, it is posted to the drawer's account, either immediately or at a later time. If paid, it is so marked and filed with other items of the same customer. This process may take either a few hours or substantially all of the day of receipt and of the next banking day.

Within this period of processing by the payor bank subsection (1) first recognizes two types of overt external acts constituting final payment. Traditionally and under various decisions payment in cash of an item by a payor bank has been considered final payment. Chambers v. Miller, 13 C.B.N.S. 125 (Eng. 1862); Fidelity & Casualty Co. of New York v. Planenscheck, 200 Wis. 304, 309, 227 N.W. 387, 389, 71 A.L.R. 331 (1929); see Bellevue Bank of Allen Kimberly & Co. v. Security Nat. Bank of Sioux City, 168 Iowa 707, 712, 150 N.W. 1076, 1077 (1915); 1 Paton's Digest 1066. Subsection (1)(a) first recognizes and provides that payment of an item in cash by a payor bank is final payment.

4. Section 30-4-104(j) defines "settle" as meaning "to pay in cash, by clearing house settlement, in a charge or credit or by remittance, or otherwise as instructed. A settlement may be either provisional or final;" Subsection (1)(b) of Section 30-4-213 provides that an item is finally paid by a payor bank when the bank has "settled for the item without reserving a right to revoke the settlement and without having such right under statute, clearing house rule or agreement". Subsection (1)(b) provides in effect that if the payor bank finally settles for an item this constitutes final payment of the item. The subsection operates if nothing has occurred and no situation exists making the settlement provisional. If at the time of settlement the payor bank reserves a right to revoke the settlement, the settlement is provisional. In the alternative, if under statute, clearing house rule or agreement, a right of revocation of the settlement exists the settlement is provisional. Conversely, if there is an absence of a reservation of the right to revoke and also an absence of a right to revoke under statute, clearing house rule or agreement, the settlement is final and such final settlement constitutes final payment of the item.

A primary example of a statutory right on the part of the payor bank to revoke a settlement is the right to revoke conferred by Section 30-4-301. The underlying theory and reason for deferred posting statutes (Section 30-4-301) is to require a settlement on the date of receipt of an item but to keep that settlement provisional with the right to revoke prior to the midnight deadline. In any case where Section 30-4-301 is applicable, any settlement by the payor bank is provisional solely by virtue of the statute, subsection (1)(b) of Section 30-4-213 does not operate and such provisional settlement does not constitute final payment of the item.

A second important example of a right to revoke a settlement is that arising under clearing house rules. It is very common for clearing house rules to provide that items exchanged and settled for in a clearing, (e.g., before 10:00 a.m. on Monday) may be returned and the settlements revoked up to but not later than 2:00 p.m. on the same day (Monday) or under deferred posting at some hour on the next business day (e.g., 2:00 p.m. Tuesday). Under this type of rule the Monday morning settlement is provisional and being provisional does not constitute a final payment of the item.

An example of a reservation of a right to revoke a settlement is where the payor bank is also the depositary bank and has signed a receipt or duplicate deposit ticket or has made an entry in a passbook acknowledging receipt, for credit to the account of A, of a check drawn on it by B. If the receipt, deposit ticket, passbook or other agreement with A is to the effect that any credit so entered is provisional and may be revoked pending the time required by the payor bank to process the item to determine if it is in good form and there are funds to cover it, such reservation or agreement keeps the receipt or credit provisional and avoids it being either final settlement or final payment.

In other ways the payor bank may keep settlements provisional: by general or special agreement with the presenting party or bank; by simple reservation at the time the settlement is made; or otherwise. Thus a payor bank (except in the case of statutory provisions) has control whether a settlement made by it is provisional or final, by participating in general agreements or clearing house rules or by special agreement or reservation. If it fails to keep a settlement provisional and if no applicable statute keeps the settlement provisional, its settlement is final and, unless the item had previously been paid by one of the other methods prescribed in subsection (1), such final settlement constitutes final payment. In this manner payor banks may without difficulty avoid the effect of such cases as: Cohen v. First Nat. Bank of Nogales, 22 Ariz. 394, 400 198 P. 122, 124, 15 A.L.R. 701 (1921); Briviesca v. Coronado, 19 Cal.2d 244, 120 P.2d 649 (1941); White Brokerage Co. v. Cooperman, 207 Minn. 239, 290 N.W. 790 (1940); Scotts Bluff County v. First Nat. Bank of Gering, 115 Neb. 273, 212 N.W. 617 (1927); Provident Savings Bank & Trust Co. v. Hildebrand, 49 Ohio App. 207, 196 N.E. 790, 791 (1934); Schaer v. First Nat. Bank of Brenham, 132 Tex. 499, 124 S.W.2d 108 (1939) (bill of exchange); Union State Bank of Lancaster v. Peoples State Bank of Lancaster, 192 Wis. 28, 33, 211 N.W. 931, 933 (1927); 1 Paton's Digest 1067.

5. If a payor bank has not previously paid an item in cash or finally settled for it, certain internal acts or procedures will produce final payment of the item. Exclusive of the external acts of payment in cash or final settlement, the key point at which the decision of the bank to pay or dishonor is made is when the bookkeeper for the drawer's account determines or verifies that the check is in good form and that there are sufficient funds in the drawer's account to cover it. Previous steps in the processing of an item are preliminary to this vital step and in no way indicate a decision to pay. However, a more tangible measuring point is desirable than a mere examination of the account of the person to be charged. The mechanical step that usually indicates that the examination has been completed and the decision to pay has been made is the posting of the item to the account to be charged. Therefore, subsection (1)(c) adopts as the third measuring point the completion of the process of posting. The phrase "completed the process of posting" is used rather than simple "posting" because under current machine operations posting is a process and something more than simply making entries on the customer's ledger. Subsection (1) follows fairly closely the New York statute, 37 McKinney's Consolidated Laws of New York, Negotiable Instruments, Art. 19-A, Sec. 350-b as amended by L. 1950, C. 153, Sec. 1. However, subsections (1)(a) and (b) furnish more precise rules for determining "final settlement" by the payor bank than does the New York statute in using the term "irrevocable credit", the definition of which is not helpful.

6. Subsection (1)(d) covers the situation where the payor bank makes a provisional settlement for an item, which settlement becomes final at a later time by reason of the failure of the payor bank to revoke it in the time and manner permitted by statute, clearing house rule or agreement. An example of this type of situation is the clearing house settlement referred to in Comment 4. In the illustration there given if the time limit for the return of items received in the Monday morning clearing is 2:00 p.m. on Tuesday and the provisional settlement has not been revoked at that time in a manner permitted by the clearing house rules, the provisional settlement made on Monday morning becomes final at 2:00 p.m. on Tuesday. Subsection (1)(d) provides specifically that in this situation the item is finally paid at 2:00 p.m. Tuesday. If on the other hand a payor bank receives an item in the mail on Monday and makes some provisional settlement for the

item on Monday, it has until midnight on Tuesday to return the item or give notice and revoke any settlement under Section 30-4-301. In this situation subsection (1)(d) of Section 30-4-213 provides that if the provisional settlement made on Monday is not revoked before midnight on Tuesday as permitted by Section 30-4-301, the item is finally paid at midnight on Tuesday even if the process of posting the item to the account of the drawer has not been completed at that time.

7. Subsection (1) provides that an item is finally paid by the payor bank when any one of the four events set forth in subparagraphs (a), (b), (c) and (d) have occurred, whichever happens first, and then provides that upon a final payment under subparagraphs (b), (c) or (d) the payor bank shall be accountable for the amount of the item. It is not made accountable if it has paid the item in cash because such payment is itself a sufficient accounting. The term "accountable" is used as imposing a duty to account, which duty is met if and when a settlement for the item satisfactorily clears. The fact that determination of the time of final payment is based exclusively upon action of the payor bank is not detrimental to the interests of owners of items or collecting banks because of the general obligations of payors to honor or dishonor and the time limits for action imposed by Sections 30-4-301 and 30-4-302.

8. Subsection (2) states the country-wide usage that when the item is finally paid by the payor bank under subsection (1) this final payment automatically without further action "firms up" other provisional settlements made for it. However, the subsection makes clear that this "firming up" occurs only where the settlement between the presenting and payor banks was made either through a clearing house or by debits and credits in accounts between them. It does not take place where the payor bank remits for the item with some form of remittance instrument. Further, the "firming up" continues only to the extent that provisional debits and credits are entered seriatim in accounts between banks which are successive to the presenting bank. The automatic "firming up" is broken at any time that any collecting bank remits for the item with a remittance draft, because final payment to the remittee then usually depends upon final payment of the remittance draft.

9. Subsection (3) states the general rule that if a collecting bank receives settlement for an item which is or becomes final, the bank is accountable to its customer for the amount of the item. One means of accounting is to remit to its customer the amount it has received on the item. If previously it gave to its customer a provisional credit for the item in an account its receipt of final settlement for the item "firms up" this provisional credit and makes it final. When this credit given by it so becomes final, in the usual case its agency status terminates and it becomes a debtor to its customer for the amount of the item. See Section 30-4-201(1). If the accounting is by a remittance instrument or authorization to charge further time will usually be required to complete its accounting (Section 30-4-211).

10. Subsection (4) states when certain credits given by a bank to its customer become available for withdrawal as of right. Subsection (4)(a) deals with the situation where a bank has given a credit (usually provisional) for an item to its customer and in turn has received a provisional settlement for the item from an intermediary or payor bank to which it has forwarded the item. In this situation before the provisional credit entered by the collecting bank in the account of its customer becomes available for withdrawal as of right, it is not only necessary that the provisional settlement received by the bank for the item becomes final but also that the collecting bank has a reasonable time to learn that this is so. Hence, subsection (4)(a) imposes both of these conditions. If the provisional settlement received is a provisional debit or credit in an account with the intermediary or payor bank or a remittance instrument on some bank other than the collecting bank itself, the collecting bank will usually learn that this debit or credit is final or that the remittance instrument has been paid merely by not learning the opposite within a reasonable time. How much time is "reasonable" for these purposes will of course depend on the distance the item has to travel and the number of banks through which it must pass (having in mind not only travel time by regular lines of transmission but also the successive midnight deadlines of the several banks) and other pertinent facts. Also, if the provisional settlement received is some form of a remittance instrument or authorization to charge, the "reasonable" time depends on the identity and location of the payor of the remittance instrument, the means for clearing such instrument and other pertinent facts.

11. Subsection (4)(b) deals with the situation of a bank which is both a depositary bank and a payor bank. The subsection recognizes that where A and B are both customers of a depositary-payor bank and A deposits B's check on the depositary-payor in A's account on Monday, time must be allowed to permit the check under the deferred posting rules of Section 30-4-301 to reach the bookkeeper for B's account at some time on Tuesday, and if there are insufficient funds in B's account to reverse or charge back the provisional credit in A's account. Consequently this

provisional credit in A's account does not become available for withdrawal as of right until the opening of business on Wednesday. If it is determined on Tuesday that there are insufficient funds in B's account to pay the check the credit to A's account can be reversed on Tuesday. On the other hand if the item is in fact paid on Tuesday, the rule of subsection (4)(b) is desirable to avoid uncertainty and possible disputes between the bank and its customer as to exactly what hour within the day the credit is available.

12. Subsection (5) recognizes that even when A makes a deposit of cash in his account on Monday it takes some period of time to record that cash deposit and communicate it to A's bookkeeper (the bookkeeper handling A's account) so that A's bookkeeper has a record of it when she considers whether there are available funds to pay A's check. Where as indicated in Comment 5 A's bookkeeper is the particular employee in the bank to determine, in most cases and subject to supervisory control, whether the item may be paid, the effectiveness of a deposit of cash as a basis for paying a check must of necessity rest upon when the record of that deposit reaches such bookkeeper rather than when it passes through the teller's window. Consequently, although the bank is charged with responsibility for cash deposited from the moment it is received on Monday the cash is not effective as a basis for paying checks until the opening of business on Tuesday.

Official Comment to 1991 Amendment:

1. Subsection (1)(b) is modified to make clear that a payor bank cannot make settlement provisional by unilaterally reserving a right to revoke the settlement. The right must come from a statute (*e.g.*, Section 4-301 [30-4-301]), clearing house rule or other agreement. Subsection (1)(c) is deleted for the reasons discussed in the comment to deleted Section 4-109 [30-4-109, now repealed].

2. The last sentence of present Section 4-213(1) [30-4-213(1) prior to 1991 revision] is deleted as an unnecessary source of confusion. Initially the view that payor bank may be accountable for, that is, liable for the amount of, an item that it has already paid seems incongruous. This is particularly true in the light of the language found in present Section 4-302 [30-4-302 prior to 1991 revision] stating that the payor bank can defend against liability for accountability by showing that it has already settled for the item. But, at least with respect to present Section 4-213(1)(c) [30-4-213(1)(c) prior to 1991 revision], such a provision is needed because under the process-of-posting test a payor bank may have paid a check without settling for it. Now that proposed Article 4 [Title 30, chapter 4] has abandoned the process-of-posting test, the sentence is no longer needed. If a purported settlement fails to provide the collecting bank with usable funds, no settlement has occurred and the payor bank may be accountable under Section 4-302 [30-4-302].

3. Proposed subsection (4) states when a depositor has a right to withdraw the proceeds of deposited items from its account. "Applicable law" means Regulation CC or state laws providing funds availability schedules. Present subparagraph (4)(a) [subsection (4)(a) prior to 1991 revision] was impractical in making the time for withdrawal depend on when a collecting bank has had a reasonable time to learn that the settlement is final because a bank will not know when a settlement is final.

Compiler's Comments

1997 Amendment: Chapter 42 in (3) substituted "subsection (2) of this section" for "subsection (2) of 30-4-213". Amendment effective March 12, 1997.

1991 Amendment: In (1)(b), after "without", substituted "having" for "reserving" and after "settlement" deleted "and without having such right"; deleted former (1)(c) that read: "(c) completed the process of posting the item to the indicated account of the drawer, maker or other person to be charged therewith"; in (1)(c) deleted former second sentence that read: "Upon a final payment under subparagraphs (b), (c) or (d) the payor bank shall be accountable for the amount of the item"; in (3), in parenthetical, inserted reference to 30-4-211(4); in (4), after "Subject to", inserted "applicable law stating a time for availability of funds and"; at end of (4)(a) substituted "receive return of the item and the item has not been received within that time" for "learn that the settlement is final"; at beginning of (5) substituted "Subject to applicable law stating a time for availability of funds and" for "A deposit of money in a bank is final when made but, subject to", near middle, after "obligation of the", substituted "depositor" for "customer", and after "deposit" inserted "of money"; and made minor changes in style.

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

Drawer and Payee Identical — Circuitous Accountability: Checks were drawn on the account of Capital Preservation Fund, Inc., maintained with First National Bank of Great Falls, Montana, by John Bennett, an authorized signatory on the account. The checks were endorsed and deposited by Bennett in another account he maintained with the Ashford Bank of Houston, Texas. Ashford Bank sent the checks through normal banking channels and extended cash to Bennett in reliance on the checks. The checks, however, were dishonored by First National Bank. Ashford then charged back the account of Bennett but alleged that it sustained a loss of $500,000. An affidavit from the Federal Reserve Bank established that First National had timely returned the checks in advance of the "midnight deadline". Bennett contended that payment became final prior to dishonor because First National had completed the process of posting. Section 30-4-213 provides that "final" payment by a drawee bank is the point at which all "provisional" settlements as allowed by 30-4-104(1)(j) in the bank collection chain became "final" settlements. Typically, provisional credits given through a clearinghouse or mutual bank account are made final upon payment of the item by completion of the process of posting the drawer's account. The agency relationships established under 30-4-201 are thereby transformed into a series of debtor-creditor relationships ending with the depository bank indebted to its customer for the amount of the item. The right of a collecting bank under 30-4-212(1) to charge back the account of its customer for any credit given for an item terminates when payment on the item becomes final. Section 30-4-213 holds a "payor" bank accountable for an item once "final" payment has been rendered. The "payor" bank must act in a timely manner in either dishonoring or paying the instrument. Timely dishonor was established. Bennett in this instance had the roles of both a "drawer" and the "payee". To allow Bennett to allege that payment by First National, the "payor" bank, was final would result in circuitous accountability. First National would simply charge the account on which the checks were drawn, Capital Preservation Fund, Inc., in order to recoup the amount paid. Capital Preservation Fund, Inc., would in turn have a cause of action against Bennett for recovery of the money. Any litigation emanating from this unique factual situation properly was between Capital Preservation Fund, Inc., and Bennett. The cause of action against First National Bank was found to be illusory, and it was granted summary judgment. Ashford Bank v. Capital Preservation Fund, Inc., 544 F. Supp. 26, 39 St. Rep. 1385 (D.C. Mont. 1982).

30-4-214. Insolvency and preference.

Official Comment

Source: Section 4-216, U.C.C.

Prior Uniform Statutory Provision: See Section 13, American Bankers Association Bank Collection Code.

Purposes:

1. The underlying purpose of the provisions of this section is not to confer upon banks, holders of items or anyone else preferential positions in the event of bank failures over general depositors or any other creditors of the failed banks. The purpose is to fix as definitely as possible the cut-off point of time for the completion or cessation of the collection process in the case of items that happen to be in such process at the time a particular bank suspends payments. It must be remembered that in bank collections as a whole and in the handling of items by an individual bank, items go through a whole series of processes. It must also be remembered that at any particular point of time a particular bank (at least one of any size) is functioning as a depositary bank for some items, as an intermediary bank for others, as a presenting bank for still others and as a payor bank for still others, and that when it suspends payments it will have close to its normal load of items working through its various processes. For the convenience of receivers, owners of items, banks, and in fact substantially everyone concerned, it is recognized that at the particular moment of time that a bank suspends payment, a certain portion of the items being handled by it have progressed far enough in the bank collection process that it is preferable to permit them to continue the remaining distance, rather than to send them back and reverse the many entries that have been made or the steps that have been taken with respect to them. Therefore, having this background and these purposes in mind, the section states what items must be turned backward at the moment suspension intervenes and what items have progressed far enough that the collection process with respect to them continues, with the resulting necessary statement of rights of various parties flowing from this prescription of the cut-off time.

2. The rules stated are similar to those stated in the American Bankers Association Bank Collection Code, but with the abandonment of any theory of trust. Although for practical purposes Federal Deposit Insurance affects materially the result of bank failures on holders of items and banks, no attempt is made to vary the rules of the section by reason of such insurance.

3. It is recognized that in view of Jennings v. United States Fidelity & Guaranty Co., 294 U.S. 216, 55 S.Ct. 394, 79 L.Ed. 869, 99 A.L.R. 1248 (1935), amendment of the National Bank Act would be necessary to have this section apply to national banks. But there is no reason why it should not apply to others. See Section 30-1-108.

Compiler's Comments

1991 Amendment: In (3), in parenthetical, inserted references to 30-4-211(4) and 30-4-213(1)(c); and made minor changes in style.

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

30-4-215. Presentment warranties.

Official Comment

Source: Section 4-208, U.C.C.

Official Comment:

This section conforms to Section 3-417 [30-3-424] and extends its coverage to items. The substance of this section is discussed in the comment to Section 3-417 [30-3-424]. "Draft" is defined in Section 4-104 [30-4-104] as including an item that is an order to pay so as to make clear that the term "draft" in Article 4 [Title 30, chapter 4] may include items that are not instruments within Section 3-104 [30-3-104].

30-4-216. Encoding and retention warranties.

Official Comment

Source: Section 4-209, U.C.C.

Official Comment:

1. Encoding and retention warranties are included in Article 4 [Title 30, chapter 4] because they are unique to the bank collection process. These warranties are breached only by the person doing the encoding or retaining the item and not by subsequent banks handling the item. Encoding and check retention may be done by customers who are payees of a large volume of checks; hence, this section imposes warranties on customers as well as banks. If a customer encodes, the depositary bank is also liable for any breach of this warranty.

2. A misencoding of the amount on the MICR line is not a material alteration under Section 3-407(a) [30-3-407(1)] which defines alteration as changing the contract of the parties. If a drawer wrote a check for $2,500 and the depositary bank encoded $25,000 on the MICR line, the payor bank could debit the drawer's account for only $2,500. This subsection would allow the payor bank to hold the depositary bank liable for the amount paid out over $2,500. Intervening collecting banks would not be liable to the payor bank for the depositary bank's error. If a drawer wrote a check for $25,000 and the depositary bank encoded $2,500, the payor bank becomes liable for the full amount of the check. The payor bank's rights against the depositary bank depend on whether the payor bank has suffered a loss. Since the payor bank can debit the drawer's account for $25,000, the payor bank has a loss only to the extent that the drawer's account is less than the full amount of the check. See Georgia Railroad Bank & Trust Co. v. First National Bank & Trust, 229 S.E.2d 482 (Ga. App. 1976), *aff'd*, 235 S.E.2d 1 (Ga. 1977).

3. A keeper under a truncation agreement warrants that it has complied with the terms of the agreement regarding its possession of the item and its sending a proper presentment notice. If the keeper is a customer, its depositary bank also makes this warranty.

Part 3
Collection of Items — Payor Banks

30-4-301. Deferred posting — recovery of payment by return of items — time of dishonor — return of items by payor bank.

Official Comment

Source: Section 4-301, U.C.C.

Prior Uniform Statutory Provision: See American Bankers Association Model Deferred Posting Statute.

Purposes:

1. Deferred posting and delayed returns is that practice whereby a payor bank sorts and proves items received by it on the day they are received, e.g., Monday, but does not post the items to the customer's account or return "not good" items until the next day, e.g., Tuesday. The practice typifies "production line" methods currently used in bank collection and is based upon the necessity of an even flow of items through payor banks on a day by day basis in a manner which can be handled evenly by employee personnel without abnormal peak load periods, night

work, and other practices objectionable to personnel. Since World War II statutes authorizing deferred posting and delayed returns have been passed in almost all of the states. This section codifies the content of these statutes and approves the practice.

2. The time limits for action imposed by Subsection (1) are adopted by Subsection (2) for cases where the payor bank is also the depositary bank, but in this case the requirement of a settlement on the day of receipt is omitted.

3. Subsection (3) fixes a base point from which to measure the time within which notice of dishonor must be given. See Section 30-3-508.

4. Subsection (4) leaves banks free to agree upon the manner of returning items but establishes a precise time when an item is "returned". For definition of "sent" as used in subsections (a) and (b) see Section 30-1-201(38).

5. Obviously the section assumes that the item has not been "finally paid" under Section 30-4-213(1). If it has been, this section has no operation.

Official Comment to 1991 Amendment:

1. The term "authorized settlement" is deleted from subsection (1). It is not defined in present Article 4 [Title 30, chapter 4] and is no longer needed in proposed Section 4-301 [30-4-301] because of the provisions in proposed Section 4-213(1) [30-4-211(1)] concerning the medium of settlement.

2. The function of this section is to provide the circumstances under which a payor bank that has made timely settlement for an item may return the item and revoke the settlement so that it may recover any settlement made. These circumstances are: (1) the item must be a demand item other than a documentary draft; (2) the item must be presented otherwise than for immediate payment over the counter; and (3) the payor bank must return the item (or give notice if the item is unavailable for return) before its midnight deadline and before it has paid the item in cash. Subsection 4-215(1)(b) [30-4-213(1)(b)] provides that final payment occurs if the payor bank has settled for an item without a right to revoke the settlement under statute, clearing house rule or agreement. Comment 4 to present Section 4-213 [30-4-213 prior to 1991 revision] states: "In any case where Section 4-301 [30-4-301 prior to 1991 revision] is applicable, any settlement by the payor bank is provisional solely by virtue of the statute, subsection (1)(b) of Section 4-213 [30-4-213(1)(b) prior to 1991 revision] does not operate and such provisional settlement does not constitute final payment of the item." Hence, if the settlement is not over the counter and the payor bank settles by any medium other than cash (Section 4-215(1)(a) [30-4-213(1)(a)]), the payor bank can revoke the settlement by returning the item before its midnight deadline. The amendment to Section 4-301(1) [30-4-301(1)] spells out this result more clearly by deleting any reference to Section 4-215(1)(b) [30-4-213(1)(b)].

3. The fact that an item has been paid under proposed Section 4-215 [30-4-213] does not preclude the payor bank from asserting rights of restitution or revocation under Section 3-418 [30-3-425]. National Savings and Trust Co. v. Park Corp., 722 F.2d 1303 (6th Cir. 1983), cert. denied, 466 U.S. 939 (1984), is the correct interpretation of the present law on this issue.

Compiler's Comments

1991 Amendment: In catchline, at end, inserted "return of items by payor bank"; at beginning of (1) substituted "If a payor bank settles" for "Where an authorized settlement", after "documentary draft" substituted "presented" for "received by a payor bank", after "recover any" substituted "settlement" for "payment", before parenthetical substituted "paid the item in cash" for "made final payment", and in parenthetical inserted reference to subsection (a) of 30-4-213(1); in (1)(b), after "item is", deleted "held for protest or is otherwise"; in (4)(a), after "item", substituted "presented" for "received"; and made minor changes in style.

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

30-4-302. Payor bank's responsibility for late return of item.

Official Comment

Source: Section 4-302, U.C.C.

Prior Uniform Statutory Provision: See American Bankers Association Model Deferred Posting Statute.

Purposes:

Under Section 30-4-301, time limits are prescribed within which a payor bank must take action if it receives an item payable by it. Section 30-4-302 states the rights of the customer if the payor bank fails to take the action required within the time limits prescribed.

Official Comment to 1991 Amendment:

1. Subsection (1)(a) continues the present law [prior to 1991 revision] distinguishing between cases in which the payor bank is not also the depositary bank and those in which the payor bank

is also the depositary bank ("on us" items). For "on us" items the payor bank is accountable if it retains the item beyond its midnight deadline without settling for it. If the payor bank is not the depositary bank it is accountable if it retains the item beyond midnight of the banking day of receipt without settling for it. It may avoid accountability either by settling for the item on the day of receipt and returning the item before its midnight deadline under Section 4-301 [30-4-301] or by returning the item on the day of receipt. This rule is consistent with the deferred posting practice authorized by Section 4-301 [30-4-301] which allows the payor bank to make provisional settlement for an item on the day of receipt and to revoke that settlement by returning the item on the next day.

2. If the settlement given by a payor bank fails, there has been no settlement under this section and the payor bank remains accountable. For example, the payor bank purports to settle either by giving a teller's check drawn on an account in which there are insufficient funds to pay the check, or by giving a collecting bank authority to charge the account of the payor bank which contains insufficient funds. In these cases no final settlement has taken place (subsections (3) and (4) of Section 4-213 [30-4-211(3) and (4)]), and the payor bank remains liable.

3. Subsection (2) is an elaboration of the deleted introductory language of present Section 4-302 [30-4-302 prior to 1991 revision]. "In the absence of a valid defense such as breach of a presentment warranty (subsection (1) of Section 4-207 [30-4-207(1) prior to 1991 revision]), settlement effected or the like ..." A payor bank can defend an action against it based on accountability by showing that the item contained a forged indorsement or a fraudulent alteration. Proposed subsection (2) drops the ambiguous "or the like" language and provides that the payor bank may also raise the defense of fraud. Decisions that hold an accountable bank's liability to be "absolute" are rejected. A payor bank that makes a late return of an item should not be liable to a defrauder operating a check kiting scheme. In Bank of Leumi Trust Co. v. Balley's Park Place Inc., 528 F.Supp. 349 (S.D.N.Y. 1981), and American National Bank v. Foodbasket, 497 P.2d 546 (Wyo. 1972), banks that were accountable under Section 4-302 [30-4-302] for missing their midnight deadline were successful in defending against parties who initiated collection knowing that the check would not be paid. The "settlement effected" language is deleted as unnecessary. If a payor bank is accountable for an item it is liable to pay it. If it has made final payment for an item, it is no longer accountable for the item.

Compiler's Comments

1991 Amendment: At beginning of (1) deleted "In the absence of a valid defense such as breach of a presentment warranty (subsection (1) of 30-4-207), settlement effected or the like"; inserted (2) concerning liability of payor bank; and made minor changes in style.

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

1987 Amendment: Substituted "(1)" and "(2)" for "(a)" and "(b)".

Case Notes

"Demand Item" and "Presentment" Construed — Waiver of Midnight Deadline Rule: When defendant's, Nuernberger's, check was twice refused and returned for insufficient funds by the payor bank, First Bank of Billings (First Bank), an officer of the joint payee, Montana Livestock Production Credit Association (MLPCA) returned the check to First Bank with a written memo authorizing First Bank to "hold it for longer than the usual 24-hour period" and to pay when funds became available. The District Court granted summary judgment for the plaintiff (the other joint payee) and MLPCA and found First Bank strictly liable for the face amount of the check because of its failure to comply with the midnight deadline rule. The Supreme Court reversed and found that the midnight deadline rule did not apply, holding that the check was not a "demand item" because it was transmitted with the understanding it would be held for sufficient funds and that there had been no "presentment" by the plaintiff, but only by the joint payee, MLPCA. The Supreme Court further held that there had been a waiver of the midnight rule time requirements by MLPCA's memo. Iverson v. First Bank of Billings, 219 M 283, 712 P2d 1285, 42 St. Rep. 2021 (1985).

"Accountable" Construed: The word "accountable" as used in this section is synonymous with "liable". Sun River Cattle Co., Inc. v. Miners Bank of Mont., 164 M 237, 521 P2d 679 (1974).

Construction: Essentially this section says that in absence of a valid defense, retention by payor bank of a demand item beyond the "midnight deadline" without either paying, returning or giving notice of dishonor renders the bank liable to the payee for the face amount of the item. Sun River Cattle Co., Inc. v. Miners Bank of Mont., 164 M 237, 521 P2d 679 (1974).

Interest on Judgment: Determination by the Court that the bank was liable for payment of dishonored checks by virtue of this section was based on contract law of negotiable instruments, and interest was ordered from the second day after the bank's final receipt of the checks. Sun River Cattle Co., Inc. v. Miners Bank of Mont., 164 M 479, 525 P2d 19 (1974).

"Midnight Rule"— Failure to Give Notice of Dishonor: "Midnight rule" was applicable to payor bank and rendered it liable to payees for face amount of checks presented for collection since: (1) the checks were demand items and 30-3-511(4) (now repealed) was thus inapplicable and did not operate to excuse failure to give timely notice of dishonor; (2) there was no agreement between the parties under 30-4-103 excepting bank from strict liability since bank's holding and paying of one check as to each of two of the plaintiffs was not sufficient to form "a sequence of previous conduct" necessary to establish a course of dealing from which an agreement could be implied under 30-1-201(3) and 30-1-205(1); (3) alleged understanding with one payee's agent would not be considered an agreement under 30-4-103 in view of bank's unique position as drawers' creditor; (4) any oral notice of dishonor given to one plaintiff was ineffective under the circumstances; and (5) custom and practice were not relevant since their relevancy lay only in establishing what standard should constitute ordinary care and bank was subject to more than ordinary standard of care because of its unique position. Sun River Cattle Co., Inc. v. Miners Bank of Mont., 164 M 237, 521 P2d 679 (1974).

Strict Accountability: Degree of diligence required of payor bank attempting to come under "escape clause" provisions of 30-4-108(2) was greater than it would otherwise have been where bank had financed and refinanced drawers of checks and refinancing loans had not yet been completely repaid. Evidence that armored car which delivered checks to clearinghouse broke down on day checks were presented by payees and that clearinghouse's computer malfunctioned after checks were received by it the next day was insufficient excuse for bank's delay beyond "midnight deadline" and did not relieve it of liability for face amount of checks under the strict accountability rule imposed by this section where there was no testimony as to what happened on day after checks were received by bank. Sun River Cattle Co., Inc. v. Miners Bank of Mont., 164 M 237, 521 P2d 679 (1974).

30-4-303. When items subject to notice, stop order, legal process or setoff — order in which items may be charged or certified.

Official Comment

Source: Section 4-303, U.C.C.

Purposes:

1. The comments to Section 30-4-213 describe the process through which an item passes in the payor bank. Prior to this process or at any time while it is going on, the payor bank may receive knowledge or a legal notice affecting the item, such as knowledge or a notice that the drawer has filed a petition in bankruptcy or made an assignment for the benefit of creditors; may receive an order of the drawer stopping payment on the item; may have served on it an attachment of the account of the drawer; or the bank itself may exercise a right of setoff against the drawer's account. Each of these events affects the account of the drawer and may eliminate or freeze all or part of whatever balance is available to pay the item. Subsection (1) states the rule for determining the relative priorities between these various legal events and the item.

2. The rule is that if any one of several things has been done to the item or if it has reached any one of several stages in its processing at the time the knowledge, notice, stop-order or legal process is received or served and a reasonable time for the bank to act thereon expires or the setoff is exercised, the knowledge, notice, stop-order, legal process or setoff comes too late, the item has priority and a charge to the customer's account may be made and is effective. Certain of the tests determining the priority status of the item are the same as for final payment under Section 30-4-213(1), but additional tests apply in the context of the present section. The first event mentioned, namely, acceptance, means formal acceptance as that term is used and defined in Section 30-3-410. Certification is the type of certification defined in Section 30-3-411 [now repealed]. Payment of the item in cash under Section 30-4-213(1)(a), final settlement for the item under Section 30-4-213(1)(b) and completion of the process of posting under Section 30-4-213(1)(c) all constitute final payment of the item and confer priority. After a cash payment, final settlement or the completion of the process of posting, any knowledge, notice, stop-order, legal process or setoff comes too late and cannot interfere with either the payment of the item or a charge to the customer's account based upon such payment.

3. The sixth event conferring priority is stated by the language "or otherwise has evidenced by examination of such indicated account and by action its decision to pay the item." This general "omnibus" language is necessary to pick up other possible types of action impossible to specify particularly but where the bank has examined the account to see if there are sufficient funds and

has taken some action indicating an intention to pay. An example is what has sometimes been called "sight posting" where the bookkeeper examines the account and makes a decision to pay but postpones posting. The clause should be interpreted in the light of Nineteenth Ward Bank v. First Nat. Bank of South Weymouth, 184 Mass. 49, 67 N.E. 670 (1903). It is not intended to refer to various preliminary acts in no way close to a true decision of the bank to pay the item, such as receipt of the item over the counter for deposit, entry of a provisional credit in a passbook, or the making of a provisional settlement for the item through the clearing house, by entries in accounts, remittance or otherwise. All actions of this type are provisional and none of them evidences the bank's decision to pay the item. In this Section as in Section 30-4-213 reasoning such as appears in Cohen v. First Nat. Bank of Nogales, 22 Ariz. 394, 400, 198 P. 122, 124, 15 A.L.R. 701 (1921); Briviesca v. Coronado, 19 Cal.2d 244, 120 P.2d 649 (1941); White Brokerage Co. v. Cooperman, 207 Minn. 239, 290 N.W. 790 (1940); Scotts Bluff County v. First Nat. Bank of Gering, 115 Neb. 273, 212 N.W. 617, 618 (1927); Provident Savings Bank & Trust Co. v. Hildebrand, 49 Ohio App. 207, 196 N.E. 790, 791 (1934); Schaer v. First Nat. Bank of Brenham, 132 Tex. 499, 124 S.W.2d 108 (1939) (bill of exchange); Union State Bank of Lancaster v. People's State Bank of Lancaster, 192 Wis. 28, 33, 211 N.W. 931, 933 (1927); 1 Paton's Digest 1067, is rejected.

4. The seventh and last event conferring priority for an item and a charge to the customer's account based upon the item is stated by the language "become accountable for the amount of the item under subsection (1)(d) of Section 30-4-213 and Section 30-4-302 dealing with the payor bank's responsibility for late return of items". Under Section 30-4-213(1)(d) if a payor bank makes a provisional settlement for an item and fails to revoke the settlement in the time and manner permitted by statute, clearing house rule or agreement, such combination of events constitutes final payment of the item. Under Section 30-4-302 a payor bank may also become accountable for the amount of an item in certain other situations even though there has been no provisional settlement for the item or such action as constitutes final payment under Section 30-4-213(1). Expiration of the deadlines under Sections 30-4-213(1)(d) or 30-4-302 with resulting accountability by the payor bank for the amount of the item, establish priority of the item over notices, stop-orders, legal process or setoff.

5. In the case of knowledge, notice, stop-orders and legal process the effective time for determining whether they were received too late to affect the payment of an item and a charge to the customer's account by reason of such payment, is receipt plus a reasonable time for the bank to act on any of these communications. Usually a relatively short time is required to communicate to the bookkeeping department advice of one of these events but certainly some time is necessary. Compare Sections 30-1-201(27) and 30-4-403. In the case of setoff the effective time is when the setoff is actually made.

6. As between one item and another no priority rule is stated, other than the convenience of the bank. This rule is justified because of the impossibility of stating a rule that would be fair in all cases, having in mind the almost infinite number of combinations of large and small checks in relation to the available balance on hand in the drawer's account; the possible methods of receipt; and other difficulties. Further, where the drawer has drawn all the checks, he should have funds available to meet all of them and has no basis for urging one should be paid before another; and the holders have no direct right against the payor bank in any event, unless of course, the bank has accepted, certified or finally paid a particular item, or has become liable for it under Section 30-4-302. Under subsection (2) the bank obviously has the right to pay items for which it is itself liable ahead of those for which it is not.

Official Comment to 1991 Amendment:

1. Once a payor bank has accepted or certified an item or has paid the item in cash, the event has occurred that determines priorities between the item and the various legal events usually described as the "four legals." Subsection (1)(a) and (b) so provide.

2. In the usual case settlement for checks is by entries in bank accounts. Since the process-of-posting test has been abandoned as inappropriate for automated check collection, the determining event for priorities is a given hour on the day after the item is received. The hour may be fixed by the bank no earlier than one hour after the opening on the next banking day after the bank received the check and no later than the close of that banking day. If an item is received after the payor bank's regular Section 4-108 [30-4-107] cutoff hour, it is treated as received the next banking day. If a bank receives an item after its regular cutoff hour on Monday and an attachment is levied at noon on Tuesday, the attachment is prior to the item if the bank had not before that hour certified or paid. Under Section 4-301(1) [30-4-301(1)], the bank has until its midnight deadline on Wednesday to return a check if the attachment rendered the account insufficient to pay the item. The knowledge referred to in subsection (1) means knowledge of

the claims of third parties and not the payor bank's knowledge that the drawer's account is insufficient to pay the item.

Compiler's Comments

1991 Amendment: At end of (1), before "of the following", substituted "earliest" for "bank has done any"; in (1)(c), after "without", substituted "having" for "reserving" and after "settlement" deleted "and without having such right"; deleted former (1)(d) that read: "(d) completed the process of posting the item to the indicated account of the drawer, maker or other person to be charged therewith or otherwise has evidenced by examination of such indicated account and by action its decision to pay the item"; in middle of (1)(d), after "under", deleted "subsection (1)(d) of 30-4-213 and"; inserted (1)(e) concerning cutoff hour for checks; at end of (2) deleted "convenient to the bank"; and made minor changes in style.

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

Setoff at Time of Presentation of Writ of Execution: A judgment creditor claimed that because a bank took no action to exercise its right of setoff before a writ of execution was presented, the writ took precedence over the setoff. However, the bank acquired a right to setoff at the time payment became delinquent but chose instead to perform the setoff when presented with the writ. The judgment creditor had no greater right against the bank than did the debtor at that time, and because a judgment creditor seeking execution of a debtor's property in possession of a third party stands in the shoes of the debtor as far as the rights of the third party are concerned, the writ did not take precedence. Under these circumstances, this section did not apply. The bank properly asserted the setoff at the time the writ was presented. Victor Werlhof Aviation Ins. v. Farmers St. Bank, 237 M 51, 771 P2d 962, 46 St. Rep. 613 (1989).

Part 4
Relationship Between Payor Bank and Its Customer

30-4-401. When bank may charge customer's account.

Official Comment

Source: Section 4-401, U.C.C.

Purposes:

1. It is fundamental that upon proper payment of a draft the drawee may charge the account of the drawer. This is true even though the draft is an overdraft since the draft itself authorizes the payment for the drawer's account and carries an implied promise to reimburse the drawee.

2. Subsection (2) parallels the provision which protects a holder in due course against discharge by reason of alteration and permits him to enforce the instrument according to its original tenor. Section 30-3-407(3). It adopts the rule of cases extending the same protection to a drawee who pays in good faith. The subsection also follows the policy of Sections 30-3-115 and 30-3-407(3) by protecting the drawee who pays a completed instrument in good faith according to the instrument as completed.

Official Comment to 1991 Amendment:

1. An item is properly payable from a customer's account if the customer has authorized the payment and the payment does not violate any agreement that may exist between the bank and its customer. An item drawn for more than the amount of a customer's account may be properly payable. Thus under subsection (1) a bank may charge the customer's account for an item even though payment results in an overdraft. An item containing a forged drawer's signature or forged indorsement is not properly payable. Concern has arisen whether a bank is justified in asking a customer to execute a stop order when the customer notifies the bank of the loss of an unindorsed or specially indorsed check. Since such a check cannot be properly payable from the customer's account, it is inappropriate for a bank to require stop order authorization in such a case.

2. Subsection (2) adopts the view of case authority holding that if there is more than one customer who can draw on an account, the nonsigning customer is not liable for an overdraft unless that person benefits from the proceeds of the item.

3. Subsection (3) is added because the automated check collection system cannot accommodate postdated checks. A check is usually paid upon presentment without respect to the date of the check. Under the present law [prior to 1991 revision], if a payor bank pays a postdated check before its stated date, it cannot charge the customer's account under subsection (1) because the check was not "properly payable." Hence, the bank may be liable for wrongfully dishonoring subsequent checks of the drawer that would have been paid had the postdated check not been prematurely paid.

Compiler's Comments

1991 Amendment: Inserted second sentence of (1) concerning authorization by customer in accordance with agreement with bank; inserted (2) concerning nonliability for overdraft; inserted (3) concerning notice of postdating; in (4)(a) and (4)(b) substituted "terms" for "tenor"; and made minor changes in style.

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

"Properly Payable": A check that has not been properly endorsed is not "properly payable" within the meaning of this section. Eatinger v. First Nat'l Bank of Lewistown, 199 M 377, 649 P2d 1253, 39 St. Rep. 1465 (1982).

Drawer and Payee Identical — Circuitous Accountability: Checks were drawn on the account of Capital Preservation Fund, Inc., maintained with First National Bank of Great Falls, Montana, by John Bennett, an authorized signatory on the account. The checks were endorsed and deposited by Bennett in another account he maintained with the Ashford Bank of Houston, Texas. Ashford Bank sent the checks through normal banking channels and extended cash to Bennett in reliance on the checks. The checks, however, were dishonored by First National Bank. Ashford then charged back the account of Bennett but alleged that it sustained a loss of $500,000. An affidavit from the Federal Reserve Bank established that First National had timely returned the checks in advance of the "midnight deadline". Bennett contended that payment became final prior to dishonor because First National had completed the process of posting. Section 30-4-213 provides that "final" payment by a drawee bank is the point at which all "provisional" settlements as allowed by 30-4-104(1)(j) in the bank collection chain became "final" settlements. Typically, provisional credits given through a clearinghouse or mutual bank account are made final upon payment of the item by completion of the process of posting the drawer's account. The agency relationships established under 30-4-201 are thereby transformed into a series of debtor-creditor relationships ending with the depository bank indebted to its customer for the amount of the item. The right of a collecting bank under 30-4-212(1) to charge back the account of its customer for any credit given for an item terminates when payment on the item becomes final. Section 30-4-213 holds a "payor" bank accountable for an item once "final" payment has been rendered. The "payor" bank must act in a timely manner in either dishonoring or paying the instrument. Timely dishonor was established. Bennett in this instance had the roles of both a "drawer" and the "payee". To allow Bennett to allege that payment by First National, the "payor" bank, was final would result in circuitous accountability. First National would simply charge the account on which the checks were drawn, Capital Preservation Fund, Inc., in order to recoup the amount paid. Capital Preservation Fund, Inc., would in turn have a cause of action against Bennett for recovery of the money. Any litigation emanating from this unique factual situation properly was between Capital Preservation Fund, Inc., and Bennett. The cause of action against First National Bank was found to be illusory, and it was granted summary judgment. Ashford Bank v. Capital Preservation Fund, Inc., 544 F. Supp. 26, 39 St. Rep. 1385 (D.C. Mont. 1982).

30-4-402. Bank's liability to customer for wrongful dishonor — time of determining insufficiency of account.

Official Comment

Source: Section 4-402, U.C.C.

Purposes:

1. This section is new to the Uniform Laws, although similar statutory provisions are in existence in twenty-three jurisdictions.

2. The liability of the drawee for dishonor has sometimes been stated as one for breach of contract, sometimes as for negligence or other breach of a tort duty, and sometimes as for defamation. This section does not attempt to specify a theory. "Wrongful dishonor" excludes any permitted or justified dishonor, as where the drawer has no credit extended by the drawee, or where the draft lacks a necessary indorsement or is not properly presented.

3. This section rejects decisions which have held that where the dishonored item has been drawn by a merchant, trader or fiduciary he is defamed in his business, trade or profession by a reflection on his credit and hence that substantial damages may be awarded on the basis of defamation "per se" without proof that damage has occurred. The merchant, trader and fiduciary are placed on the same footing as any other drawer and in all cases of dishonor by mistake damages recoverable are limited to those actually proved.

4. Wrongful dishonor is different from "failure to exercise ordinary care in handling an item", and the measure of damages is that stated in this section, not that stated in Section 30-4-103(5).

5. The fourth sentence of the section rejects decisions holding that as a matter of law the dishonor of a check is not the "proximate cause" of the arrest and prosecution of the customer, and leaves to determination in each case as a question of fact whether the dishonor is or may be the "proximate cause".

Official Comment to 1991 Amendment:

1. Subsection (1) states positively what has been assumed under the present Act [prior to 1991 revision]: that if a bank fails to honor a properly payable item it may be liable to its customer for wrongful dishonor. Under subsection (2) the payor bank's wrongful dishonor of an item gives rise to a statutory cause of action. Damages may include consequential damages. Confusion has resulted from the attempts of courts to reconcile the first and second sentences of present Section 4-402 [30-4-402 prior to 1991 revision]. The second sentence implies that the bank is liable for some form of damages other than those proximately caused by the dishonor if the dishonor is other than by mistake. But nothing in the section describes what these noncompensatory damages might be. Some courts have held that in distinguishing between mistaken dishonors and nonmistaken dishonors, the so-called "trader" rule has been retained that allowed a "merchant or trader" to recover substantial damages for wrongful dishonor without proof of damages actually suffered. Comment 3 to present Section 4-402 [30-4-402 prior to 1991 revision] indicates that this was not the intent of the drafters. White & Summers, Uniform Commercial Code, Section 18-4 (1988), states: "The negative implication is that when wrongful dishonors occur not 'through mistake' but willfully, the court may impose damages greater than 'actual damages' ... . Certainly the reference to 'mistake' in the second sentence of 4-402 [30-4-402 prior to 1991 revision] invites a court to adopt the relevant pre-Code distinction." The proposed amendment deleting the reference to mistake in the second sentence precludes any inference that Section 4-402 [30-4-402] retains the "trader" rule. Whether a bank is liable for noncompensatory damages, such as punitive damages, must be decided by Section 1-103 [30-1-103] and Section 1-106 [30-1-106] ("by other rule of law").

2. Banks commonly determine whether there are sufficient funds in an account to pay an item after the close of banking hours on the day of presentment when they post debit and credit items to the account. The determination is made on the basis of credits available for withdrawal as of right or made available for withdrawal by the bank as an accommodation to its customer. When it is determined that payment of the item would overdraw the account, the item may be returned at any time before the bank's midnight deadline the following day. Before the item is returned new credits that are withdrawable as of right may have been added to the account. Subsection (3) eliminates uncertainty under the existing Code [prior to 1991 revision] as to whether the failure to make a second determination before the item is returned on the day following presentment is a wrongful dishonor when new credits were added to the account on that day that would have covered the amount of the check.

3. Section 4-402 [30-4-402] has been construed to preclude an action for wrongful dishonor by a plaintiff other than the bank's customer. Loucks v. Albuquerque National Bank, 418 P.2d 191 (N.Mex. 1966). Some courts have allowed a plaintiff other than the customer to sue when the customer is a business entity that is one and the same with the individual or individuals operating it. Murdaugh Volkswagen, Inc. v. First National Bank, 801 F.2d 719 (4th Cir. 1986) and Karsh v. American City Bank, 113 Cal.App.3d 419, 169 Cal.Rptr. 851 (1980). However, where the wrongful dishonor impugns the reputation of an operator of the business, the issue is not merely, as the court in Koger v. East First National Bank, 443 So.2d 141 (Fla.App. 1983), put it, one of a literal versus a liberal interpretation of Section 4-402 [30-4-402]. Rather the issue is whether the statutory cause of action in Section 4-402 [30-4-402] displaces, in accordance with Section 1-103 [30-1-103], any cause of action that existed at common law in a person who is not the customer whose reputation was damaged. *See* Marcum v. Security Trust and Savings Co., 221 Ala. 419, 129 So.74 (1930). While Section 4-402 [30-4-402] should not be interpreted to displace any such latter cause of action, the section itself gives no cause of action to other than a "customer", however that definition is construed, and thus confers no cause of action on the holder of a dishonored item. First American National Bank v. Commerce Union Bank, 692 S.W.2d 642 (Tenn.App. 1985).

Compiler's Comments

1991 Amendment: At end of catchline inserted "time of determining insufficiency of account"; inserted (1) concerning wrongful dishonor of item; in (2), at beginning of second sentence, deleted "When the dishonor occurs through mistake" and in second sentence, after "proved", deleted "If so proximately caused and proved damages"; inserted (3) concerning decision to dishonor based upon bank's determination of account balance; and made minor changes in style.

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

30-4-403. Customer's right to stop payment — burden of proof of loss.

Official Comment

Source: Section 4-403, U.C.C.

Purposes:

1. This section is new. It is intended to replace separate statutes in twenty-nine states which regulate stop-payment orders.

2. The position taken by this section is that stopping payment is a service which depositors expect and are entitled to receive from banks notwithstanding its difficulty, inconvenience and expense. The inevitable occasional losses through failure to stop should be borne by the banks as a cost of the business of banking.

3. Subsection (1) follows the decisions holding that a payee or indorsee has no right to stop payment. This is consistent with the provision governing payment or satisfaction. See Section 30-3-603. The sole exception to this rule is found in Section 30-4-405 on payment after notice of death, by which any person claiming an interest in the account can stop payment.

4. Payment is commonly stopped only on checks; but the right to stop payment is not limited to checks, and extends to any item payable by any bank. Where the maker of a note payable at a bank is in a position analogous to that of a drawer (Section 30-3-121 [now repealed]) he may stop payment of the note. By analogy the rule extends to drawees other than banks.

5. There is no right to stop payment after certification of a check or other acceptance of a draft, and this is true no matter who procures the certification. See Sections 30-3-411 [now repealed] and 30-4-303. The acceptance is the drawee's own engagement to pay, and he is not required to impair his credit by refusing payment for the convenience of the drawer.

6. Normally a direction to stop payment is first given by telephone. Notwithstanding statutes which require a written order, banks customarily accept such directions, and have been held to waive the writing. Subsection (2) is intended to protect both parties by making the oral direction effective for only a short time during which the drawer must confirm it in writing, and by eliminating thereafter any claim of waiver by acceptance of the oral direction.

7. The existing statutes all specify a time limit after which any direction to stop payment becomes ineffective unless it is renewed in writing; and the majority of them have specified six months. The purpose of the provision is, of course, to facilitate stopping payment by clearing the records of the drawee of accumulated unrevoked stop orders, as where the drawer has found a lost instrument or has settled his controversy with the payee, but has failed to notify the drawee. The last sentence of subsection (2), together with the second clause in Section 30-4-404, rejects the reasoning of such cases as Goldberg v. Manufacturers Trust Company, 199 Misc. 167, 102 N.Y.S.2d 144 (1951).

8. A payment in violation of an effective direction to stop payment is an improper payment, even though it is made by mistake or inadvertence. Any agreement to the contrary is invalid under Section 30-4-103(1) if in paying the item over the stop payment order the bank has failed to exercise ordinary care. The drawee is, however, entitled to subrogation to prevent unjust enrichment (Section 30-4-407); retains common-law defenses, e.g., that by conduct in recognizing the payment the customer has ratified the bank's action in paying over a stop payment order (Section 30-1-103); and retains common-law rights, e.g., to recover money paid under a mistake (Section 30-1-103) in cases where the payment is not made final by Section 30-3-418 [now repealed]. It has sometimes been said that payment cannot be stopped against a holder in due course, but the statement is inaccurate. The payment can be stopped but the drawer remains liable on the instrument to the holder in due course (Sections 30-3-305, 30-3-413) and the drawee, if he pays, becomes subrogated to the rights of the holder in due course against the drawer. Section 30-4-407. Any defenses available against a holder in due course remain available to the drawer, but other defenses are cut off to the same extent as if the holder himself were bringing the action.

Official Comment to 1991 Amendment:

1. The amendment makes clear that if there is more than one person authorized to draw on a customer's account any one of them can stop payment of any check drawn on the account or can order the account closed. Moreover, if there is a customer, such as a corporation, that requires its checks to bear the signatures of more than one person, any of these persons may stop payment on a check. In describing the item, the customer, in the absence of a contrary agreement, must meet the standard of what information allows the bank under the technology then existing to identify the item with reasonable certainty.

2. A stop order becomes effective when the order, whether written or oral, is first received by the bank. If the order is written it remains in effect for six months from that time. If the order is

oral it lapses after 14 days unless there is written confirmation. If there is written confirmation within the 14-day period, the six-month period dates from the giving of the oral order. A stop order may be renewed any number of times by notice given during a six-month period while a stop order is in effect. A new stop order may be given after a six-month period expires, but such a notice takes effect from the date given. When a stop order expires it is as though the order had never been given, and the payor bank may pay the item in good faith under Section 4-404 [30-4-404] even though a stop order had once been given.

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "(1) Subject to 27-1-717, a customer may by order to his bank stop payment of any item payable for his account but the order must be received at such time and in such manner as to afford the bank a reasonable opportunity to act on it prior to any action by the bank with respect to the item described in 30-4-303.

(2) An oral order is binding upon the bank only for 14 calendar days unless confirmed in writing within that period. A written order is effective for only 6 months unless renewed in writing.

(3) The burden of establishing the fact and amount of loss resulting from the payment of an item contrary to a binding stop payment order is on the customer."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

1985 Amendment: At beginning of (1) inserted "Subject to 27-1-717".

Montana Changes: The 1985 amendment inserted at beginning of subsection (1) "Subject to 27-1-717".

30-4-404. Bank not obligated to pay check more than 6 months old.

Official Comment

Source: Section 4-404, U.C.C.

Purposes:

This section incorporates a type of statute adopted in twenty-six jurisdictions. The time limit is set at six months because banking and commercial practice regards a check outstanding for longer than that period as stale, and a bank will normally not pay such a check without consulting the depositor. It is therefore not required to do so, but is given the option to pay because it may be in a position to know, as in the case of dividend checks, that the drawer wants payment made.

Certified checks are excluded from the section because they are the primary obligation of the certifying bank (Sections 30-3-411 [now repealed] and 30-3-413), which obligation runs direct to the holder of the check. The customer's account was charged when the check was certified.

30-4-405. Death or incompetence of customer.

Official Comment

Source: Section 4-405, U.C.C.

Purposes:

1. This section is new, although similar statutory provisions are in existence in seven states.

2. Subsection (1) follows existing decisions which hold that a drawee (payor) bank is not liable for the payment of a check before it has notice of the death or incompetence of the drawer. The justice and necessity of the rule are obvious. A check is an order to pay which the bank must obey under penalty of possible liability for dishonor. Further, with the tremendous volume of items handled any rule which required banks to verify the continued life and competency of drawers would be completely unworkable.

One or both of these same reasons apply to other phases of the bank collection and payment process and the rule is made wide enough to apply to these other phases. It applies to all kinds of "items"; to "customers" who own items as well as "customers" who draw or make them; to the function of collecting items as well as the function of accepting or paying them; to the carrying out of instructions to account for proceeds even though these may involve transfers to third parties; to depositary and intermediary banks as well as payor banks; and to incompetency existing at the time of the issuance of an item or the commencement of the collection or payment process as well as to incompetency occurring thereafter. Further, the requirement of actual knowledge makes inapplicable the rule of some cases that an adjudication of incompetency is constructive notice to all the world because obviously it is as impossible for banks to keep posted on such adjudications (in the absence of actual knowledge) as it is to keep posted as to death of immediate or remote customers.

3. Subsection (2) provides a limited period after death during which a bank may continue to pay checks (as distinguished from other items) even though it has notice. The purpose of the provision, as of the existing statutes, is to permit holders of checks drawn and issued shortly before death to cash them without the necessity of filing a claim in probate. The justification is that such checks normally are given in immediate payment of an obligation, that there is almost never any reason why they should not be paid, and that filing in probate is a useless formality, burdensome to the holder, the executor, the court and the bank.

This section does not prevent an executor or administrator from recovering the payment from the holder of the check. It is not intended to affect the validity of any gift causa mortis or other transfer in contemplation of death, but merely to relieve the bank of liability for the payment.

4. Any surviving relative, creditor or other person who claims an interest in the account may give a direction to the bank not to pay checks, or not to pay a particular check. Such notice has the same effect as a direction to stop payment. The bank has no responsibility to determine the validity of the claim or even whether it is "colorable". But obviously anyone who has an interest in the estate, including the person named as executor in a will, even if the will has not yet been admitted to probate, is entitled to claim an interest in the account.

30-4-406. Customer's duty to discover and report unauthorized signature or alteration.

Official Comment

Source: Section 4-406, U.C.C.

Purposes:

1. This section is new to Uniform Laws. It is to replace statutes in forty jurisdictions dealing with the general subject of a depositor's duty to discover and report forgeries and alterations. In these statutes there is substantial variation in rules prescribed as to the following matters: application of the statute to unauthorized signatures, raised checks or altered checks; inclusion of special provisions with respect to fictitious payees; periods of time prescribed for termination of right of customer to assert claims against bank; time when limitation period begins to run; restriction of rights of customer stated in terms of liability for loss, preclusion of rights or limitations on time in which suits may be brought.

2. Subsection (1) states the general duty of a customer to exercise reasonable care and promptness to examine his bank statements and items to discover his unauthorized signature or any alteration and to promptly notify the bank if he discovers an unauthorized signature or alteration. This duty becomes operative when the bank does any one of three things with respect to the statement of account and supporting items paid in good faith. The first action is the sending of the statement and items to the customer. The sending may be either by mailing or any other action within the definition of "send" (Section 30-1-201). The second action is the holding of such statement and items available for the customer pursuant to a request for instructions of the customer. The third action is stated as "or otherwise in a reasonable manner makes the statement and items available to the customer." Such wider residual language is desirable to cover unusual situations. An example might be where the bank knows a customer has left a former address but does not know any new address to which to send the statement or item or to obtain instructions from the customer. The third residual type of action, however, must be "reasonable" and any court has the power to determine that a particular action or practice of a bank, other than sending statements and items or holding them pursuant to instructions, is not reasonable.

3. Subsection (2) states the effect of a failure of a customer to comply with subsection (1). The first effect stated in subparagraph (a) is that he is precluded from asserting against the bank his unauthorized signature and alteration if the bank establishes that it suffered a loss by reason of the customer's failure. The bank has the burden of establishing that it suffered some loss.

Under subparagraph (b) if, after the first item and statement becomes available plus a reasonable period not exceeding fourteen calendar days, the bank pays in good faith any other item on which there is an unauthorized signature or alteration by the same wrongdoer, which payment is prior to receipt by the bank of notification of such unauthorized signature or alteration on the first item, the customer is precluded from asserting the additional unauthorized signature or alteration. This rule follows substantial case law that payment of an additional item or items bearing an unauthorized signature or alteration by the same wrongdoer is a loss suffered by the bank traceable to the customer's failure to exercise reasonable care in examining his statement and notifying the bank of objections to it. One of the most serious consequences of failure of the customer to comply with the requirements of subsection (1) is the opportunity presented to the wrongdoer to repeat his misdeeds. Conversely, one of the best ways to keep down losses in this type of situation is for the customer to promptly examine his statement and notify the bank of an unauthorized signature or alteration so that the bank will be alerted to stop paying further items. Hence, the rule of subparagraph (b) is prescribed and to avoid dispute a specific time limit for action by the customer is designated, namely fourteen calendar days.

4. The two effects on the customer of his failure to comply with subsection (1) (subparagraphs (a) and (b) of subsection (2)) are stated in terms of preclusion from asserting a claim against the bank. However, these two effects occur only if the customer has failed to exercise reasonable care and promptness in examining his statement and items and notifying the bank and as to this question of fact the burden is upon the bank to establish such failure. Further, even if the bank succeeds in establishing that the customer has failed to exercise ordinary care, if in turn the customer succeeds in establishing that the bank failed to exercise ordinary care in paying the item(s) the preclusion rule does not apply. This distribution of the burden of establishing between the customer and the bank provides reasonable equality of treatment and requires each person asserting the negligence to establish such negligence rather than requiring either person to establish that his entire course of conduct constituted ordinary care.

5. Whether the preclusion rule of subsection (2) operates or does not operate depends upon determinations as to ordinary care of the customer and possibly of the bank. However, subsection (4) places an absolute time limit on the right of a customer to make claim for payment of altered or forged paper without regard to care or lack of care of either the customer or the bank. In the case of alteration or the unauthorized signature of the customer himself the absolute time limit is one year. In the case of unauthorized indorsements it is three years. This recognizes that there is little excuse for a customer not detecting an alteration of his own check or a forgery of his own signature. However, he does not know the signatures of indorsers and may be delayed in learning that indorsements are forged. The three year absolute time limit on the discovery of forged indorsements should be ample, because in the great preponderance of cases the customer will learn of the forged indorsements within this time and if in any exceptional case he does not, the balance in favor of a mechanical termination of the liability of the bank outweighs what few residuary risks the customer may still have. In thirteen of the existing statutes there are limitations on the liability of a bank for payment of items bearing forged indorsements which limitation periods range from thirty days to two years. In the remaining twenty-seven no provision is made for forged indorsements.

6. Nothing in this section is intended to affect any decision holding that a customer who has notice of something wrong with an indorsement must exercise reasonable care to investigate and to notify the bank. It should be noted that under the rules relating to impostors and signatures in the name of the payee (Section 30-3-405) certain forged indorsements on which the bank has paid the item in good faith may be treated as effective notwithstanding such discovery and notice. If the alteration or forgery results from the drawer's negligence the drawee who pays in good faith is also protected. Section 30-3-406.

7. The forty existing statutes on the subject as well as Section 30-4-406 evidence a public policy in favor of imposing on customers the duty of prompt examination of their bank statements and the notification of banks of forgeries and alterations and in favor of reasonable time limitations on the responsibility of banks for payment of forged or altered items. In two New York cases, however, it has been held that a payor bank may waive defenses of the kind prescribed by the section and ignore the public policy indicated by these defenses and recover the full amount of a forged or altered item from a collecting bank. Fallick v. Amalgamated Bank of New York, 232 App. Div. 127, 249 N.Y.S. 238 (1st Dep't 1931); National Surety Corp. v. Federal Reserve Bank of New York, 188 Misc. 207, 70 N.Y.S.2d, 636 (1946), affirmed without opinion 188 Misc. 213, 70 N.Y.S.2d, 642 (1946). Subsection (5) is intended to reject the holding of these and like cases. Although the principle of subsection (5) might well be applied to other types of claims of customers against banks and defenses to these claims, the rule of the subsection is limited to defenses of a payor bank under this section. No present need is known to give the rule wider effect.

Official Comment to 1991 Amendment:

1. In order to impose on its customer the duty stated in subsection (3) to examine a statement or the returned items and report forgeries or alterations, the bank must comply with subsection (1) in sending or making available to the customer a statement of account. Whether the bank returns to the customer the items paid is a matter for bank-customer agreement. If the bank does not return the items paid, a general standard is stated that the customer must be given "information sufficient to allow the customer reasonably to identify the item." But a safe harbor rule is provided. If the item is described by item number, amount, and date of payment, the bank

does comply. This information was chosen because it can be obtained by the bank's computer without examination of the items involved. The other two items of information that the customer would normally want to know — the name of the payee and the date of the item — cannot be produced without adding substantially to the cost of producing the statement. A customer who keeps a record of items written will have sufficient information to identify the item on the basis of item number, amount and date of payment. But customers who don't keep records may not.

The safe harbor rule is important in determining the economic feasibility of payor or depositary bank check retention plans. If the name of the payee must be included on the customer's statement, the bank must employ people who will engage in the labor-intensive task of deciphering the names of payees on the checks paid and typing these names on the customer's statements. These costs will inhibit the growth of truncation plans.

2. Subsection (2) applies if the items are not returned to the customer. Check retention plans may include a simple payor bank check retention plan or the kind of check retention plan that would be authorized by a truncation agreement in which a collecting bank or the payee may retain the items. Even after agreeing to a check retention plan, a customer may need to see one or more checks for litigation or other purposes. The customer's request for the check may always be made to the payor bank. Under subsection (2) retaining banks may destroy items but must maintain the capacity to furnish legible copies for seven years. The practice of the present Code [prior to 1991 revision] of remaining silent on the right of banks to make charges for their services is followed. The assumption is that banks will differentiate their charges on the basis of whether the customer wishes the return of checks.

3. Subsection (3) imposes on the customer the duty to examine for and report unauthorized payments. Subsection (4) changes present subsection (2)(b) [subsection (2)(b) prior to 1991 revision] by making the 14-day period presumptively a reasonable period for the customer to examine and notify. The 14-day period may not be a reasonable period if the customer is temporarily out of the country or ill. Subsection (5) replaces present subsection (3) [subsection (3) prior to 1991 revision] and poses a modified comparative negligence test for determining liability. See the discussion on this point in the comments on Section 3-405 [30-3-420]. The term "good faith" is defined in Section 3-103(a)(4) [30-3-102(1)(d)] as including "observance of reasonable commercial standards of fair dealing." The connotation of this standard is fairness and not absence of negligence.

4. The term "ordinary care" used in proposed subsection (5) is defined in Section 3-103(a)(7) [30-3-102(1)(g)] to provide that sight examination by a payor bank is not required if its procedure is reasonable and is commonly followed by other comparable banks in the area. The case law is divided on this issue. The definition of "ordinary care" in Section 3-103 [30-3-102] rejects those authorities that hold, in effect, that failure to use sight examination is negligence as a matter of law.

5. Several changes are made in present Section 4-406(5) [30-4-406(5) prior to 1991 revision]. First, present subsection (5) [subsection (5) prior to 1991 revision] is deleted and its substance is made applicable only to the one-year notice preclusion in present subsection (4) [now subsection (6)]. Thus if a drawer has not notified the payor bank of a forged check or material alteration within the one-year period, the payor bank may not choose to recredit the drawer's account and pass the loss to the collecting banks on the theory of breach of warranty. Second, the reference in present subsection (4) [subsection (4) prior to 1991 revision] to unauthorized indorsements is deleted. Section 4-406 [30-4-406] imposes no duties on the drawer to look for forged indorsements. Proposed Section 4-111 [30-4-112] sets out a statute of limitations allowing a customer a three-year period to seek a credit to an account improperly charged by payment of an item bearing a forged indorsement. Third, subsection (3) is added to Section 4-304 [30-4-304] to assure that when a depositary bank is sued for breach of a presentment warranty, it can defend by showing that the drawer is precluded by Section 3-405 [30-3-420] or Section 4-406(3) and (4) [30-4-406(3) and (4)].

Compiler's Comments

1991 Amendment: Substituted current language (see 1991 Session Law for text) for former text that read: "(1) When a bank sends to its customer a statement of account accompanied by items paid in good faith in support of the debit entries or holds the statement and items pursuant to a request or instructions of its customer or otherwise in a reasonable manner makes the statement and items available to the customer, the customer must exercise reasonable care and promptness to examine the statement and items to discover his unauthorized signature or any alteration on an item and must notify the bank promptly after discovery thereof.

(2) If the bank establishes that the customer failed with respect to an item to comply with the duties imposed on the customer by subsection (1) the customer is precluded from asserting against the bank:

(a) his unauthorized signature or any alteration on the item if the bank also establishes that it suffered a loss by reason of such failure; and

(b) an unauthorized signature or alteration by the same wrongdoer on any other item paid in good faith by the bank after the first item and statement was available to the customer for a reasonable period not exceeding 14 calendar days and before the bank receives notification from the customer of any such unauthorized signature or alteration.

(3) The preclusion under subsection (2) does not apply if the customer establishes lack of ordinary care on the part of the bank in paying the item(s).

(4) Without regard to care or lack of care of either the customer or the bank a customer who does not within 1 year from the time the statement and items are made available to the customer (subsection (1)) discover and report his unauthorized signature or any alteration on the face or back of the item or does not within 3 years from that time discover and report any unauthorized endorsement is precluded from asserting against the bank such unauthorized signature or endorsement or such alteration.

(5) If under this section a payor bank has a valid defense against a claim of a customer upon or resulting from payment of an item and waives or fails upon request to assert the defense the bank may not assert against any collecting bank or other prior party presenting or transferring the item a claim based upon the unauthorized signature or alteration giving rise to the customer's claim."

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Case Notes

Commission of Bad Faith Tort Against Depositor by Bank: The District Court did not err in instructing the jury to consider recovery by bank depositor against the bank under bad faith tort principles and to accordingly consider punitive damages. The depositor and his nephew opened a checking account with a card requiring the signatures of both on checks. They then formed a partnership. The nephew induced the bank to change the card so that he could issue checks without the depositor's signature. The bank did not notify the depositor of the change or obtain his authorization for it. The bank told depositor his signature was not needed but did not tell him about the new card, and depositor disagreed. Later the bank told him it would not change its policy of honoring checks signed only by the nephew. When depositor's attorney told bank not to do so, the bank stated the card required only one signature and the bank would not change the card unless both the nephew and the depositor requested it. The bank then told depositor the card was lost but later that day produced both cards. Depositor sued, and the bank subsequently took various negative and detrimental actions against his credit status, refused loans of a type formerly granted, canceled his ready reserve account, and refused to pay several items presented before he was notified that the account had been canceled. Tribby v. NW. Bank of Great Falls, 217 M 196, 704 P2d 409, 42 St. Rep. 1133 (1985).

Instruction on Duty to Examine Bank Statement That Was Not Sent: Trial court properly refused defendant bank's offered jury instruction on the duty of plaintiff depositor to examine statements and report errors within a reasonable time because the statements were not sent to depositor and there was no question in the case as to his unauthorized signature or as to alterations. Tribby v. NW. Bank of Great Falls, 217 M 196, 704 P2d 409, 42 St. Rep. 1133 (1985).

Separate Suits Against Copartner and Bank — Settlement With One — No Release of Other: Bank depositor sued his bank and his partner in separate actions after the partner induced the bank to change a signature card requiring both partners' signatures so that defendant partner could make withdrawals on his signature alone. Depositor did not release his claim against the bank when he settled with his partner because: (1) the claims against the two were not based entirely on the same conduct; (2) assuming the two were joint tortfeasors, any release of one might specifically exclude the other; and (3) nothing in the record indicated either a release or nonrelease of the bank. Tribby v. NW. Bank of Great Falls, 217 M 196, 704 P2d 409, 42 St. Rep. 1133 (1985).

Suit for Wrongfully Honoring Checks — Relevance of Evidence and Claims: Plaintiff depositor's partner induced bank to disregard account signature card requiring signature of each partner on a check and to issue a card allowing the partner to make withdrawals on his signature alone. The partner did so, and the depositor sued the bank. The court should not have excluded bank's offered evidence that the partner told bank he had authority to change the card, testimony of the partner, a letter from partner to the bank on this point, and that portion of the partnership agreement authorizing the partner to write checks. However, the court properly refused to dismiss the complaint on the asserted ground that the partnership agreement authorized the bank's action, because a jury could find the bank unauthorized to act as it did. The court also properly refused to dismiss on the asserted ground that the cause of action was a partnership asset, because depositor could show it was not, particularly when the account was opened and the original signature card issued prior to the formation of the partnership. Tribby v. NW. Bank of Great Falls, 217 M 196, 704 P2d 409, 42 St. Rep. 1133 (1985).

30-4-407. Payor bank's right to subrogation on improper payment.

Official Comment

Source: Section 4-407, U.C.C.

Purposes:

1. Section 30-4-403 states that a stop payment order is binding on a bank. If a bank pays an item over such a stop order it is prima facie liable, but under subsection (3) of 30-4-403 the burden of establishing the fact and amount of loss from such payment is on the customer. A defense frequently interposed by a bank in an action against it for wrongful payment over a stop-order is that the drawer or maker suffered no loss because he would have been liable to a holder in due course in any event. On this argument some cases have held that payment cannot be stopped against a holder in due course. Payment can be stopped, but if it is, the drawer or maker is liable and the sound rule is that the bank is subrogated to the rights of the holder in due course. The preamble and subsection (a) of this section state this rule.

2. Subsection (b) also subrogates the bank to the rights of the payee or other holder against the drawer or maker either on the item or under the transaction out of which it arose. It may well be that the payee is not a holder in due course but still has good rights against the drawer. These may be on the check but also may not be as, for example, where the drawer buys goods from the payee and the goods are partially defective so that the payee is not entitled to the full price, but the goods are still worth a portion of the contract price. If the drawer retains the goods he is obligated to pay a part of the agreed price. If the bank has paid the check it should be subrogated to this claim of the payee against the drawer.

3. Subsection (c) subrogates the bank to the rights of the drawer or maker against the payee or other holder with respect to the transaction out of which the item arose. If, for example, the payee was a fraudulent salesman inducing the drawer to issue his check for defective securities, and the bank pays the check over a stop order but reimburses the drawer for such payment, the bank should have a basis for getting the money back from the fraudulent salesman.

4. The limitations of the preamble prevent the bank itself from getting any double recovery or benefits out of its subrogation rights conferred by the section.

5. The spelling out of the affirmative rights of the bank in this section does not destroy other existing rights (Section 30-1-103). Among others these may include the defense of a payor bank that by conduct in recognizing the payment a customer has ratified the bank's action in paying in disregard of a stop payment order or rights to recover money paid under a mistake.

Official Comment to 1991 Amendment:

The amendment conforms this section to the change in Section 4-403 [30-4-403] with reference to a closed account.

Compiler's Comments

1991 Amendment: In introductory clause, after "maker", inserted "after an account has been closed"; and made minor change in style.

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

Part 5
Collection of Documentary Drafts

30-4-501. Handling of documentary drafts — duty to send for presentment and to notify customer of dishonor.

Official Comment

[*Corresponding U.C.C. Section:* Section 4-501, U.C.C.]

Source: Section 4-501, U.C.C.

Purposes:

This section states the duty of a bank handling a documentary draft for a customer. "Documentary draft" is defined in Section 4-104 [30-4-104]. The duty stated exists even if the bank has bought the draft. This is because to the customer the draft normally represents an underlying commercial transaction, and if that is not going through as planned the customer should know it promptly. An electronic document of title may be presented through allowing access to the document or delivery of the document. Article 1, Section 1-201 [30-1-201] (definition of "delivery").

30-4-502. Presentment of "on arrival" drafts.

Official Comment

Source: Section 4-502, U.C.C.

Purposes:

The section is designed to establish a definite rule for "on arrival" drafts. The term includes not only drafts drawn payable "on arrival" but also drafts forwarded with instructions to present "on arrival". The term refers to the arrival of the relevant goods. Unless a bank has actual knowledge of the arrival of the goods, as for example, when it is the "notify" party on the bill of lading, the section only requires the exercise of such judgment in estimating time as a bank may be expected to have. Commonly the buyer-drawee will want the goods and will therefore call for the documents and take up the draft when they do arrive.

30-4-503. Responsibility of presenting bank for documents and goods — report of reasons for dishonor — referee in case of need.

Official Comment

[*Corresponding U.C.C. Section:* Section 4-503, U.C.C.]

Source: Section 4-503, U.C.C.

Prior Uniform Statutory Provision: Section 131(3), Uniform Negotiable Instruments Law.

Changes: Completely rewritten and enlarged.

Purposes:

1. This section states the rules governing, in the absence of instructions, the duty of the presenting bank in case either of honor or of dishonor of a documentary draft. The section should be read in connection with Section 2-514 [30-2-514] on when documents are deliverable on acceptance, when on payment. In the case of a dishonor of the draft, the bank, subject to Section 4-504 [30-4-504], must return possession or control of the documents to its principal.

2. If the draft is drawn under a letter of credit, Article 5 [Title 30, chapter 5] controls. See Sections 5-109 through 5-114 [30-5-129 through 30-5-134].

Compiler's Comments

1991 Amendment: Made minor changes in style.

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

30-4-504. Privilege of presenting bank to deal with goods — security interest for expenses.

Official Comment

Source: Section 4-504, U.C.C.

Purposes:

To give the presenting bank, after dishonor, a privilege to deal with the goods in any commercially reasonable manner pending instructions from its transferor and, if still unable to communicate with its principal after a reasonable time, a right to realize its expenditures as if foreclosing on an unpaid seller's lien (Section 30-2-706). The provision includes situations in which storage of goods or other action becomes commercially necessary pending receipt of any requested instructions, even if the requested instructions are later received.

The "reasonable manner" referred to means one reasonable in the light of business factors and the judgment of a business man.

CHAPTER 4A
UNIFORM COMMERCIAL CODE
FUNDS TRANSFERS

Chapter Official Comment

Official Comment:

Description of transaction covered by Article 4A [Title 30, chapter 4A].

There are a number of mechanisms for making payments through the banking system. Most of these mechanisms are covered in whole or part by state or federal statutes. In terms of number of transactions, payments made by check or credit card are the most common payment methods. Payment by check is covered by Articles 3 and 4 [Title 30, chapters 3 and 4] of the UCC and some aspects of payment by credit card are covered by federal law. In recent years electronic funds transfers have been increasingly common in consumer transactions. For example, in some cases a retail customer can pay for purchases by use of an access or debit card inserted in a terminal at the retail store that allows the bank account of the customer to be instantly debited. Some aspects of these point-of-sale transactions and other consumer payments that are effected electronically are covered by a federal statute, the Electronic Fund Transfer Act (EFTA). If any part of a funds transfer is covered by EFTA, the entire funds transfer is excluded from Article 4A [Title 30, chapter 4A].

Another type of payment, commonly referred to as a wholesale wire transfer, is the primary focus of Article 4A [Title 30, chapter 4A]. Payments that are covered by Article 4A [Title 30, chapter 4A] are overwhelmingly between business or financial institutions. The dollar volume of payments made by wire transfer far exceeds the dollar volume of payments made by other means. The volume of payments by wire transfer over the two principal wire payment systems—the Federal Reserve wire transfer network (Fedwire) and the New York Clearing House Interbank Payments Systems (CHIPS)—exceeds one trillion dollars per day. Most payments carried out by use of automated clearing houses are consumer payments covered by EFTA and therefore not covered by Article 4A [Title 30, chapter 4A]. There is, however, a significant volume of nonconsumer ACH payments that closely resemble wholesale wire transfers. These payments are also covered by Article 4A [Title 30, chapter 4A].

There is some resemblance between payments made by wire transfer and payments made by other means such as paper-based checks and credit cards or electronically-based consumer payments, but there are also many differences. Article 4A [Title 30, chapter 4A] excludes from its coverage these other payment mechanisms. Article 4A [Title 30, chapter 4A] follows a policy of treating the transaction that it covers—a "funds transfer"—as a unique method of payment that is governed by unique principles of law that address the operational and policy issues presented by this kind of payment.

The funds transfer that is covered by Article 4A [Title 30, chapter 4A] is not a complex transaction and can be illustrated by the following example which is used throughout the Prefatory Note as a basis for discussion. X, a debtor, wants to pay an obligation owed to Y. Instead of delivering to Y a negotiable instrument such as a check or some other writing such as a credit card slip that enables Y to obtain payment from a bank, X transmits an instruction to X's bank to credit a sum of money to the bank account of Y. In most cases X's bank and Y's bank are different banks. X's bank may carry out X's instruction by instructing Y's bank to credit Y's account in the amount that X requested. The instruction that X issues to its bank is a "payment order." X is the "sender" of the payment order and X's bank is the "receiving bank" with respect to X's order. Y is the "beneficiary" of X's order. When X's bank issues an instruction to Y's bank to carry out X's payment order, X's bank "executes" X's order. The instruction of X's bank to Y's bank is also a payment order. With respect to that order, X's bank is the sender, Y's bank is the receiving bank, and Y is the beneficiary. The entire series of transactions by which X pays Y is knows [sic] as the "funds transfer." With respect to the funds transfer, X is the "originator," X's bank is the "originator's bank," Y is the "beneficiary" and Y's bank is the "beneficiary's bank." In more complex transactions there are one or more additional banks known as "intermediary banks" between X's bank and Y's bank. In the funds transfer the instruction contained in the payment order of X to its bank is carried out by a series of payment orders by each bank in the transmission chain to the next bank in the chain until Y's bank receives a payment order to make the credit to Y's account. In most cases, the payment order of each bank to the next bank in the chain is transmitted electronically, and often the payment order of X to its bank is also transmitted electronically, but the means of transmission does not have any legal significance. A payment order may be transmitted by any means, and in some cases the payment order is transmitted by a slow means such as first class mail. To reflect this fact, the broader term "funds transfer" rather than the narrower term "wire transfer" is used in Article 4A [Title 30, chapter 4A] to describe the overall payment transaction.

Funds transfers are divided into two categories determined by whether the instruction to pay is given by the person making payment or the person receiving payment. If the instruction is given by the person making the payment, the transfer is commonly referred to as a "credit transfer." If the instruction is given by the person receiving payment, the transfer is commonly referred to as a "debit transfer." Article 4A [Title 30, chapter 4A] governs credit transfers and excludes debit transfers.

Why is Article 4A [Title 30, chapter 4A] needed?

There is no comprehensive body of law that defines the rights and obligations that arise from wire transfers. Some aspects of wire transfers are governed by rules of the principal transfer systems. Transfers made by Fedwire are governed by Federal Reserve Regulation J and transfers over CHIPS are governed by the CHIPS rules. Transfers made by means of automated clearing houses are governed by uniform rules adopted by various associations of banks in various parts of the nation or by Federal Reserve rules or operating circulars. But the various funds transfer system rules apply to only limited aspects of wire transfer transactions. The resolution of the many issues that are not covered by funds transfer system rules depends on contracts of the parties, to the extent that they exist, or principles of law applicable to other payment mechanisms that might be applied by analogy. The result is a great deal of uncertainty. There is no consensus about the juridical nature of a wire transfer and consequently of the rights and obligations that are created. Article 4A [Title 30, chapter 4A] is intended to provide the comprehensive body of law that we do not have today.

Characteristics of a funds transfer.

There [are] a number of characteristics of funds transfers covered by Article 4A [Title 30, chapter 4A] that have influenced the drafting of the statute. The typical funds transfer involves a large amount of money. Multimillion dollar transactions are commonplace. The originator of the transfer and the beneficiary are typically sophisticated business or financial organizations. High speed is another predominant characteristic. Most funds transfers are completed on the same day, even in complex transactions in which there are several intermediary banks in the transmission chain. A funds transfer is a highly efficient substitute for payments made by the delivery of paper instruments. Another characteristic is extremely low cost. A transfer that involves many millions of dollars can be made for a price of a few dollars. Price does not normally vary very much or at all with the amount of the transfer. This system of pricing may not be feasible if the bank is exposed to very large liabilities in connection with the transaction. The pricing system assumes that the price reflects primarily the cost of the mechanical operation performed by the bank, but in fact, a bank may have more or less potential liability with respect to a funds transfer depending upon the amount of the transfer. Risk of loss to banks carrying out a funds transfer may arise from a variety of causes. In some funds transfers, there may be extensions of very large amounts of credit for short periods of time by the banks that carry out a funds transfer. If a payment order is issued to the beneficiary's bank, it is normal for the bank to release funds to the beneficiary immediately. Sometimes, payment to the beneficary's [sic] bank by the bank that issued the order to the beneficiary's bank is delayed until the end of the day. If that payment is not received because of the insolvency of the bank that is obliged to pay, the beneficiary's bank may suffer a loss. There is also risk of loss if a bank fails to execute the payment order of a customer, or if the order is executed late. There also may be an error in the payment order issued by a bank that is executing the payment order of its customer. For example, the error might relate to the amount to be paid or to the identity of the person to be paid. Because the dollar amounts involved in funds transfers are so large, the risk of loss if something goes wrong in a transaction may also be very large. A major policy issue in the drafting of Article 4A [Title 30, chapter 4A] is that of determining how risk of loss is to be allocated given the price structure in the industry.

Concept of acceptance and effect of acceptance by the beneficiary's bank.

Rights and obligations under Article 4A [Title 30, chapter 4A] arise as the result of "acceptance" of a payment order by the bank to which the order is addressed. Section 4A-209 [30-4A-209]. The effect of acceptance varies depending upon whether the payment order is issued to the beneficiary's bank or to a bank other than the beneficiary's bank. Acceptance by the beneficiary's bank is particularly important because it defines when the beneficiary's bank becomes obligated to the beneficiary to pay the amount of the payment order. Although Article 4A [Title 30, chapter 4A] follows convention in using the term "funds transfer" to identify the payment from X to Y that is described above, no money or property right of X is actually transferred to Y. X pays Y by causing Y's bank to become indebted to Y in the amount of the payment. This debt arises when Y's bank accepts the payment order that X's bank issued to Y's bank to execute X's order. If the funds transfer was carried out by use of one or more intermediary banks between X's bank and Y's bank, Y's bank becomes indebted to Y when Y's bank accepts the payment order issued to it by an intermediary bank. The funds transfer is completed when this debt is incurred. Acceptance, the event that determines when the debt of Y's bank to Y arises, occurs (i) when Y's bank pays Y or notifies Y of receipt of the payment order, or (ii) when Y's bank receives payment from the bank that issued a payment order to Y's bank.

The only obligation of the beneficiary's bank that results from acceptance of a payment order is to pay the amount of the order to the beneficiary. No obligation is owed to either the sender of the payment order accepted by the beneficiary's bank or to the originator of the funds transfer. The obligation created by acceptance by the beneficiary's bank is for the benefit of the beneficiary. The purpose of the sender's payment order is to effect payment by the originator to the beneficiary and that purpose is achieved when the beneficiary's bank accepts the payment order. Section

4A-405 [30-4A-405] states rules for determining when the obligation of the beneficiary's bank to the beneficiary has been paid.

Acceptance by a bank other than the beneficiary's bank.

In the funds transfer described above, what is the obligation of X's bank when it receives X's payment order? Funds transfers by a bank on behalf of its customer are made pursuant to an agreement or arrangement that may or may not be reduced to a formal document signed by the parties. It is probably true that in most cases there is either no express agreement or the agreement addresses only some aspects of the transaction. Substantial risk is involved in funds transfers and a bank may not be willing to give this service to all customers, and may not be willing to offer it to any customer unless certain safeguards against loss such as security procedures are in effect. Funds transfers often involve the giving of credit by the receiving bank to the customer, and that also may involve an agreement. These considerations are reflected in Article 4A [Title 30, chapter 4A] by the principle that, in the absence of a contrary agreement, a receiving bank does not incur liability with respect to a payment order until it accepts it. If X and X's bank in the hypothetical case had an agreement that obliged the bank to act on X's payment orders and the bank failed to comply with the agreement, the bank can be held liable for breach of the agreement. But apart from any obligation arising by agreement, the bank does not incur any liability with respect to X's payment order until the bank accepts the order. X's payment order is treated by Article 4A [Title 30, chapter 4A] as a request by X to the bank to take action that will cause X's payment order to be carried out. That request can be accepted by X's bank by "executing" X's payment order. Execution occurs when X's bank sends a payment order to Y's bank intended by X's bank to carry out the payment order of X. X's bank could also execute X's payment order by issuing a payment order to an intermediary bank instructing the intermediary bank to instruct Y's bank to make the credit to Y's account. In that case execution and acceptance of X's order occur when the payment order of X's bank is sent to the intermediary bank. When X's bank executes X's payment order the bank is entitled to receive payment from X and may debit an authorized account of X. If X's bank does not execute X's order and the amount of the order is covered by a withdrawable credit balance in X's authorized account, the bank must pay X interest on the money represented by X's order unless X is given prompt notice of rejection of the order. Section 4A-210(b) [30-4A-210(2)].

Bank error in funds transfers.

If a bank, other than the beneficiary's bank, accepts a payment order, the obligations and liabilities are owed to the originator of the funds transfer. Assume in the example stated above, that X's bank executes X's payment order by issuing a payment order to an intermediary bank that executes the order of X's bank by issuing a payment order to Y's bank. The obligations of X's bank with respect to execution are owed to X. The obligations of the intermediary bank with respect to execution are also owed to X. Section 4A-302 [30-4A-302] states standards with respect to the time and manner of execution of payment orders. Section 4A-305 [30-4A-305] states the measure of damages for improper execution. It also states that a receiving bank is liable for damages if it fails to execute a payment order that it was obliged by express agreement to execute. In each case consequential damages are not recoverable unless an express agreement of the receiving bank provides for them. The policy basis for this limitation is discussed in Comment 2 to Section 4A-305 [30-4A-305].

Error in the consummation of a funds transfer is not uncommon. There may be a discrepancy in the amount that the originator orders to be paid to the beneficiary and the amount that the beneficiary's bank is ordered to pay. For example, if the originator's payment order instructs payment of $100,000 and the payment order of the originator's bank instructs payment of $1,000,000, the originator's bank is entitled to receive only $100,000 from the originator and has the burden of recovering the additional $900,000 paid to the beneficiary by mistake. In some cases the originator's bank or an intermediary bank instructs payment to a beneficiary other than the beneficiary stated in the originator's payment order. If the wrong beneficiary is paid the bank that issued the erroneous payment order is not entitled to receive payment of the payment order that it executed and has the burden of recovering the mistaken payment. The originator is not obliged to pay its payment order. Section 4A-303 [30-4A-303] and Section 4A-207 [30-4A-207] state rules for determining the rights and obligations of the various parties to the funds transfer in these cases and in other typical cases in which error is made.

Pursuant to Section 4A-402(c) [30-4A-402(3)] the originator is excused from the obligation to pay the originator's bank if the funds transfer is not completed, i.e. payment by the originator to the beneficiary is not made. Payment by the originator to the beneficiary occurs when the beneficiary's bank accepts a payment order for the benefit of the beneficiary of the originator's payment order. Section 4A-406 [30-4A-406]. If for any reason that acceptance does not occur, the originator is not required to pay the payment order that it issued or, if it already paid, is entitled to refund of the payment with interest. This "money-back guarantee" is an important protection of the originator of a funds transfer. The same rule applies to any other sender in the funds transfer. Each sender's obligation to pay is excused if the beneficiary's bank does not accept a payment order for the benefit of the beneficiary of that sender's order. There is an important exception to this rule. It is common practice for the originator of a funds transfer to designate the intermediary bank or banks through which the funds transfer is to be routed. The originator's bank is required by Section 4A-302 [30-4A-302] to follow the instruction of the originator with respect to intermediary banks. If the originator's bank sends a payment order to the intermediary bank designated in the originator's order and the intermediary bank causes the funds transfer to miscarry by failing to execute the payment order or by instructing payment to the wrong beneficiary, the originator's bank is not required to pay its payment order and if it has already paid it is entitled to recover payment from the intermediary bank. This remedy is normally adequate, but if the originator's bank already paid its order and the intermediary bank has suspended payments or is not permitted by law to refund payment, the originator's bank will suffer a loss. Since the originator required the originator's bank to use the failed intermediary bank, Section 4A-402(e) [30-4A-402(5)] provides that in this case the originator is obliged to pay its payment order and has a claim against the intermediary bank for the amount of the order. The same principle applies to any other sender that designates a subsequent intermediary bank.

Unauthorized payment orders.

An important issue addressed in Section 4A-202 [30-4A-202] and Section 4A-203 [30-4A-203] is how the risk of loss from unauthorized payment orders is to be allocated. In a large percentage of cases, the payment order of the originator of the funds transfer is transmitted electronically to the originator's bank. In these cases it may not be possible for the bank to know whether the electronic message has been authorized by its customer. To ensure that no unauthorized person is transmitting messages to the bank, the normal practice is to establish security procedures that usually involve the use of codes or identifying numbers or words. If the bank accepts a payment order that purports to be that of its customer after verifying its authenticity by complying with a security procedure agreed to by the customer and the bank, the customer is bound to pay the order even if it was not authorized. But there is an important limitation on this rule. The bank is entitled to payment in the case of an unauthorized order only if the court finds that the security procedure was a commercially reasonable method of providing security against unauthorized payment orders. The customer can also avoid liability if it can prove that the unauthorized order was not initiated by an employee or other agent of the customer having access to confidential security information or by a person who obtained that information from a source controlled by the customer. The policy issues are discussed in the comments following Section 4A-203 [30-4A-203]. If the bank accepts an unauthorized payment order without verifying it in compliance with a security procedure, the loss falls on the bank.

Security procedures are also important in cases of error in the transmission of payment orders. There may be an error by the sender in the amount of the order, or a sender may transmit a payment order and then erroneously transmit a duplicate of the order. Normally, the sender is bound by the payment order even if it is issued by mistake. But in some cases an error of this kind can be detected by a security procedure. Although the receiving bank is not obliged to provide a security procedure for the detection of error, if such a procedure is agreed to by the bank Section 4A-205 [30-4A-205] provides that if the error is not detected because the receiving bank does not comply with the procedure, any resulting loss is borne by the bank failing to comply with the security procedure.

Insolvency losses.

Some payment orders do not involve the granting of credit to the sender by the receiving bank. In those cases, the receiving bank accepts the sender's oirder [sic] at the same time the bank receives payment of the order. This is true of a transfer of funds by Fedwire or of cases in which the receiving bank can debit a funded account of the sender. But in some cases the granting of credit is the norm. This is true of a payment order over CHIPS. In a CHIPS transaction the receiving bank usually will accept the order before receiving payment from the sending bank. Payment is delayed until the end of the day when settlement is made through the Federal Reserve System. If the receiving bank is an intermediary bank, it will accept by issuing a payment order to another bank and the intermediary bank is obliged to pay that payment order. If the receiving bank is the beneficiary's bank, the bank usually will accept by releasing funds to the beneficiary before the bank has received payment. If a sending bank suspends payments before settling its liabilities at the end of the day, the financial stability of banks that are net creditors of the insolvent bank may also be put into jeopardy, because the dollar volume of funds transfers between the banks may be extremely large. With respect to two banks that are dealing with each other in a series of transactions in which each bank is sometimes a receiving bank and sometimes a sender, the risk of insolvency can be managed if amounts payable as a sender and amounts receivable as a receiving bank are roughly equal. But if these amounts are significantly out of balance, a net creditor bank may have a very significant credit risk during the day before settlement occurs. The Federal Reserve System and the banking community are greatly concerned with this risk, and various measures have been instituted to reduce this credit exposure. Article 4A [Title 30, chapter 4A] also addresses this problem. A receiving bank can always avoid this risk by delaying acceptance of a payment order until after the bank has received payment. For example, if the beneficiary's bank credits the beneficiary's account it can avoid acceptance by not notifying the beneficiary of the receipt of the order or by notifying the beneficiary that the credit may not be withdrawn until the beneficiary's bank receives payment. But if the beneficiary's bank releases funds to the beneficiary before receiving settlement, the result in a funds transfer other than a transfer by means of an automated clearing house or similar provisional settlement system is that the beneficiary's bank may not recover the funds if it fails to receive settlement. This rule encourages the banking system to impose credit limitations on banks that issue payment orders. These limitations are already in effect. CHIPS has also proposed a loss-sharing plan to be adopted for implementation in the second half of 1990 under which CHIPS participants will be required to provide funds necessary to complete settlement of the obligations of one or more participants that are unable to meet settlement obligations. Under this plan, it will be a virtual certainty that there will be settlement on CHIPS in the event of failure by a single bank. Section 4A-403(b) and (c) [30-4A-403(2) and (3)] are also addressed to reducing risks of insolvency. Under these provisions the amount owed by a failed bank with respect to payment orders it issued is the net amount owing after setting off amounts owed to the failed bank with respect to payment orders it received. This rule allows credit exposure to be managed by limitations on the net debit position of a bank.

Chapter Compiler's Comments

Saving Clause: Section 232, Ch. 410, L. 1991, was a saving clause.

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Part 1
Subject Matter and Definitions

30-4A-102. Subject matter.

Official Comment

Source: Section 4A-102, U.C.C.

Official Comment:

Article 4A [Title 30, chapter 4A] governs a specialized method of payment referred to in the Article as a funds transfer but also commonly referred to in the commercial community as a wholesale wire transfer. A funds transfer is made by means of one or more payment orders. The scope of Article 4A [Title 30, chapter 4A] is determined by the definitions of "payment order" and "funds transfer" found in Section 4A-103 [30-4A-103] and Section 4A-104 [30-4A-104].

The funds transfer governed by Article 4A [Title 30, chapter 4A] is in large part a product of recent and developing technological changes. Before this Article was drafted there was no comprehensive body of law—statutory or judicial—that defined the juridical nature of a funds transfer or the rights and obligations flowing from payment orders. Judicial authority with respect to funds transfers is sparse, undeveloped and not uniform. Judges have had to resolve disputes by referring to general principles of common law or equity, or they have sought guidance in statutes such as Article 4 [Title 30, chapter 4] which are applicable to other payment methods. But attempts to define rights and obligations in funds transfers by general principles or by analogy to rights and obligations in negotiable instrument law or the law of check collection have not been satisfactory.

In the drafting of Article 4A [Title 30, chapter 4A], a deliberate decision was made to write on a clean slate and to treat a funds transfer as a unique method of payment to be governed by unique rules that address the particular issues raised by this method of payment. A deliberate decision was also made to use precise and detailed rules to assign responsibility, define behavioral norms, allocate risks and establish limits on liability, rather than to rely on broadly stated, flexible principles. In the drafting of these rules, a critical consideration was that the various parties to funds transfers need to be able to predict risk with certainty, to insure against risk, to adjust operational and security procedures, and to price funds transfer services appropriately. This consideration is particularly important given the very large amounts of money that are involved in funds transfers.

Funds transfers involve competing interests—those of the banks that provide funds transfer services and the commercial and financial organizations that use the services, as well as the public interest. These competing interests were represented in the drafting process and they were thoroughly considered. The rules that emerged represent a careful and delicate balancing of those interests and are intended to be the exclusive means of determining the rights, duties and liabilities of the affected parties in any situation covered by particular provisions of the Article. Consequently, resort to principles of law or equity outside of Article 4A [Title 30, chapter 4A] is not appropriate to create rights, duties and liabilities inconsistent with those stated in this Article.

30-4A-103. Payment order — definitions.

Official Comment

Source: Section 4A-103, U.C.C.

Official Comment:

This section is discussed in the Comment following Section 4A-104 [30-4A-104].

30-4A-104. Funds transfer — definitions.

Official Comment

Source: Section 4A-104, U.C.C.

Official Comment:

1. Article 4A [Title 30, chapter 4A] governs a method of payment in which the person making payment (the "originator") directly transmits an instruction to a bank either to make payment to the person receiving payment (the "beneficiary") or to instruct some other bank to make payment to the beneficiary. The payment from the originator to the beneficiary occurs when the bank that is to pay the beneficiary becomes obligated to pay the beneficiary. There are two basic definitions: "Payment order" stated in Section 4A-103 [30-4A-103] and "Funds transfer" stated in Section 4A-104 [30-4A-104]. These definitions, other related definitions, and the scope of Article 4A [Title 30, chapter 4A] can best be understood in the context of specific fact situations. Consider the following cases:

Case #1. X, which has an account in Bank A, instructs that bank to pay $1,000,000 to Y's account in Bank A. Bank A carries out X's instruction by making a credit of $1,000,000 to Y's account and notifying Y that the credit is available for immediate withdrawal. The instruction by X to Bank A is a "payment order" which was issued when it was sent to Bank A. Section 4A-103(a)(1) and (c) [30-4A-103(1)(a) and (3)]. X is the "sender" of the payment order and Bank A is the "receiving bank." Section 4A-103(a)(5) and (a)(4) [30-4A-103(1)(e) and (1)(d)]. Y is the "beneficiary" of the payment order and Bank A is the "beneficiary's bank." Section 4A-103(a)(2) and (a)(3) [30-4A-103(1)(b) and (1)(c)]. When Bank A notified Y of receipt of the payment order, Bank A "accepted" the payment order. Section 4A-209(b)(1) [30-4A-209(2)(a)]. When Bank A accepted the order it incurred an obligation to Y to pay the amount of the order. Section 4A-404(a) [30-4A-404(1)]. When Bank A accepted X's order, X incurred an obligation to pay Bank A the amount of the order. Section 4A-402(b) [30-4A-402(2)]. Payment from X to Bank A would normally be made by a debit to X's account in Bank A. Section 4A-403(a)(3) [30-4A-403(1)(c)]. At the time Bank A incurred the obligation to pay Y, payment of $1,000,000 by X to Y was also made. Section 4A-406(a) [30-4A-406(1)]. Bank A paid Y when it gave notice to Y of a withdrawable credit of $1,000,000 to Y's account. Section 4A-405(a) [30-4A-405(1)]. The overall transaction, which comprises the acts of X and Bank A, in which the payment by X to Y is accomplished is referred to as the "funds transfer." Section 4A-104(a) [30-4A-104(1)]. In this case only one payment order was involved in the funds transfer. A one-payment-order funds transfer is usually referred to as a "book transfer" because the payment is accomplished by the receiving bank's debiting the account of the sender and crediting the account of the beneficiary in the same bank. X, in addition to being the sender of the payment order to Bank A, is the "originator" of the funds transfer. Section 4A-104(c) [30-4A-104(3)]. Bank A is the "originator's bank" in the funds transfer as well as the beneficiary's bank. Section 4A-104(d) [30-4A-104(4)].

Case #2. Assume the same facts as in Case #1 except that X instructs Bank A to pay $1,000,000 to Y's account in Bank B. With respect to this payment order, X is the sender, Y is the beneficiary, and Bank A is the receiving bank. Bank A carries out X's order by instructing Bank B to pay $1,000,000 to Y's account. This instruction is a payment order in which Bank A is the sender, Bank B is the receiving bank, and Y is the beneficiary. When Bank A issued its payment order to Bank B, Bank A "executed" X's order. Section 4A-301(a) [30-4A-301(1)]. In the funds transfer, X is the originator, Bank A is the originator's bank, and Bank B is the beneficiary's bank. When Bank A executed X's order, X incurred an obligation to pay Bank A the amount of the order. Section 4A-402(c) [30-4A-402(3)]. When Bank B accepts the payment order issued to it by Bank A, Bank B incurs an obligation to Y to pay the amount of the order (Section 4A-404(a) [30-4A-404(1)]) and Bank A incurs an obligation to pay Bank B. Section 4A-402(b) [30-4A-402(2)]. Acceptance by Bank B also results in payment of $1,000,000 by X to Y. Section 4A-406(a) [30-4A-406(1)]. In this case two payment orders are involved in the funds transfer.

Case #3. Assume the same facts as in Case #2 except that Bank A does not execute X's payment order by issuing a payment order to Bank B. One bank will not normally act to carry out a funds transfer for another bank unless there is a preexisting arrangement between the banks for transmittal of payment orders and settlement of accounts. For example, if Bank B is a foreign bank with which Bank A has no relationship, Bank A can utilize a bank that is a correspondent of both Bank A and Bank B. Assume Bank A issues a payment order to Bank C to pay $1,000,000 to Y's account in Bank B. With respect to this order, Bank A is the sender, Bank C is the receiving bank, and Y is the beneficiary. Bank C will execute the payment order of Bank A by issuing a payment order to Bank B to pay $1,000,000 to Y's account in Bank B. With respect to Bank C's payment order, Bank C is the sender, Bank B is the receiving bank, and Y is the beneficiary. Payment of $1,000,000 by X to Y occurs when Bank B accepts the payment order issued to it by Bank C. In this case the funds transfer involves three payment orders. In the funds transfer, X is the originator, Bank A is the originator's bank, Bank B is the beneficiary's bank, and Bank C is an "intermediary bank." Section 4A-104(b) [30-4A-104(2)]. In some cases there may be more than one intermediary bank, and in those cases each intermediary bank is treated like Bank C in Case #3.

As the three cases demonstrate, a payment under Article 4A [Title 30, chapter 4A] involves an overall transaction, the funds transfer, in which the originator, X, is making payment to the beneficiary, Y, but the funds transfer may encompass a series of payment orders that are issued in order to effect the payment initiated by the originator's payment order.

In some cases the originator and the beneficiary may be the same person. This will occur, for example, when a corporation orders a bank to transfer funds from an account of the corporation in that bank to another account of the corporation in that bank or in some other bank. In some funds transfers the first bank to issue a payment order is a bank that is executing a payment order of a customer that is not a bank. In this case the customer is the originator. In other cases, the first bank to issue a payment order is not acting for a customer, but is making a payment for its own account. In that event the first bank to issue a payment order is the originator as well as the originator's bank.

2. "Payment order" is defined in Section 4A-103(a)(1) [30-4A-103(1)(a)] as an instruction to a bank to pay, or to cause another bank to pay, a fixed or determinable amount of money. The bank to which the instruction is addressed is known as the "receiving bank." Section 4A-103(a)(4) [30-4A-103(1)(d)]. "Bank" is defined in Section 4A-105(a)(2) [30-4A-105(1)(b)]. The effect of this definition is to limit Article 4A [Title 30, chapter 4A] to payments made through the banking system. A transfer of funds made by an entity outside the banking system is excluded. A transfer of funds through an entity other than a bank is usually a consumer transaction involving relatively small amounts of money and a single contract carried out by transfers of cash or a cash equivalent such as a check. Typically, the transferor delivers cash or a check to the company making the transfer, which agrees to pay a like amount to a person designated by the transferor. Transactions covered by Article 4A [Title 30, chapter 4A] typically involve very large amounts of money in which several transactions involving several banks may be necessary to carry out the payment. Payments are normally made by debits or credits to bank accounts. Originators and beneficiaries are almost always business organizations and the transfers are usually made to pay obligations. Moreover, these transactions are frequently done on the basis of very short-term credit granted by the receiving bank to the sender of the payment order. Wholesale wire transfers involve policy questions that are distinct from those involved in consumer-based transactions by nonbanks.

3. Further limitations on the scope of Article 4A [Title 30, chapter 4A] are found in the three requirements found in subparagraphs (i), (ii), and (iii) of Section 4A-103(a)(1) [30-4A-103(1)(a)(i) through (1)(a)(iii)]. Subparagraph (i) [30-4A-103(1)(a)(i)] states that the instruction to pay is a

payment order only if it "does not state a condition to payment to the beneficiary other than time of payment." An instruction to pay a beneficiary sometimes is subject to a requirement that the beneficiary perform some act such as delivery of documents. For example, a New York bank may have issued a letter of credit in favor of X, a California seller of goods to be shipped to the New York bank's customer in New York. The terms of the letter of credit provide for payment to X if documents are presented to prove shipment of the goods. Instead of providing for presentment of the documents to the New York bank, the letter of credit states that they may be presented to a California bank that acts as an agent for payment. The New York bank sends an instruction to the California bank to pay X upon presentation of the required documents. The instruction is not covered by Article 4A [Title 30, chapter 4A] because payment to the beneficiary is conditional upon receipt of shipping documents. The function of banks in a funds transfer under Article 4A [Title 30, chapter 4A] is comparable to the role of banks in the collection and payment of checks in that it is essentially mechanical in nature. The low price and high speed that characterize funds transfers reflect this fact. Conditions to payment by the California bank other than time of payment impose responsibilities on that bank that go beyond those in Article 4A [Title 30, chapter 4A] funds transfers. Although the payment by the New York bank to X under the letter of credit is not covered by Article 4A [Title 30, chapter 4A], if X is paid by the California bank, payment of the obligation of the New York bank to reimburse the California bank could be made by an Article 4A [Title 30, chapter 4A] funds transfer. In such a case there is a distinction between the payment by the New York bank to X under the letter of credit and the payment by the New York bank to the California bank. For example, if the New York bank pays its reimbursement obligation to the California bank by a Fedwire naming the California bank as beneficiary (see Comment 1 to Section 4A-107 [30-4A-107]), payment is made to the California bank rather than to X. That payment is governed by Article 4A [Title 30, chapter 4A] and it could be made either before or after payment by the California bank to X. The payment by the New York bank to X under the letter of credit is not governed by Article 4A [Title 30, chapter 4A] and it occurs when the California bank, as agent of the New York bank, pays X. No payment order was involved in that transaction. In this example, if the New York bank had erroneously sent an instruction to the California bank unconditionally instructing payment to X, the instruction would have been an Article 4A [Title 30, chapter 4A] payment order. If the payment order was accepted (Section 4A-209(b) [30-4A-209(2)]) by the California bank, a payment by the New York bank to X would have resulted (Section 4A-406(a) [30-4A-406(1)]). But Article 4A [Title 30, chapter 4A] would not prevent recovery of funds from X on the basis that X was not entitled to retain the funds under the law of mistake and restitution, letter of credit law or other applicable law.

4. Transfers of funds made through the banking system are commonly referred to as either "credit" transfers or "debit" transfers. In a credit transfer the instruction to pay is given by the person making payment. In a debit transfer the instruction to pay is given by the person receiving payment. The purpose of subparagraph (ii) of subsection (a)(1) of Section 4A-103 [30-4A-103(1)(a)(ii)] is to include credit transfers in Article 4A [Title 30, chapter 4A] and to exclude debit transfers. All of the instructions to pay in the three cases described in Comment 1 fall within subparagraph (ii). Take Case #2 as an example. With respect to X's instruction given to Bank A, Bank A will be reimbursed by debiting X's account or otherwise receiving payment from X. With respect to Bank A's instruction to Bank B, Bank B will be reimbursed by receiving payment from Bank A. In a debit transfer, a creditor, pursuant to authority from the debtor, is enabled to draw on the debtor's bank account by issuing an instruction to pay to the debtor's bank. If the debtor's bank pays, it will be reimbursed by the debtor rather than by the person giving the instruction. For example, the holder of an insurance policy may pay premiums by authorizing the insurance company to order the policyholder's bank to pay the insurance company. The order to pay may be in the form of a draft covered by Article 3 [Title 30, chapter 3], or it might be an instruction to pay that is not an instrument under that Article. The bank receives reimbursement by debiting the policyholder's account. Or, a subsidiary corporation may make payments to its parent by authorizing the parent to order the subsidiary's bank to pay the parent from the subsidiary's account. These transactions are not covered by Article 4A [Title 30, chapter 4A] because subparagraph (2) [30-4A-103(1)(b)] is not satisfied. Article 4A [Title 30, chapter 4A] is limited to transactions in which the account to be debited by the receiving bank is that of the person in whose name the instruction is given.

If the beneficiary of a funds transfer is the originator of the transfer, the transfer is governed by Article 4A [Title 30, chapter 4A] if it is a credit transfer in form. If it is in the form of a debit transfer it is not governed by Article 4A [Title 30, chapter 4A]. For example, Corporation has accounts in Bank A and Bank B. Corporation instructs Bank A to pay to Corporation's account in Bank B. The funds transfer is governed by Article 4A [Title 30, chapter 4A]. Sometimes, Corporation will authorize Bank B to draw on Corporation's account in Bank A for the purpose of transferring funds into Corporation's account in Bank B. If Corporation also makes an agreement with Bank A under which Bank A is authorized to follow instructions of Bank B, as agent of Corporation, to transfer funds from Customer's account in Bank A, the instruction of Bank B is a payment order of Customer and is governed by Article 4A [Title 30, chapter 4A]. This kind of transaction is known in the wire-transfer business as a "drawdown transfer." If Corporation does not make such an agreement with Bank A and Bank B instructs Bank A to make the transfer, the order is in form a debit transfer and is not governed by Article 4A [Title 30, chapter 4A]. These debit transfers are normally ACH transactions in which Bank A relies on Bank B's warranties pursuant to ACH rules, including the warranty that the transfer is authorized.

5. The principal effect of subparagraph (iii) of subsection (a) of Section 4A-103 [30-4A-103(1)(a)(iii)] is to exclude from Article 4A [Title 30, chapter 4A] payments made by check or credit card. In those cases the instruction of the debtor to the bank on which the check is drawn or to which the credit card slip is to be presented is contained in the check or credit card slip signed by the debtor. The instruction is not transmitted by the debtor directly to the debtor's bank. Rather, the instruction is delivered or otherwise transmitted by the debtor to the creditor who then presents it to the bank either directly or through bank collection channels. These payments are governed by Articles 3 and 4 [Title 30, chapters 3 and 4] and federal law. There are, however, limited instances in which the paper on which a check is printed can be used as the means of transmitting a payment order that is covered by Article 4A [Title 30, chapter 4A]. Assume that Originator instructs Originator's Bank to pay $10,000 to the account of Beneficiary in Beneficiary's Bank. Since the amount of Originator's payment order is small, if Originator's Bank and Beneficiary's Bank do not have an account relationship, Originator's Bank may execute Originator's order by issuing a teller's check payable to Beneficiary's Bank for $10,000 along with instructions to credit Beneficiary's account in that amount. The instruction to Beneficiary's Bank to credit Beneficiary's account is a payment order. The check is the means by which Originator's Bank pays its obligation as sender of the payment order. The instruction of Originator's Bank to Beneficiary's Bank might be given in a letter accompanying the check or it may be written on the check itself. In either case the instruction to Beneficiary's Bank is a payment order but the check itself (which is an order to pay addressed to the drawee rather than to Beneficiary's Bank) is an instrument under Article 3 [Title 30, chapter 3] and is not a payment order. The check can be both the means by which Originator's Bank pays its obligation under § 4A-402(b) [30-4A-402(2)] to Beneficiary's Bank and the means by which the instruction to Beneficiary's Bank is transmitted.

6. Most payments covered by Article 4A [Title 30, chapter 4A] are commonly referred to as wire transfers and usually involve some kind of electronic transmission, but the applicability of Article 4A [Title 30, chapter 4A] does not depend upon the means used to transmit the instruction of the sender. Transmission may be by letter or other written communication, oral communication or electronic communication. An oral communication is normally given by telephone. Frequently the message is recorded by the receiving bank to provide evidence of the transaction, but apart from problems of proof there is no need to record the oral instruction. Transmission of an instruction may be a direct communication between the sender and the receiving bank or through an intermediary such as an agent of the sender, a communication system such as international cable, or a funds transfer system such as CHIPS, SWIFT or an automated clearing house.

Case Notes

Federal Regulations Applicable to Wire Transfer — Summary Judgment on Wire Transfer Negligence Claim Proper: Hughes was the victim of a "Nigerian scam". Hughes was promised millions of dollars if he transferred money to a bank in Amman, Jordan. Hughes requested the plaintiff bank to wire $800,000 to the Jordan bank. Upon discovering that checks sent to Hughes to cover the transfer were bogus, Hughes sought to cancel the transfer, but the transfer had been completed, and the money subsequently disappeared. Hughes filed a negligence claim against plaintiff regarding the wire transfer, but the District Court granted summary judgment to plaintiff, and on appeal, the Supreme Court affirmed. The parties agreed that the federal Electronic Fund Transfer Act did not apply, but Hughes failed to offer authority that Article 4A of the Uniform Commercial Code did not apply. The District Court correctly held that nothing in federal regulations or in Article 4A requires a bank to agree to a cancellation, so there was no liability that could be alleged, and summary judgment for plaintiff on the negligence claim regarding the wire transfer was proper. Valley Bank of Ronan v. Hughes, 2006 MT 285, 334 M 335, 147 P3d 185 (2006).

30-4A-105. Other definitions.

Official Comment

Source: Section 4A-105, U.C.C.

Official Comment:

1. The definition of "bank" in subsection (a)(2) [subsection (1)(b) of this section] includes some institutions that are not commercial banks. The definition reflects the fact that many financial institutions now perform functions previously restricted to commercial banks, including acting on behalf of customers in funds transfers. Since many funds transfers involve payment orders to or from foreign countries the definition also covers foreign banks. The definition also includes Federal Reserve Banks. Funds transfers carried out by Federal Reserve Banks are described in Comments 1 and 2 to Section 4A-107 [30-4A-107].

2. Funds transfer business is frequently transacted by banks outside of general banking hours. Thus, the definition of banking day in Section 4-104(1)(c) [30-4-104(1)(c)] cannot be used to describe when a bank is open for funds transfer business. Subsection (a)(4) [subsection (1)(d) of this section] defines a new term, "funds transfer business day," which is applicable to Article 4A [Title 30, chapter 4A]. The definition states, "is open for the receipt, processing, and transmittal of payment orders and cancellations and amendments of payment orders." In some cases it is possible to electronically transmit payment orders and other communications to a receiving bank at any time. If the receiving bank is not open for the processing of an order when it is received, the communication is stored in the receiving bank's computer for retrieval when the receiving bank is open for processing. The use of the conjunctive makes clear that the defined term is limited to the period during which all functions of the receiving bank can be performed, i.e., receipt, processing, and transmittal of payment orders, cancellations and amendments.

3. Subsection (a)(5) [subsection (1)(e) of this section] defines "funds transfer system." The term includes a system such as CHIPS which provides for transmission of a payment order as well as settlement of the obligation of the sender to pay the order. It also includes automated clearing houses, operated by a clearing house or other association of banks, which process and transmit payment orders of banks to other banks. In addition the term includes organizations that provide only transmission services such as SWIFT. The definition also includes the wire transfer network and automated clearing houses of Federal Reserve Banks. Systems of the Federal Reserve Banks, however, are treated differently from systems of other associations of banks. Funds transfer systems other than systems of the Federal Reserve Banks are treated in Article 4A [Title 30, chapter 4A] as a means of communication of payment orders between participating banks. Section 4A-206 [30-4A-206]. The Comment to that section and the Comment to Section 4A-107 [30-4A-107] explain how Federal Reserve Banks function under Article 4A [Title 30, chapter 4A]. Funds transfer systems are also able to promulgate rules binding on participating banks that, under Section 4A-501 [30-4A-501], may supplement or in some cases may even override provisions of Article 4A [Title 30, chapter 4A].

4. Subsection (d) [subsection (4) of this section] incorporates definitions stated in Article 1 [Title 30, chapter 1] as well as principles of construction and interpretation stated in that Article. Included is Section 1-103 [30-1-103]. The last paragraph of the Comment to Section 4A-102 [30-4A-102] is addressed to the issue of the extent to which general principles of law and equity should apply to situations covered by provisions of Article 4A [Title 30, chapter 4A].

Compiler's Comments

2005 Amendment: Chapter 575 in definition of prove substituted "30-1-201(2)(i)" for "30-1-201(8)". Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-4A-106. Time payment order is received.

Official Comment

Source: Section 4A-106, U.C.C.

Official Comment:
The time that a payment order is received by a receiving bank usually defines the payment date or the execution date of a payment order. Section 4A-401 [30-4A-401] and Section 4A-301 [30-4A-301]. The time of receipt of a payment order, or communication cancelling or amending a payment order is defined in subsection (a) [subsection (1) of this section] by reference to the rules stated in Section 1-201(27) [30-1-201(27)]. Thus, time of receipt is determined by the same rules that determine when a notice is received. Time of receipt, however, may be altered by a cut-off time.

Compiler's Comments

2005 Amendment: Chapter 575 in (1) in first sentence at end substituted "30-1-210" for "30-1-201(27)". Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-4A-107. Federal reserve regulations and operating circulars.

Official Comment

Source: Section 4A-107, U.C.C.

Official Comment:

1. Funds transfers under Article 4A [Title 30, chapter 4A] may be made, in whole or in part, by payment orders through a Federal Reserve Bank in what is usually referred to as a transfer by Fedwire. If Bank A, which has an account in Federal Reserve Bank X, wants to pay $1,000,000 to Bank B, which has an account in Federal Reserve Bank Y, Bank A can issue an instruction to Reserve Bank X requesting a debit of $1,000,000 to Bank A's Reserve account and an equal credit to Bank B's Reserve account. Reserve Bank X will debit Bank A's account and will credit the account of Reserve Bank Y. Reserve Bank X will issue an instruction to Reserve Bank Y requesting a debit of $1,000,000 to the account of Reserve Bank X and an equal credit to Bank B's account in Reserve Bank Y. Reserve Bank Y will make the requested debit and credit and will give Bank B an advice of credit. The definition of "bank" in Section 4A-105(a)(2) [30-4A-105(1)(b)] includes both Reserve Bank X and Reserve Bank Y. Bank A's instruction to Reserve Bank X to pay money to Bank B is a payment order under Section 4A-103(a)(1) [30-4A-103(1)(a)]. Bank A is the sender and Reserve Bank X is the receiving bank. Bank B is the beneficiary of Bank A's order and of the funds transfer. Bank A is the originator of the funds transfer and is also the originator's bank. Section 4A-104(c) and (d) [30-4A-104(3) and (4)]. Reserve Bank X, an intermediary bank under Section 4A-104(b) [30-4A-104(2)], executes Bank A's order by sending a payment order to Reserve Bank Y instructing that bank to credit the Federal Reserve account of Bank B. Reserve Bank Y is the beneficiary's bank.

Suppose the transfer of funds from Bank A to Bank B is part of a larger transaction in which Originator, a customer of Bank A, wants to pay Beneficiary, a customer of Bank B. Originator issues a payment order to Bank A to pay $1,000,000 to the account of Beneficiary in Bank B. Bank A may execute Originator's order by means of Fedwire which simultaneously transfers $1,000,000 from Bank A to Bank B and carries a message instructing Bank B to pay $1,000,000 to the account of Y. The Fedwire transfer is carried out as described in the previous paragraph, except that the beneficiary of the funds transfer is Beneficiary rather than Bank B. Reserve Bank X and Reserve Bank Y are intermediary banks. When Reserve Bank Y advises Bank B of the credit to its Federal Reserve account it will also instruct Bank B to pay to the account of Beneficiary. The instruction is a payment order to Bank B which is the beneficiary's bank. When Reserve Bank Y advises Bank B of the credit to its Federal Reserve account Bank B receives payment of the payment order issued to it by Reserve Bank Y. Section 4A-403(a)(1) [30-4A-403(1)(a)]. The payment order is automatically accepted by Bank B at the time it receives the payment order of Reserve Bank Y. Section 4A-209(b)(2) [30-4A-209(2)(b)]. At the time of acceptance by Bank B payment by Originator to Beneficiary also occurs. Thus, in a Fedwire transfer, payment to the beneficiary's bank, acceptance by the beneficiary's bank and payment by the originator to the beneficiary all occur simultaneously by operation of law at the time the payment order to the beneficiary's bank is received.

If Originator orders payment to the account of Beneficiary in Bank C rather than Bank B, the analysis is somewhat modified. Bank A may not have any relationship with Bank C and may not be able to make payment directly to Bank C. In that case, Bank A could send a Fedwire instructing Bank B to instruct Bank C to pay Beneficiary. The analysis is the same as the previous case except that Bank B is an intermediary bank and Bank C is the beneficiary's bank.

2. A funds transfer can also be made through a Federal Reserve Bank in an automated clearing house transaction. In a typical case, Originator instructs Originator's Bank to pay to the account of Beneficiary in Beneficiary's Bank. Originator's instruction to pay a particular beneficiary is transmitted to Originator's Bank along with many other instructions for payment to other beneficiaries by many different beneficiary's banks. All of these instructions are contained in a magnetic tape or other electronic device. Transmission of instructions to the various beneficiary's banks requires that Originator's instructions be processed and repackaged with instructions of other originators so that all instructions to a particular beneficiary's bank are transmitted together to that bank. The repackaging is done in processing centers usually referred to as automated clearing houses. Automated clearing houses are operated either by Federal Reserve Banks or by other associations of banks. If Originator's Bank chooses to execute Originator's instructions by transmitting them to a Federal Reserve Bank for processing by the Federal Reserve Bank, the transmission to the Federal Reserve Bank results in the issuance of payment orders by Originator's Bank to the Federal Reserve Bank, which is an intermediary bank. Processing by the Federal Reserve Bank will result in the issuance of payment orders by the Federal Reserve Bank to Beneficiary's Bank as well as payment orders to other beneficiary's banks making payments to carry out Originator's instructions.

3. Although the terms of Article 4A [Title 30, chapter 4A] apply to funds transfers involving Federal Reserve Banks, federal preemption would make ineffective any Article 4A [Title 30, chapter 4A] provision that conflicts with federal law. The payments activities of the Federal Reserve Banks are governed by regulations of the Federal Reserve Board and by operating circulars issued by the Reserve Banks themselves. In some instances, the operating circulars are issued pursuant to a Federal Reserve Board regulation. In other cases, the Reserve Bank issues the operating circular under its own authority under the Federal Reserve Act, subject to review by the Federal Reserve Board. Section 4A-107 [30-4A-107] states that Federal Reserve Board regulations and operating circulars of the Federal Reserve Banks supersede any inconsistnt [sic] provision of Article 4A [Title 30, chapter 4A] to the extent of the inconsistency. Federal Reserve Board regulations, being valid exercises of regulatory authority pursuant to a federal statute, take precedence over state law if there is an inconsistency. Childs v. Federal Reserve Bank of Dallas, 719 F.2d 812 (5th Cir. 1983), reh. den. 724 F.2d 127 (5th Cir. 1984). Section 4A-107 [30-4A-107] treats operating circulars as having the same effect whether issued under the Reserve Bank's own authority or under a Federal Reserve Board regulation.

30-4A-108. Relationship to Electronic Fund Transfer Act.

Official Comment

Source: Section 4A-108, U.C.C.

Official Comment:

1. The Electronic Fund Transfer Act (EFTA), implemented by Regulation E, 12 C.F.R. Part 1005, is a federal statute that covers aspects of electronic fund transfers involving consumers. EFTA also governs remittance transfers, defined in 15 U.S.C. Sec. 1693o-1, which involve transfers of funds through electronic means by consumers to recipients in another country through persons or financial institutions that provide such transfers in the normal course of their business. Not all "remittance transfers" as defined in EFTA, however, qualify as "electronic fund transfers" as defined under the EFTA, 15 U.S.C. Sec. 1693a(7). While Section 4A-108(a) [30-4A-108(1)] broadly states that Article 4A [Title 30, chapter 4A] does not apply to any funds transfer that is governed in any part by EFTA, subsection (b) [subsection (2)] provides an exception. The purpose of Section 4A-108(b) [30-4A-108(2)] is to allow this Article [Title 30, chapter 4A] to apply to a funds transfer as defined in Section 4A-104(a) [30-4A-104(1)] (see Section 4A-102 [30-4A-102]) that also is a remittance transfer as defined in EFTA, so long as that remittance transfer is not an electronic fund transfer as defined in EFTA. If the resulting application of this Article [Title 30, chapter 4A] to an EFTA-defined "remittance transfer" that is not an EFTA-defined "electronic fund transfer" creates an inconsistency between an applicable provision of this Article [Title 30, chapter 4A] and an applicable provision of EFTA, then, as a matter of federal supremacy, the provision of EFTA governs to the extent of the inconsistency. Section 4A-108(c) [30-4A-108(3)]. Of course, in the case of a funds transfer that also relates to another jurisdiction, the forum's conflict of laws principles

determine whether it will apply the law in effect in this State (including this Article [Title 30, chapter 4A] and EFTA) or the law of another jurisdiction to all or any part of the funds transfer. See Section 4A-507 [30-4A-507].

2. The following cases illustrate the relationship between EFTA and this Article [Title 30, chapter 4A] pursuant to Section 4A-108 [30-4A-108].

Case #1. A commercial customer of Bank A sends a payment order to Bank A, instructing Bank A to transfer funds from its account at Bank A to the account of a consumer at Bank B. The funds transfer is executed by a payment order from Bank A to an intermediary bank and is executed by the intermediary bank by means of an automated clearinghouse credit entry to the consumer's account at Bank B (the beneficiary's bank). The transfer into the consumer's account is an "electronic fund transfer" as defined in 15 U.S.C. Sec. 1693a(7). Pursuant to Section 4A-108(a) [30-4A-108(1)], Article 4A [Title 30, chapter 4A] does not apply to any part of the funds transfer because EFTA governs part of the funds transfer. The transfer is not a "remittance transfer" as defined in 15 U.S.C. Sec. 1693o-1 because the originator is not a consumer customer. Thus Section 4A-108(b) [30-4A-108(2)] does not apply.

A court might, however, apply appropriate principles from Article 4A [Title 30, chapter 4A] by analogy in analyzing any part of the funds transfer that is not subject to the provisions of EFTA or other law, such as the obligation of the intermediary bank to execute the payment order of the originator's bank (Section 4A-302 [30-4A-302]), or whether the payment order of the commercial customer to Bank A is authorized or verified (Sections 4A-202 [30-4A-202] and 4A-203 [30-4A-203]).

Case #2. A consumer originates a payment order that is a remittance transfer as defined in 15 U.S.C. Sec. 1693o-1 and provides the remittance transfer provider (Bank A) with cash in the amount of the transfer plus any relevant fees. The funds transfer is routed through an intermediary bank for final credit to the designated recipient's account at Bank B. Bank A's payment order identifies the designated recipient by both name and account number in Bank B, but the name and number provided identify different persons. This remittance transfer is not an "electronic fund transfer" as defined in 15 U.S.C. Sec. 1693a(7) because it is not initiated by electronic means from a consumer's account, but does qualify as a "funds transfer" as defined in Section 4A-104 [30-4A-104]. Both Article 4A [Title 30, chapter 4A] and EFTA apply to the funds transfer. Sections 4A-102 [30-4A-102], 4A-108(a), (b) [30-4A-108(1), (2)]. Article 4A's [Title 30, chapter 4A's] provision on mistakes in identifying the designated beneficiary, Section 4A-207 [30-4A-207], would apply as long as not inconsistent with the governing EFTA provisions. See 15 U.S.C. Sec. 1693o-1(d), Section 4A-108(c) [30-4A-108(3)]. See Comment 1 to this Section.

Case #3. A consumer originates a payment order from the consumer's account at Bank A to the designated recipient's account at Bank B located outside the United States. Bank A uses the CHIPS system to execute that payment order. The funds transfer is a "remittance transfer" as defined in 15 U.S.C. Sec. 1693o-1. This transfer is not an "electronic fund transfer" as defined in 15 U.S.C. Sec. 1693a(7) because of the exclusion for transfers through systems such as CHIPS in 15 U.S.C. Sec. 1693a(7)(B), but qualifies as a "funds transfer" as defined in Section 4A-104 [30-4A-104]. Under Sections 4A-102 [30-4A-102] and 4A-108(b) [30-4A-108](2), both Article 4A [Title 30, chapter 4A] and EFTA apply to the funds transfer. The EFTA will prevail to the extent of any inconsistency between EFTA and Article 4A [Title 30, chapter 4A]. Section 4A-108(c) [30-4A-108(3)]. See Comment 1 to this Section. For example, if the consumer subsequently exercises a right under EFTA to cancel the remittance transfer and obtain a refund, Bank A would be required to comply with the EFTA rule even if Article 4A [Title 30, chapter 4A] prevents Bank A from cancelling or reversing the payment order that Bank A sent to its receiving bank. Section 4A-211 [30-4A-211].

Case #4. A person fraudulently originates an unauthorized payment order from a consumer's account through use of an online banking interface and the payment order is executed using a system that qualifies the transaction as an "electronic fund transfer" under EFTA. The funds transfer that results from execution of the unauthorized payment order is not governed by Article 4A [Title 30, chapter 4A]. Section 4A-108(a) [30-4A-108(1)]. Whether the funds transfer also qualifies as a "remittance transfer" under EFTA has no bearing on the application of Article 4A [Title 30, chapter 4A].

Case #5. A person fraudulently originates an unauthorized payment order from a consumer's account at Bank A through forging written documents that are provided in person to an employee of Bank A. This transaction is not an "electronic fund transfer" as defined in 15 U.S.C. Sec. 1693a(7) because it was not initiated by electronic means, but qualifies as a "funds transfer" as defined in Section 4A-104 [30-4A-104]. Article 4A [Title 30, chapter 4A] applies regardless of whether the funds transfer also qualifies as a "remittance transfer" under 15 U.S.C. Sec. 1693o-1. If the funds transfer is not a remittance transfer, the provisions of Section 4A-108 [30-4A-108] are not implicated because the funds transfer does not fall under EFTA, and the general scope provision of Article 4A [Title 30, chapter 4A] governs. Section 4A-102 [30-4A-102]. If the funds transfer is a remittance transfer, and thus governed by EFTA, Section 4A-108(b) [30-4A-108(2)] provides that Article 4A [Title 30, chapter 4A] also applies. The provisions of Article 4A [Title 30, chapter 4A] allocate the loss arising from the unauthorized payment order as long as those provisions are not inconsistent with the provisions of the EFTA applicable to remittance transfers. See 15 U.S.C. Sec. 1693o-1, Section 4A-108(c) [30-4A-108(3)]. See Comment 1 to this Section.

3. Regulation J, 12 C.F.R. Part 210, of the Federal Reserve Board addresses the application of that regulation and EFTA to fund transfers made through Fedwire. Fedwire transfers are further described in Official Comments 1 and 2 to Section 4A-107 [30-4A-107]. In addition, funds transfer system rules may be applicable pursuant to Section 4A-501 [30-4A-501].

Compiler's Comments

2013 Amendment: Chapter 71 substituted current catchline for "Exclusion of consumer transactions governed by federal law"; at beginning of (1) inserted exception clause and at end deleted "as amended from time to time"; inserted (2) and (3) regarding applicability of chapter; and made minor changes in style. Amendment effective March 18, 2013.

Montana Changes: To avoid an unconstitutional delegation of authority, the Montana version omitted the words "as amended from time to time" after federal U.S.C. citations in subsections (1) and (2).

Part 2
Issue and Acceptance of Payment Order

30-4A-201. Security procedure.

Official Comment

Source: Section 4A-201, U.C.C.

Official Comment:

A large percentage of payment orders and communications amending or cancelling payment orders are transmitted electronically and it is standard practice to use security procedures that are designed to assure the authenticity of the message. Security procedures can also be used to detect error in the content of messages or to detect payment orders that are transmitted by mistake as in the case of multiple transmission of the same payment order. Security procedures might also apply to communications that are transmitted by telephone or in writing. Section 4A-201 [30-4A-201] defines these security procedures. The definition of security procedure limits the term to a procedure "established by agreement of a customer and a receiving bank." The term does not apply to procedures that the receiving bank may follow unilaterally in processing payment orders. The question of whether loss that may result from the transmission of a spurious or erroneous payment order will be borne by the receiving bank or the sender or purported sender is affected by whether a security procedure was or was not in effect and whether there was or was not compliance with the procedure. Security procedures are referred to in Sections 4A-202 [30-4A-202] and 4A-203 [30-4A-203], which deal with authorized and verified payment orders, and Section 4A-205 [30-4A-205], which deals with erroneous payment orders.

30-4A-202. Authorized and verified payment orders.

Official Comment

Source: Section 4A-202, U.C.C.

Official Comment:

This section is discussed in the Comment following Section 4A-203 [30-4A-203].

30-4A-203. Unenforceability of certain verified payment orders.

Official Comment

Source: Section 4A-203, U.C.C.

Official Comment:

1. Some person will always be identified as the sender of a payment order. Acceptance of the order by the receiving bank is based on a belief by the bank that the order was authorized by the person identified as the sender. If the receiving bank is the beneficiary's bank acceptance means that the receiving bank is obliged to pay the beneficiary. If the receiving bank is not the beneficiary's bank, acceptance means that the receiving bank has executed the sender's order and is obliged to pay the bank that accepted the order issued in execution of the sender's order.

In either case the receiving bank may suffer a loss unless it is entitled to enforce payment of the payment order that it accepted. If the person identified as the sender of the order refuses to pay on the ground that the order was not authorized by that person, what are the rights of the receiving bank? In the absence of a statute or agreement that specifically addresses the issue, the question usually will be resolved by the law of agency. In some cases, the law of agency works well. For example, suppose the receiving bank executes a payment order given by means of a letter apparently written by a corporation that is a customer of the bank and apparently signed by an officer of the corporation. If the receiving bank acts solely on the basis of the letter, the corporation is not bound as the sender of the payment order unless the signature was that of the officer and the officer was authorized to act for the corporation in the issuance of payment orders, or some other agency doctrine such as apparent authority or estoppel causes the corporation to be bound. Estoppel can be illustrated by the following example. Suppose P is aware that A, who is unauthorized to act for P, has fraudulently misrepresented to T that A is authorized to act for P. T believes A and is about to rely on the misrepresentation. If P does not notify T of the true facts although P could easily do so, P may be estopped from denying A's lack of authority. A similar result could follow if the failure to notify T is the result of negligence rather than a deliberate decision. Restatement, Second, Agency § 8B. Other equitable principles such as subrogation or restitution might also allow a receiving bank to recover with respect to an unauthorized payment order that it accepted. In Gatoil (U.S.A.), Inc. v. Forest Hill State Bank, 1 U.C.C. Rep. Serv. 2d 171 (D.Md. 1986), a joint venturer not authorized to order payments from the account of the joint venture, ordered a funds transfer from the account. The transfer paid a bona fide debt of the joint venture. Although the transfer was unauthorized the court refused to require recredit of the account because the joint venture suffered no loss. The result can be rationalized on the basis of subrogation of the receiving bank to the right of the beneficiary of the funds transfer to receive the payment from the joint venture.

But in most cases these legal principles give the receiving bank very little protection in the case of an authorized payment order. Cases like those just discussed are not typical of the way that most payment orders are transmitted and accepted, and such cases are likely to become even less common. Given the large amount of the typical payment order, a prudent receiving bank will be unwilling to accept a payment order unless it has assurance that the order is what it purports to be. This assurance is normally provided by security procedures described in Section 4A-201 [30-4A-201].

In a very large percentage of cases covered by Article 4A [Title 30, chapter 4A], transmission of the payment order is made electronically. The receiving bank may be required to act on the basis of a message that appears on a computer screen. Common law concepts of authority of agent to bind principal are not helpful. There is no way of determining the identity or the authority of the person who caused the message to be sent. The receiving bank is not relying on the authority of any particular person to act for the purported sender. The case is not comparable to payment of a check by the drawee bank on the basis of a signature that is forged. Rather, the receiving bank relies on a security procedure pursuant to which the authenticity of the message can be "tested" by various devices which are designed to provide certainty that the message is that of the sender identified in the payment order. In the wire transfer business the concept of "authorized" is different from that found in agency law. In that business a payment order is treated as the order of the person in whose name it is issued if it is properly tested pursuant to a security procedure and the order passes the test.

Section 4A-202 [30-4A-202] reflects the reality of the wire transfer business. A person in whose name a payment order is issued is considered to be the sender of the order if the order is "authorized" as stated in subsection (a) [30-4A-202(1)] or if the order is "verified" pursuant to a security procedure in compliance with subsection (b) [30-4A-202(2)]. If subsection (b) [30-4A-202(2)] does not apply, the question of whether the customer is responsible for the order is determined by the law of agency. The issue is one of actual or apparent authority of the person who caused the order to be issued in the name of the customer. In some cases the law of agency might allow the customer to be bound by an unauthorized order if conduct of the customer can be used to find an estoppel against the customer to deny that the order was unauthorized. If the customer is bound by the order under any of these agency doctrines, subsection (a) [30-4A-202(1)] treats the order as authorized and thus the customer is deemed to be the sender of the order. In most cases, however, subsection (b) [30-4A-202(2)] will apply. In that event there is no need to make an agency law analysis to determine authority. Under Section 4A-202 [30-4A-202], the issue of liability of the purported sender of the payment order will be determined by agency law only if the receiving bank did not comply with subsection (b) [30-4A-202(2)].

2. The scope of Section 4A-202 [30-4A-202] can be illustrated by the following cases.

Case #1. A payment order purporting to be that of Customer is received by Receiving Bank but the order was fraudulently transmitted by a person who had no authority to act for Customer.

Case #2. An authentic payment order was sent by Customer, but before the order was received by Receiving Bank the order was fraudulently altered by an unauthorized person to change the beneficiary.

Case #3. An authentic payment order was received by Receiving Bank, but before the order was executed by Receiving Bank a person who had no authority to act for Customer fraudulently sent a communication purporting to amend the order by changing the beneficiary. In each case Receiving Bank acted on the fraudulent communication by accepting the payment order. These cases are all essentially similar and they are treated identically by Section 4A-202 [30-4A-202]. In each case Receiving Bank acted on a communication that it thought was authorized by Customer when in fact the communication was fraudulent. No distinction is made between Case #1 in which Customer took no part at all in the transaction and Case #2 and Case #3 in which an authentic order was fraudulently altered or amended by an unauthorized person. If subsection (b) [30-4A-202(2)] does not apply, each case is governed by subsection (a) [30-4A-202(1)]. If there are no additional facts on which an estoppel might be found, Customer is not responsible in Case #1 for the fraudulently issued payment order, in Case #2 for the fraudulent alteration or in Case #3 for the fraudulent amendment. Thus, in each case Customer is not liable to pay the order and Receiving Bank takes the loss. The only remedy of Receiving Bank is to seek recovery from the person who received payment as beneficiary of the fraudulent order. If there was verification in compliance with subsection (b) [30-4A-202(2)], Customer will take the loss unless Section 4A-203 [30-4A-203] applies.

3. Subsection (b) of Section 4A-202 [30-4A-202(2)] is based on the assumption that losses due to fraudulent payment orders can best be avoided by the use of commercially reasonable security procedures, and that the use of such procedures should be encouraged. The subsection is designed to protect both the customer and the receiving bank. A receiving bank needs to be able to rely on objective criteria to determine whether it can safely act on a payment order. Employees of the bank can be trained to "test" a payment order according to the various steps specified in the security procedure. The bank is responsible for the acts of these employees. Subsection (b)(ii) [30-4A-202(2)] requires the bank to prove that it accepted the payment order in good faith and "in compliance with the security procedure." If the fraud was not detected because the bank's employee did not perform the acts required by the security procedure, the bank has not complied. Subsection (b)(ii) [30-4A-202(2)] also requires the bank to prove that it complied with any agreement or instruction that restricts acceptance of payment orders issued in the name of the customer. A customer may want to protect itself by imposing limitations on acceptance of payment orders by the bank. For example, the customer may prohibit the bank from accepting a payment order that is not payable from an authorized account, that exceeds the credit balance in specified accounts of the customer, or that exceeds some other amount. Another limitation may relate to the beneficiary. The customer may provide the bank with a list of authorized beneficiaries and prohibit acceptance of any payment order to a beneficiary not appearing on the list. Such limitations may be incorporated into the security procedure itself or they may be covered by a separate agreement or instruction. In either case, the bank must comply with the limitations if the conditions stated in subsection (b) [30-4A-202(2)] are met. Normally limitations on acceptance would be incorporated into an agreement between the customer and the receiving bank, but in some cases the instruction might be unilaterally given by the customer. If standing instructions or an agreement state limitations on the ability of the receiving bank to act, provision must be made for later modification of the limitations. Normally this would be done by an agreement that specifies particular procedures to be followed. Thus, subsection (b) [30-4A-202(2)] states that the receiving bank is not required to follow an instruction that violates a written agreement. The receiving bank is not bound by an instruction unless it has adequate notice of it. Subsections (25), (26) and (27) of Section 1-201 [30-1-201(25) through (27)] apply.

Subsection (b)(i) [30-4A-202(2)] assures that the interests of the customer will be protected by providing an incentive to a bank to make available to the customer a security procedure that is commercially reasonable. If a commercially reasonable security procedure is not made available to the customer, subsection (b) [30-4A-202(2)] does not apply. The result is that subsection (a) [30-4A-202(1)] applies and the bank acts at its peril in accepting a payment order that may be unauthorized. Prudent banking practice may require that security procedures be utilized in virtually all cases except for those in which personal contact between the customer and the bank eliminates the possibility of an unauthorized order. The burden of making available commercially reasonable security procedures is imposed on receiving banks because they generally determine what security procedures can be used and are in the best position to evaluate the efficacy of procedures offered to customers to combat fraud. The burden on the customer is to supervise its employees to assure compliance with the security procedure and to safeguard confidential security information and access to transmitting facilities so that the security procedure cannot be breached.

4. The principal issue that is likely to arise in litigation involving subsection (b) [30-4A-202(2)] is whether the security procedure in effect when a fraudulent payment order was accepted was commercially reasonable. The concept of what is commercially reasonable in a given case is flexible. Verification entails labor and equipment costs that can vary greatly depending upon the degree of security that is sought. A customer that transmits very large numbers of payment orders in very large amounts may desire and may reasonably expect to be provided with state-of-the-art procedures that provide maximum security. But the expense involved may make use of a state-of-the-art procedure infeasible for a customer that normally transmits payments orders infrequently or in relatively low amounts. Another variable is the type of receiving bank. It is reasonable to require large money center banks to make available state-of-the-art security procedures. On the other hand, the same requirement may not be reasonable for a small country bank. A receiving bank might have several security procedures that are designed to meet the varying needs of different customers. The type of payment order is another variable. For example, in a wholesale wire transfer, each payment order is normally transmitted electronically and individually. A testing procedure will be individually applied to each payment order. In funds transfers to be made by means of an automated clearing house many payment orders are incorporated into an electronic device such as a magnetic tape that is physically delivered. Testing of the individual payment orders is not feasible. Thus, a different kind of security procedure must be adopted to take into account the different mode of transmission.

The issue of whether a particular security procedure is commercially reasonable is a question of law. Whether the receiving bank complied with the procedure is a question of fact. It is appropriate to make the finding concerning commercial reasonability a matter of law because security procedures are likely to be standardized in the banking industry and a question of law standard leads to more predictability concerning the level of security that a bank must offer to its customers. The purpose of subsection (b) [30-4A-202(2)] is to encourage banks to institute reasonable safeguards against fraud but not to make them insurers against fraud. A security procedure is not commercially unreasonable simply because another procedure might have been better or because the judge deciding the question would have opted for a more stringent procedure. The standard is not whether the security procedure is the best available. Rather it is whether the procedure is reasonable for the particular customer and the particular bank, which is a lower standard. On the other hand, a security procedure that fails to meet prevailing standards of good banking practice applicable to the particular bank should not be held to be commercially reasonable. Subsection (c) [30-4A-202(3)] states factors to be considered by the judge in making the determination of commercial reasonableness. Sometimes an informed customer refuses a security procedure that is commercially reasonable and suitable for that customer and insists on using a higher-risk procedure because it is more convenient or cheaper. In that case, under the last sentence of subsection (c) [30-4A-202(3)], the customer has voluntarily assumed the risk of failure of the procedure and cannot shift the loss to the bank. But this result follows only if the customer expressly agrees in writing to assume that risk. It is implicit in the last sentence of subsection (c) [30-4A-202(3)] that a bank that accedes to the wishes of its customer in this regard is not acting in bad faith by so doing so long as the customer is made aware of the risk. In all cases, however, a receiving bank cannot get the benefit of subsection (b) [30-4A-202(2)] unless it has made available to the customer a security procedure that is commercially reasonable and suitable for use by that customer. In most cases, the mutual interest of bank and customer to protect against fraud should lead to agreement to a security procedure which is commercially reasonable.

5. The effect of Section 4A-202(b) [30-4A-202(2)] is to place the risk of loss on the customer if an unauthorized payment order is accepted by the receiving bank after verification by the bank in compliance with a commercially reasonable security procedure. An exception to this result is provided by Section 4A-203(a)(2) [30-4A-203(1)(b)]. The customer may avoid the loss resulting from such a payment order if the customer can prove that the fraud was not committed by a person described in that subsection. Breach of a commercially reasonable security procedure requires that the person committing the fraud have knowledge of how the procedure works and knowledge of codes, identifying devices, and the like. That person may also need access to

transmitting facilities through an access device or other software in order to breach the security procedure. This confidential information must be obtained either from a source controlled by the customer or from a source controlled by the receiving bank. If the customer can prove that the person committing the fraud did not obtain the confidential information from an agent or former agent of the customer or from a source controlled by the customer, the loss is shifted to the bank. "Prove" is defined in Section 4A-105(a)(7) [30-4A-105(1)(g)]. Because of bank regulation requirements, in this kind of case there will always be a criminal investigation as well as an internal investigation of the bank to determine the probable explanation for the breach of security. Because a funds transfer fraud usually will involve a very large amount of money, both the criminal investigation and the internal investigation are likely to be thorough. In some cases there may be an investigation by bank examiners as well. Frequently, these investigations will develop evidence of who is at fault and the cause of the loss. The customer will have access to evidence developed in these investigations and that evidence can be used by the customer in meeting its burden of proof.

6. The effect of Section 4A-202(b) [30-4A-202(2)] may also be changed by an agreement meeting the requirements of Section 4A-203(a)(1) [30-4A-203(1)(a)]. Some customers may be unwilling to take all or part of the risk of loss with respect to unauthorized payment orders even if all of the requirements of Section 4A-202(b) [30-4A-202(2)] are met. By virtue of Section 4A-203(a)(1) [30-4A-203(1)(a)], a receiving bank may assume all of the risk of loss with respect to unauthorized payment orders or the customer and bank may agree that losses from unauthorized payment orders are to be divided as provided in the agreement.

7. In a large majority of cases the sender of a payment order is a bank. In many cases in which there is a bank sender, both the sender and the receiving bank will be members of a funds transfer system over which the payment order is transmitted. Since Section 4A-202(f) [30-4A-202(6)] does not prohibit a funds transfer system rule from varying rights and obligations under Section 4A-202 [30-4A-202], a rule of the funds transfer system can determine how loss due to an unauthorized payment order from a participating bank to another participating bank is to be allocated. A funds transfer system rule, however, cannot change the rights of a customer that is not a participating bank. Section 4A-501(b) [30-4A-501(2)]. Section 4A-202(f) [30-4A-202(6)] also prevents variation by agreement except to the extent stated.

30-4A-204. Refund of payment and duty of customer to report with respect to unauthorized payment order.

Official Comment

Source: Section 4A-204, U.C.C.

Official Comment:

1. With respect to unauthorized payment orders, in a very large percentage of cases a commercially reasonable security procedure will be in effect. Section 4A-204 [30-4A-204] applies only to cases in which (i) no commercially reasonable security procedure is in effect, (ii) the bank did not comply with a commercially reasonable security procedure that was in effect, (iii) the sender can prove, pursuant to Section 4A-203(a)(2) [30-4A-203(1)(b)], that the culprit did not obtain confidential security information controlled by the customer, or (iv) the bank, pursuant to Section 4A-203(a)(1) [30-4A-203(1)(a)] agreed to take all or part of the loss resulting from an unauthorized payment order. In each of these cases the bank takes the risk of loss with respect to an unauthorized payment order because the bank is not entitled to payment from the customer with respect to the order. The bank normally debits the customer's account or otherwise receives payment from the customer shortly after acceptance of the payment order. Subsection (a) of Section 4A-204 [30-4A-204(1)] states that the bank must recredit the account or refund payment to the extent the bank is not entitled to enforce payment.

2. Section 4A-204 [30-4A-204] is designed to encourage a customer to promptly notify the receiving bank that it has accepted an unauthorized payment order. Since cases of unauthorized payment orders will almost always involve fraud, the bank's remedy is normally to recover from the beneficiary of the unauthorized order if the beneficiary was party to the fraud. This remedy may not be worth very much and it may not make any difference whether or not the bank promptly learns about the fraud. But in some cases prompt notification may make it easier for the bank to recover some part of its loss from the culprit. The customer will routinely be notified of the debit to its account with respect to an unauthorized order or will otherwise be notified of acceptance of the order. The customer has a duty to exercise ordinary care to determine that the order was unauthorized after it has received notification from the bank, and to advise the bank of the relevant facts within a reasonable time not exceeding 90 days after receipt of notification.

Reasonable time is not defined and it may depend on the facts of the particular case. If a payment order for $1,000,000 is wholly unauthorized, the customer should normally discover it in far less than 90 days. If a $1,000,000 payment order was authorized but the name of the beneficiary was fraudulently changed, a much longer period may be necessary to discover the fraud. But in any event, if the customer delays more than 90 days the customer's duty has not been met. The only consequence of a failure of the customer to perform this duty is a loss of interest on the refund payable by the bank. A customer that acts promptly is entitled to interest from the time the customer's account was debited or the customer otherwise made payment. The rate of interest is stated in Section 4A-506 [30-4A-506]. If the customer fails to perform the duty, no interest is recoverable for any part of the period before the bank learns that it accepted an unauthorized order. But the bank is not entitled to any recovery from the customer based on negligence for failure to inform the bank. Loss of interest is in the nature of a penalty on the customer designed to provide an incentive for the customer to police its account. There is no intention to impose a duty on the customer that might result in shifting loss from the unauthorized order to the customer.

30-4A-205. Erroneous payment orders.

Official Comment

Source: Section 4A-205, U.C.C.

Official Comment:

1. This section concerns error in the content or in the transmission of payment orders. It deals with three kinds of error.

Case #1. The order identifies a beneficiary not intended by the sender. For example, Sender intends to wire funds to a beneficiary identified only by an account number. The wrong account number is stated in the order.

Case #2. The error is in the amount of the order. For example, Sender intends to wire $1,000 to Beneficiary. Through error, the payment order instructs payment of $1,000,000.

Case #3. A payment order is sent to the receiving bank and then, by mistake, the same payment order is sent to the receiving bank again. In Case #3, the receiving bank may have no way of knowing whether the second order is a duplicate of the first or is another order. Similarly, in Case #1 and Case #2, the receiving bank may have no way of knowing that the error exists. In each case, if this section does not apply and the funds transfer is completed, Sender is obliged to pay the order. Section 4A-402 [30-4A-402]. Sender's remedy, based on payment by mistake, is to recover from the beneficiary that received payment.

Sometimes, however, transmission of payment orders of the sender to the receiving bank is made pursuant to a security procedure designed to detect one or more of the errors described above. Since "security procedure" is defined by Section 4A-201 [30-4A-201] as "a procedure established by agreement of a customer and a receiving bank for the purpose of detecting error," Section 4A-205 [30-4A-205] does not apply if the receiving bank and the customer did not agree to the establishment of a procedure for detecting error. A security procedure may be designed to detect an account number that is not one to which Sender normally makes payment. In that case, the security procedure may require a special verification that payment to the stated account number was intended. In the case of dollar amounts, the security procedure may require different codes for different dollar amounts. If a $1,000,000 payment order contains a code that is inappropriate for that amount, the error in amount should be detected. In the case of duplicate orders, the security procedure may require that each payment order be identified by a number or code that applies to no other order. If the number or code of each payment order received is registered in a computer base, the receiving bank can quickly identify a duplicate order. The three cases covered by this section are essentially similar. In each, if the error is not detected, some beneficiary will receive funds that the beneficiary was not intended to receive. If this section applies, the risk of loss with respect to the error of the sender is shifted to the bank which has the burden of recovering the funds from the beneficiary. The risk of loss is shifted to the bank only if the sender proves that the error would have been detected if there had been compliance with the procedure and that the sender (or an agent under Section 4A-206 [30-4A-206]) complied. In the case of a duplicate order or a wrong beneficiary, the sender doesn't have to pay the order. In the case of an overpayment, the sender does not have to pay the order to the extent of the overpayment. If subsection (a)(1) [subsection (1)(a) of this section] applies, the position of the receiving bank is comparable to that of a receiving bank that erroneously executes a payment order as stated in Section 4A-303 [30-4A-303]. However, failure of the sender to timely report the error is covered by Section 4A-205(b) [30-4A-205(2)] rather than by Section 4A-304 [30-4A-304] which applies only to erroneous execution under Section 4A-303 [30-4A-303]. A receiving bank to which the risk of loss is shifted by subsection (a)(1) or (2) [subsection (1)(a) or (b) of this section] is entitled to recover the amount erroneously paid to the beneficiary to the extent allowed by the law of mistake and restitution. Rights of the receiving bank against the beneficiary are similar to those of a receiving bank that erroneously executes a payment order as stated in Section 4A-303 [30-4A-303]. Those rights are discussed in Comment 2 to Section 4A-303 [30-4A-303].

2. A security procedure established for the purpose of detecting error is not effective unless both sender and receiving bank comply with the procedure. Thus, the bank undertakes a duty of complying with the procedure for the benefit of the sender. This duty is recognized in subsection (a)(1) [subsection (1)(a) of this section]. The loss with respect to the sender's error is shifted to the bank if the bank fails to comply with the procedure and the sender (or an agent under Section 4A-206 [30-4A-206]) does comply. Although the customer may have been negligent in transmitting the erroneous payment order, the loss is put on the bank on a last-clear-chance theory. A similar analysis applies to subsection (b) [subsection (2) of this section]. If the loss with respect to an error is shifted to the receiving bank and the sender is notified by the bank that the erroneous payment order was accepted, the sender has a duty to exercise ordinary care to discover the error and notify the bank of the relevant facts within a reasonable time not exceeding 90 days. If the bank can prove that the sender failed in this duty it is entitled to compensation for the loss incurred as a result of the failure. Whether the bank is entitled to recover from the sender depends upon whether the failure to give timely notice would have made any difference. If the bank could not have recovered from the beneficiary that received payment under the erroneous payment order even if timely notice had been given, the sender's failure to notify did not cause any loss of the bank.

3. Section 4A-205 [30-4A-205] is subject to variation by agreement under Section 4A-501 [30-4A-501]. Thus, if a receiving bank and its customer have agreed to a security procedure for detection of error, the liability of the receiving bank for failing to detect an error of the customer as provided in Section 4A-205 [30-4A-205] may be varied as provided in an agreement of the bank and the customer.

30-4A-206. Transmission of payment order through funds-transfer or other communication system.

Official Comment

Source: Section 4A-206, U.C.C.

Official Comment:

1. A payment order may be issued to a receiving bank directly by delivery of a writing or electronic device or by an oral or electronic communication. If an agent of the sender is employed to transmit orders on behalf of the sender, the sender is bound by the order transmitted by the agent on the basis of agency law. Section 4A-206 [30-4A-206] is an application of that principle to cases in which a funds transfer or communication system acts as an intermediary in transmitting the sender's order to the receiving bank. The intermediary is deemed to be an agent of the sender for the purpose of transmitting payment orders and related messages for the sender. Section 4A-206 [30-4A-206] deals with error by the intermediary.

2. Transmission by an automated clearing house of an association of banks other than the Federal Reserve Banks is an example of a transaction covered by Section 4A-206 [30-4A-206]. Suppose Originator orders Originator's Bank to cause a large number of payments to be made to many accounts in banks in various parts of the country. These payment orders are electronically transmitted to Originator's Bank and stored in an electronic device that is held by Originator's Bank. Or, transmission of the various payment orders is made by delivery to Originator's Bank of an electronic device containing the instruction to the bank. In either case the terms of the various payment orders by Originator are determined by the information contained in the electronic device. In order to execute the various orders, the information in the electronic device must be processed. For example, if some of the orders are for payments to accounts in Bank X and some to accounts in Bank Y, Originator's Bank will execute these orders of Originator by issuing a series of payment orders to Bank X covering all payments to accounts in that bank, and by issuing a series of payment orders to Bank Y covering all payments to accounts in that bank. The orders to Bank X may be transmitted together by means of an electronic device, and those to Bank Y may be included in another electronic device. Typically, this processing is done by an automated clearing house acting for a group of banks including Originator's Bank. The automated clearing house is a funds transfer system. Section 4A-105(a)(5) [30-4A-105(1)(e)]. Originator's Bank delivers Originator's electronic device or transmits the information contained in the device to the

funds transfer system for processing into payment orders of Originator's Bank to the appropriate beneficiary's banks. The processing may result in an erroneous payment order. Originator's Bank, by use of Originator's electronic device, may have given information to the funds transfer system instructing payment of $100,000 to an account in Bank X, but because of human error or an equipment malfunction the processing may have converted that instruction into an instruction to Bank X to make a payment of $1,000,000. Under Section 4A-206 [30-4A-206], Originator's Bank issued a payment order for $1,000,000 to Bank X when the erroneous information was sent to Bank X. Originator's Bank is responsible for the error of the automated clearing house. The liability of the funds transfer system that made the error is not governed by Article 4A [Title 30, chapter 4A]. It is left to the law of contract, a funds transfer system rule, or other applicable law.

In the hypothetical case just discussed, if the automated clearing house is operated by a Federal Reserve Bank, the analysis is different. Section 4A-206 [30-4A-206] does not apply. Originator's Bank will execute Originator's payment orders by delivery or transmission of the electronic information to the Federal Reserve Bank for processing. The result is that Originator's Bank has issued payment orders to the Federal Reserve Bank which, in this case, is acting as an intermediary bank. When the Federal Reserve Bank has processed the information given to it by Originator's Bank it will issue payment orders to the various beneficiary's banks. If the processing results in an erroneous payment order, the Federal Reserve Bank has erroneously executed the payment order of Originator's Bank and the case is governed by Section 4A-303 [30-4A-303].

30-4A-207. Misdescription of beneficiary.

Official Comment

Source: Section 4A-207, U.C.C.

Official Comment:

1. Subsection (a) [subsection (1) of this section] deals with the problem of payment orders issued to the beneficiary's bank for payment to nonexistent or unidentifiable persons or accounts. Since it is not possible in that case for the funds transfer to be completed, subsection (a) [subsection (1) of this section] states that the order cannot be accepted. Under Section 4A-402(c) [30-4A-402(3)], a sender of a payment order is not obliged to pay its order unless the beneficiary's bank accepts a payment order instructing payment to the beneficiary of that sender's order. Thus, if the beneficiary of a funds transfer is nonexistent or unidentifiable, each sender in the funds transfer that has paid its payment order is entitled to get its money back.

2. Subsection (b) [subsection (2) of this section], which takes precedence over subsection (a) [subsection (1) of this section], deals with the problem of payment orders in which the description of the beneficiary does not allow identification of the beneficiary because the beneficiary is described by name and by an identifying number or an account number and the name and number refer to different persons. A very large percentage of payment orders issued to the beneficiary's bank by another bank are processed by automated means using machines capable of reading orders on standard formats that identify the beneficiary by an identifying number or the number of a bank account. The processing of the order by the beneficiary's bank and the crediting of the beneficiary's account are done by use of the identifying or bank account number without human reading of the payment order itself. The process is comparable to that used in automated payment of checks. The standard format, however, may also allow the inclusion of the name of the beneficiary and other information which can be useful to the beneficiary's bank and the beneficiary but which plays no part in the process of payment. If the beneficiary's bank has both the account number and name of the beneficiary supplied by the originator of the funds transfer, it is possible for the beneficiary's bank to determine whether the name and number refer to the same person, but if a duty to make that determination is imposed on the beneficiary's bank the benefits of automated payment are lost. Manual handling of payment orders is both expensive and subject to human error. If payment orders can be handled on an automated basis there are substantial economies of operation and the possibility of clerical error is reduced. Subsection (b) [subsection (2) of this section] allows banks to utilize automated processing by allowing banks to act on the basis of the number without regard to the name if the bank does not know that the name and number refer to different persons. "Know" is defined in Section 1-201(25) [30-1-201(25)] to mean actual knowledge, and Section 1-201(27) [30-1-201(27)] states rules for determining when an organization has knowledge of information received by the organization. The time of payment is the pertinent time at which knowledge or lack of knowledge must be determined.

Although the clear trend is for beneficiary's banks to process payment orders by automated means, Section 4A-207 [30-4A-207] is not limited to cases in which processing is done by automated means. A bank that processes by semi-automated means or even manually may rely on number as stated in Section 4A-207 [30-4A-207].

In cases covered by subsection (b) [subsection (2) of this section] the erroneous identification would in virtually all cases be the identifying or bank account number. In the typical case the error is made by the originator of the funds transfer. The originator should know the name of the person who is to receive payment and can further identify that person by an address that would normally be known to the originator. It is not unlikely, however, that the originator may not be sure whether the identifying or account number refers to the person the originator intends to pay. Subsection (b)(1) [subsection (2)(a) of this section] deals with the typical case in which the beneficiary's bank pays on the basis of the account number and is not aware at the time of payment that the named beneficiary is not the holder of the account which was paid. In some cases the false number will be the result of error by the originator. In other cases fraud is involved. For example, Doe is the holder of shares in Mutual Fund. Thief, impersonating Doe, requests redemption of the shares and directs Mutual Fund to wire the redemption proceeds to Doe's account #12345 in Beneficiary's Bank. Mutual Fund originates a funds transfer by issuing a payment order to Originator's Bank to make the payment to Doe's account #12345 in Beneficiary's Bank. Originator's Bank executes the order by issuing a conforming payment order to Beneficiary's Bank which makes payment to account #12345. That account is the account of Roe rather than Doe. Roe might be a person acting in concert with Thief or Roe might be an innocent third party. Assume that Roe is a gem merchant that agreed to sell gems to Thief who agreed to wire the purchase price to Roe's account in Beneficiary's Bank. Roe believed that the credit to Roe's account was a transfer of funds from Thief and released the gems to Thief in good faith in reliance on the payment. The case law is unclear on the responsibility of a beneficiary's bank in carrying out a payment order in which the identification of the beneficiary by name and number is conflicting. See Securities Fund Services, Inc. v. American National Bank, 542 F.Supp. 323 (N.D.Ill. 1982) and Bradford Trust Co. v. Texas American Bank, 790 F.2d 407 (5th Cir. 1986). Section 4A-207 [30-4A-207] resolves the issue.

If Beneficiary's Bank did not know about the conflict between the name and number, subsection (b)(1) [subsection (2)(a) of this section] applies. Beneficiary's Bank has no duty to determine whether there is a conflict and it may rely on the number as the proper identification of the beneficiary of the order. When it accepts the order, it is entitled to payment from Originator's Bank. Section 4A-402(b) [30-4A-402(2)]. On the other hand, if Beneficiary's Bank knew about the conflict between the name and number and nevertheless paid Roe, subsection (b)(2) [subsection (2)(b) of this section] applies. Under that provision, acceptance of the payment order of Originator's Bank did not occur because there is no beneficiary of that order. Since acceptance did not occur Originator's Bank is not obliged to pay Beneficiary's Bank. Section 4A-402(b) [30-4A-402(2)]. Similarly, Mutual Fund is excused from its obligation to pay Originator's Bank. Section 4A-402(c) [30-4A-402(3)]. Thus, Beneficiary's Bank takes the loss. Its only cause of action is against Thief. Roe is not obliged to return the payment to the beneficiary's bank because Roe received the payment in good faith and for value. Article 4A [Title 30, chapter 4A] makes irrelevant the issue of whether Mutual Fund was or was not negligent in issuing its payment order.

3. Normally, subsection (b)(1) [subsection (2)(a) of this section] will apply to the hypothetical case discussed in Comment 2. Beneficiary's Bank will pay on the basis of the number without knowledge of the conflict. In that case subsection (c) [subsection (3) of this section] places the loss on either Mutual Fund or Originator's Bank. It is not unfair to assign the loss to Mutual Fund because it is the person who dealt with the impostor and it supplied the wrong account number. It could have avoided the loss if it had not used an account number that it was not sure was that of Doe. Mutual Fund, however, may not have been aware of the risk involved in giving both name and number. Subsection (c) [subsection (3) of this section] is designed to protect the originator, Mutual Fund, in this case. Under that subsection, the originator is responsible for the inconsistent description of the beneficiary if it had notice that the order might be paid by the beneficiary's bank on the basis of the number. If the originator is a bank, the originator always has that responsibility. The rationale is that any bank should know how payment orders are processed and paid. If the originator is not a bank, the originator's bank must prove that its customer, the originator, had notice. Notice can be proved by any admissible evidence, but the bank can always prove notice by providing the customer with a written statement of the required information and obtaining the customer's signature to the statement. That statement will then apply to any payment order accepted by the bank thereafter. The information need not be supplied more than once.

In the hypothetical case if Originator's Bank made the disclosure stated in the last sentence of subsection (c)(2) [subsection (3)(b) of this section], Mutual Fund must pay Originator's Bank. Under subsection (d)(1) [subsection (4)(a) of this section], Mutual Fund has an action to recover from Roe if recovery from Roe is permitted by the law governing mistake and restitution. Under the assumed facts Roe should be entitled to keep the money as a person who took it in good faith and for value since it was taken as payment for the gems. In that case, Mutual Fund's only remedy is against Thief. If Roe was not acting in good faith, Roe has to return the money to Mutual Fund. If Originator's Bank does not prove that Mutual Fund had notice as stated in subsection (c)(2) [subsection (3)(b) of this section], Mutual Fund is not required to pay Originator's Bank. Thus, the risk of loss falls on Originator's Bank whose remedy is against Roe or Thief as stated above. Subsection (d)(2) [subsection (4)(b) of this section].

30-4A-208. Misdescription of intermediary bank or beneficiary's bank.

Official Comment

Source: Section 4A-208, U.C.C.

Official Comment:

1. This section addresses an issue similar to that addressed by Section 4A-207 [30-4A-207]. Because of automation in the processing of payment orders, a payment order may identify the beneficiary's bank or an intermediary bank by an identifying number. The bank identified by number might or might not also be identified by name. The following two cases illustrate Section 4A-208(a) and (b) [30-4A-208(1) and (2)]:

Case #1. Originator's payment order to Originator's Bank identifies the beneficiary's bank as Bank A and instructs payment to Account #12345 in that bank. Originator's Bank executes Originator's order by issuing a payment order to Intermediary Bank. In the payment order of Originator's Bank the beneficiary's bank is identified as Bank A but is also identified by number, #67890. The identifying number refers to Bank B rather than Bank A. If processing by Intermediary Bank of the payment order of Originator's Bank is done by automated means, Intermediary Bank, in executing the order, will rely on the identifying number and will issue a payment order to Bank B rather than Bank A. If there is an Account #12345 in Bank B, the payment order of Intermediary Bank would normally be accepted and payment would be made to a person not intended by Originator. In this case, Section 4A-208(b)(1) [30-4A-208(2)(a)] puts the risk of loss on Originator's Bank. Intermediary Bank may rely on the number #67890 as the proper identification of the beneficiary's bank. Intermediary Bank has properly executed the payment order of Originator's Bank. By using the wrong number to describe the beneficiary's bank, Originator's Bank has improperly executed Originator's payment order because the payment order of Originator's Bank provides for payment to the wrong beneficiary, the holder of Account #12345 in Bank B rather than the holder of Account #12345 in Bank A. Section 4A-302(a)(1) [30-4A-302(1)(a)] and Section 4A-303(c) [30-4A-303(3)]. Originator's Bank is not entitled to payment from Originator but is required to pay Intermediary Bank. Section 4A-303(c) [30-4A-303(3)] and Section 4A-402(c) [30-4A-402(3)]. Intermediary Bank is also entitled to compensation for any loss and expenses resulting from the error by Originator's Bank.

If there is no Account #12345 in Bank B, the result is that there is no beneficiary of the payment order issued by Originator's Bank and the funds transfer will not be completed. Originator's Bank is not entitled to payment from Originator and Intermediary Bank is not entitled to payment from Originator's Bank. Section 4A-402(c) [30-4A-402(3)]. Since Originator's Bank improperly executed Originator's payment order it may be liable for damages under Section 4A-305 [30-4A-305]. As stated above, Intermediary Bank is entitled to compensation for loss and expenses resulting from the error by Originator's Bank.

Case #2. Suppose the same payment order by Originator to Originator's Bank as in Case #1. In executing the payment order Originator's Bank issues a payment order to Intermediary Bank in which the beneficiary's bank is identified only by number, #67890. That number does not refer to Bank A. Rather, it identifies a person that is not a bank. If processing by Intermediary Bank of the payment order of Originator's Bank is done by automated means, Intermediary Bank will rely on the number #67890 to identify the beneficiary's bank. Intermediary Bank has no duty to determine whether the number identifies a bank. The funds transfer cannot be completed in this case because no bank is identified as the beneficiary's bank. Subsection (a) [subsection (1) of this section] puts the risk of loss on Originator's Bank. Originator's Bank is not entitled to payment from Originator. Section 4A-402(c) [30-4A-402(3)]. Originator's Bank has improperly executed Originator's payment order and may be liable for damages under Section 4A-305 [30-4A-305].

Originator's Bank is obliged to compensate Intermediary Bank for loss and expenses resulting from the error by Originator's Bank.

Subsection (a) [subsection (1) of this section] also applies if #67890 identifies a bank, but the bank is not Bank A. Intermediary Bank may rely on the number as the proper identification of the beneficiary's bank. If the bank to which Intermediary Bank sends its payment order accepts the order, Intermediary Bank is entitled to payment from Originator's Bank, but Originator's Bank is not entitled to payment from Originator. The analysis is similar to that in Case #1.

2. Subsection (b)(2) of Section 4A-208 [30-4A-208(2)(b)] addresses cases in which an erroneous identification of a beneficiary's bank or intermediary bank by name and number is made in a payment order of a sender that is not a bank. Suppose Originator issues a payment order to Originator's Bank that instructs that bank to use an intermediary bank identified as Bank A and by an identifying number, #67890. The identifying number refers to Bank B. Originator intended to identify Bank A as intermediary bank. If Originator's Bank relied on the number and issued a payment order to Bank B the rights of Originator's Bank depend upon whether the proof of notice stated in subsection (b)(2) [subsection (2)(b) of this section] is made by Originator's Bank. If proof is made, Originator's Bank's rights are governed by subsection (b)(1) of Section 4A-208 [subsection (2)(a) of this section]. Originator's Bank is not liable for breach of Section 4A-302(a)(1) [30-4A-302(1)(a)] and is entitled to compensation from Originator for any loss and expenses resulting from Originator's error. If notice is not proved, Originator's Bank may not rely on the number in executing Originator's payment order. Since Originator's Bank does not get the benefit of subsection (b)(1) [subsection (2)(a) of this section] in that case, Originator's Bank improperly executed Originator's payment order and is in breach of the obligation stated in Section 4A-302(a)(1) [30-4A-302(1)(a)]. If notice is not given, Originator's Bank can rely on the name if it is not aware of the conflict in name and number. Subsection (b)(3) [subsection (2)(c) of this section].

3. Although the principal purpose of Section 4A-208 [30-4A-208] is to accommodate automated processing of payment orders, Section 4A-208 [30-4A-208] applies regardless of whether processing is done by automation, semi-automated means or manually.

30-4A-209. Acceptance of payment order.

Official Comment

Source: Section 4A-209, U.C.C.

Official Comment:

1. This section treats the sender's payment order as a request by the sender to the receiving bank to execute or pay the order and that request can be accepted or rejected by the receiving bank. Section 4A-209 [30-4A-209] defines when acceptance occurs. Section 4A-210 [30-4A-210] covers rejection. Acceptance of the payment order imposes an obligation on the receiving bank to the sender if the receiving bank is not the beneficiary's bank, or to the beneficiary if the receiving bank is the beneficiary's bank. These obligations are stated in Section 4A-302 [30-4A-302] and Section 4A-404 [30-4A-404].

2. Acceptance by a receiving bank other than the beneficiary's bank is defined in Section 4A-209(a) [30-4A-209(1)]. That subsection states the only way that a bank other than the beneficiary's bank can accept a payment order. A payment order to a bank other than the beneficiary's bank is, in effect, a request that the receiving bank execute the sender's order by issuing a payment order to the beneficiary's bank or to an intermediary bank. Normally, acceptance occurs at the time of execution, but there is an exception stated in subsection (d) [subsection (4) of this section] and discussed in Comment 9. Execution occurs when the receiving bank "issues a payment order intended to carry out" the sender's order. Section 4A-301(a) [30-4A-301(1)]. In some cases the payment order issued by the receiving bank may not conform to the sender's order. For example, the receiving bank might make a mistake in the amount of its order, or the order might be issued to the wrong beneficiary's bank or for the benefit of the wrong beneficiary. In all of these cases there is acceptance of the sender's order by the bank when the receiving bank issues its order intended to carry out the sender's order, even though the bank's payment order does not in fact carry out the instruction of the sender. Improper execution of the sender's order may lead to liability to the sender for damages or it may mean that the sender is not obliged to pay its payment order. These matters are covered in Section 4A-303 [30-4A-303], Section 4A-305 [30-4A-305], and Section 4A-402 [30-4A-402].

3. A receiving bank has no duty to accept a payment order unless the bank makes an agreement, either before or after issuance of the payment order, to accept it, or acceptance is required by a funds transfer system rule. If the bank makes such an agreement it incurs a

contractual obligation based on the agreement and may be held liable for breach of contract if a failure to execute violates the agreement. In many cases a bank will enter into an agreement with its customer to govern the rights and obligations of the parties with respect to payment orders issued to the bank by the customer or, in cases in which the sender is also a bank, there may be a funds transfer system rule that governs the obligations of a receiving bank with respect to payment orders transmitted over the system. Such agreements or rules can specify the circumstances under which a receiving bank is obliged to execute a payment order and can define the extent of liability of the receiving bank for breach of the agreement or rule. Section 4A-305(d) [30-4A-305(4)] states the liability for breach of an agreement to execute a payment order.

4. In the case of a payment order issued to the beneficiary's bank, acceptance is defined in Section 4A-209(b) [30-4A-209(2)]. The function of a beneficiary's bank that receives a payment order is different from that of a receiving bank that receives a payment order for execution. In the typical case, the beneficiary's bank simply receives payment from the sender of the order, credits the account of the beneficiary and notifies the beneficiary of the credit. Acceptance by the beneficiary's bank does not create any obligation to the sender. Acceptance by the beneficiary's bank means that the bank is liable to the beneficiary for the amount of the order. Section 4A-404(a) [30-4A-404(1)]. There are three ways in which the beneficiary's bank can accept a payment order which are described in the following comments.

5. Under Section 4A-209(b)(1) [30-4A-209(2)(a)], the beneficiary's bank can accept a payment order by paying the beneficiary. In the normal case of crediting an account of the beneficiary, payment occurs when the beneficiary is given notice of the right to withdraw the credit, the credit is applied to a debt of the beneficiary, or "funds with respect to the order" are otherwise made available to the beneficiary. Section 4A-405(a) [30-4A-405(1)]. The quoted phrase covers cases in which funds are made available to the beneficiary as a result of receipt of a payment order for the benefit of the beneficiary but the release of funds is not expressed as payment of the order. For example, the beneficiary's bank might express a release of funds equal to the amount of the order as a "loan" that will be automatically repaid when the beneficiary's bank receives payment by the sender of the order. If the release of funds is designated as a loan pursuant to a routine practice of the bank, the release is conditional payment of the order rather than a loan, particularly if normal incidents of a loan such as the signing of a loan agreement or note and the payment of interest are not present. Such a release of funds is payment to the beneficiary under Section 4A-405(a) [30-4A-405(1)]. Under Section 4A-405(c) [30-4A-405(3)] the bank cannot recover the money from the beneficiary if the bank does not receive payment from the sender of the payment order that it accepted. Exceptions to this rule are stated in § 4A-405(d) and (e) [30-4A-405(4) and (5)]. The beneficiary's bank may also accept by notifying the beneficiary that the order has been received. "Notifies" is defined in Section 1-201(26) [30-1-201(26)]. In some cases a beneficiary's bank will receive a payment order during the day but settlement of the sender's obligation to pay the order will not occur until the end of the day. If the beneficiary's bank wants to defer incurring liability to the beneficiary until the beneficiary's bank receives payment, it can do so. The beneficiary's bank incurs no liability to the beneficiary with respect to a payment order that it receives until it accepts the order. If the bank does not accept pursuant to subsection (b)(1) [subsection (2)(a) of this section], acceptance does not occur until the end of the day when the beneficiary's bank receives settlement. If the sender settles, the payment order will be accepted under subsection (b)(2) [subsection (2)(b) of this section] and the funds will be released to the beneficiary the next morning. If the sender doesn't settle, no acceptance occurs. In either case the beneficiary's bank suffers no loss.

6. In most cases the beneficiary's bank will receive a payment order from another bank. If the sender is a bank and the beneficiary's bank receives payment from the sender by final settlement through the Federal Reserve System or a funds transfer system (Section 4A-403(a)(1) [30-4A-403(1)(a)]) or, less commonly, through credit to an account of the beneficiary's bank with the sender or another bank (Section 4A-403(a)(2) [30-4A-403(1)(b)]), acceptance by the beneficiary's bank occurs at the time payment is made. Section 4A-209(b)(2) [subsection (2)(b) of this section]. A minor exception to this rule is stated in Section 4A-209(c) [30-4A-209(3)]. Section 4A-209(b)(2) [30-4A-209(2)(b)] results in automatic acceptance of payment orders issued to a beneficiary's bank by means of Fedwire because the Federal Reserve account of the beneficiary's bank is credited and final payment is made to that bank when the payment order is received.

Subsection (b)(2) [subsection (2)(b) of this section] would also apply to cases in which the beneficiary's bank mistakenly pays a person who is not the beneficiary of the payment order issued to the beneficiary's bank. For example, suppose the payment order provides for immediate payment to Account #12345. The beneficiary's bank erroneously credits Account #12346 and notifies the holder of that account of the credit. No acceptance occurs in this case under subsection (b)(1) [subsection (2)(a) of this section] because the beneficiary of the order has not been paid or notified. The holder of Account #12345 is the beneficiary of the order issued to the beneficiary's bank. But acceptance will normally occur if the beneficiary's bank takes no other action, because the bank will normally receive settlement with respect to the payment order. At that time the bank has accepted because the sender paid its payment order. The bank is liable to pay the holder of Account #12345. The bank has paid the holder of Account #12346 by mistake, and has a right to recover the payment if the credit is withdrawn, to the extent provided in the law governing mistake and restitution.

7. Subsection (b)(3) [subsection (2)(c) of this section] covers cases of inaction by the beneficiary's bank. It applies whether or not the sender is a bank and covers a case in which the sender and the beneficiary both have accounts with the receiving bank and payment will be made by debiting the account of the sender and crediting the account of the beneficiary. Subsection (b)(3) [subsection (2)(c) of this section] is similar to subsection (b)(2) [subsection (2)(b) of this section] in that it bases acceptance by the beneficiary's bank on payment by the sender. Payment by the sender is effected by a debit to the sender's account if the account balance is sufficient to cover the amount of the order. On the payment date (Section 4A-401 [30-4A-401]) of the order the beneficiary's bank will normally credit the beneficiary's account and notify the beneficiary of receipt of the order if it is satisfied that the sender's account balance covers the order or is willing to give credit to the sender. In some cases, however, the bank may not be willing to give credit to the sender and it may not be possible for the bank to determine until the end of the day on the payment date whether there are sufficient good funds in the sender's account. There may be various transactions during the day involving funds going into and out of the account. Some of these transactions may occur late in the day or after the close of the banking day. To accommodate this situation, subsection (b)(3) [subsection (2)(c) of this section] provides that the status of the account is determined at the opening of the next funds transfer business day of the beneficiary's bank after the payment date of the order. If the sender's account balance is sufficient to cover the order, the beneficiary's bank has a source of payment and the result in almost all cases is that the bank accepts the order at that time if it did not previously accept under subsection (b)(1) [subsection (2)(a) of this section]. In rare cases, a bank may want to avoid acceptance under subsection (b)(3) [subsection (2)(c) of this section] by rejecting the order as discussed in Comment 8.

8. Section 4A-209 [30-4A-209] is based on a general principle that a receiving bank is not obliged to accept a payment order unless it has agreed or is bound by a funds transfer system rule to do so. Thus, provision is made to allow the receiving bank to prevent acceptance of the order. This principle is consistently followed if the receiving bank is not the beneficiary's bank. If the receiving bank is not the beneficiary's bank, acceptance is in the control of the receiving bank because it occurs only if the order is executed. But in the case of the beneficiary's bank acceptance can occur by passive receipt of payment under subsection (b)(2) or (3) [subsection (2)(b) or (2)(c) of this section]. In the case of a payment made by Fedwire acceptance cannot be prevented. In other cases the beneficiary's bank can prevent acceptance by giving notice of rejection to the sender before payment occurs under Section 4A-403(a)(1) or (2) [30-4A-403(1)(a) or (1)(b)]. A minor exception to the ability of the beneficiary's bank to reject is stated in Section 4A-502(c)(3) [30-4A-502(3)(c)].

Under subsection (b)(3) [subsection (2)(c) of this section] acceptance occurs at the opening of the next funds transfer business day of the beneficiary's bank following the payment date unless the bank rejected the order before that time or it rejects within one hour after that time. In some cases the sender and the beneficiary's bank may not be in the same time zone or the beginning of the business day of the sender and the funds transfer business day of the beneficiary's bank may not coincide. For example, the sender may be located in California and the beneficiary's bank in New York. Since in most cases notice of rejection would be communicated electronically or by telephone, it might not be feasible for the bank to give notice before one hour after the opening of the funds transfer business day in New York because at that hour, the sender's business day may not have started in California. For that reason, there are alternative deadlines stated in subsection (b)(3) [subsection (2)(c) of this section]. In the case stated, the bank acts in time if it gives notice within one hour after the opening of the business day of the sender. But if the notice of rejection is received by the sender after the payment date, the bank is obliged to pay interest to the sender if the sender's account does not bear interest. In that case the bank had the use of funds of the sender that the sender could reasonably assume would be used to pay the beneficiary. The rate of interest is stated in Section 4A-506 [30-4A-506]. If the sender receives notice on the day after the payment date the sender is entitled to one day's interest. If receipt of notice is delayed for more than one day, the sender is entitled to interest for each additional day of delay.

9. Subsection (d) [subsection (4) of this section] applies only to a payment order by the originator of a funds transfer to the originator's bank and it refers to the following situation. On April 1, Originator instructs Bank A to make a payment on April 15 to the account of Beneficiary in Bank B. By mistake, on April 1, Bank A executes Originator's payment order by issuing a payment order to Bank B instructing immediate payment to Beneficiary. Bank B credited Beneficiary's account and immediately released the funds to Beneficiary. Under subsection (d) [subsection (4) of this section] no acceptance by Bank A occurred on April 1 when Originator's payment order was executed because acceptance cannot occur before the execution date which in this case would be April 15 or shortly before that date. Section 4A-301(b) [30-4A-301(2)]. Under Section 4A-402(c) [30-4A-402(3)], Originator is not obliged to pay Bank A until the order is accepted and that can't occur until the execution date. But Bank A is required to pay Bank B when Bank B accepted Bank A's order on April 1. Unless Originator and Beneficiary are the same person, in almost all cases Originator is paying a debt owed to Beneficiary and early payment does not injure Originator because Originator does not have to pay Bank A until the execution date. Section 4A-402(c) [30-4A-402(3)]. Bank A takes the interest loss. But suppose that on April 3, Originator concludes that no debt was owed to Beneficiary or that the debt was less than the amount of the payment order. Under Section 4A-211(b) [30-4A-211(2)] Originator can cancel its payment order if Bank A has not accepted. If early execution of Originator's payment order is acceptance, Originator can suffer a loss because cancellation after acceptance is not possible without the consent of Bank A and Bank B. Section 4A-211(c) [30-4A-211(3)]. If Originator has to pay Bank A, Originator would be required to seek recovery of the money from Beneficiary. Subsection (d) [subsection (4) of this section] prevents this result and puts the risk of loss on Bank A by providing that the early execution does not result in acceptance until the execution date. Since on April 3 Originator's order was not yet accepted, Originator can cancel it under Section 4A-211(b) [30-4A-211(2)]. The result is that Bank A is not entitled to payment from Originator but is obliged to pay Bank B. Bank A has paid Beneficiary by mistake. If Originator's payment order is cancelled, Bank A becomes the originator of an erroneous funds transfer to Beneficiary. Bank A has the burden of recovering payment from Beneficiary on the basis of a payment by mistake. If Beneficiary received the money in good faith in payment of a debt owed to Beneficiary by Originator, the law of mistake and restitution may allow Beneficiary to keep all or part of the money received. If Originator owed money to Beneficiary, Bank A has paid Originator's debt and, under the law of restitution, which applies pursuant to Section 1-103 [30-1-103], Bank A is subrogated to Beneficiary's rights against Originator on the debt.

If Bank A is the Beneficiary's bank and Bank A credited Beneficiary's account and released the funds to Beneficiary on April 1, the analysis is similar. If Originator's order is cancelled, Bank A has paid Beneficiary by mistake. The right of Bank A to recover the payment from Beneficiary is similar to Bank A's rights in the preceding paragraph.

30-4A-210. Rejection of payment order.

Official Comment

Source: Section 4A-210, U.C.C.

Official Comment:

1. With respect to payment orders issued to a receiving bank other than the beneficiary's bank, notice of rejection is not necessary to prevent acceptance of the order. Acceptance can occur only if the receiving bank executes the order. Section 4A-209(a) [30-4A-209(1)]. But notice of rejection will routinely be given by such a bank in cases in which the bank cannot or is not willing to execute the order for some reason. There are many reasons why a bank doesn't execute an order. The payment order may not clearly instruct the receiving bank because of some ambiguity in the order or an internal inconsistency. In some cases, the receiving bank may not be able to carry out the instruction because of equipment failure, credit limitations on the receiving bank, or some other factor which makes proper execution of the order infeasible. In those cases notice of rejection is a means of informing the sender of the facts so that a corrected payment order can be transmitted or the sender can seek alternate means of completing the funds transfer. The other major reason for not executing an order is that the sender's account is insufficient to cover the order and the receiving bank is not willing to give credit to the sender. If the sender's account is sufficient to cover the order and the receiving bank chooses not to execute the order, notice

of rejection is necessary to prevent liability to pay interest to the sender if the case falls within Section 4A-210(b) [30-4A-210(2)] which is discussed in Comment 3.

2. A payment order to the beneficiary's bank can be accepted by inaction of the bank. Section 4A-209(b)(2) and (3) [30-4A-209(2)(b) and (2)(c)]. To prevent acceptance under those provisions it is necessary for the receiving bank to send notice of rejection before acceptance occurs. Subsection (a) of Section 4A-210 [30-4A-210(1)] states the rule that rejection is accomplished by giving notice of rejection. This incorporates the definitions in Section 1-201(26) [30-1-201(26)]. Rejection is effective when notice is given if it is given by a means that is reasonable in the circumstances. Otherwise, it is effective when the notice is received. The question of when rejection is effective is important only in the relatively few cases under subsection (b)(2) and (3) [subsection (2)(b) and (2)(c) of this section] in which a notice of rejection is necessary to prevent acceptance. The question of whether a particular means is reasonable depends on the facts in a particular case. In a very large percentage of cases the sender and the receiving bank will be in direct electronic contact with each other and in those cases a notice of rejection can be transmitted instantaneously. Since time is of the essence in a large proportion of funds transfers, some quick means of transmission would usually be required, but this is not always the case. The parties may specify by agreement the means by which communication between the parties is to be made.

3. Subsection (b) [subsection (2) of this section] deals with cases in which a sender does not learn until after the execution date that the sender's order has not been executed. It applies only to cases in which the receiving bank was assured of payment because the sender's account was sufficient to cover the order. Normally, the receiving bank will accept the sender's order if it is assured of payment, but there may be some cases in which the bank chooses to reject. Unless the receiving bank had obligated itself by agreement to accept, the failure to accept is not wrongful. There is no duty of the receiving bank to accept the payment order unless it is obliged to accept by express agreement. Section 4A-212 [30-4A-212]. But even if the bank has not acted wrongfully, the receiving bank had the use of the sender's money that the sender could reasonably assume was to be the source of payment of the funds transfer. Until the sender learns that the order was not accepted the sender is denied the use of that money. Subsection (b) [subsection (2) of this section] obliges the receiving bank to pay interest to the sender as restitution unless the sender receives notice of rejection on the execution date. The time of receipt of notice is determined pursuant to § 1-201(27) [30-1-201(27)]. The rate of interest is stated in Section 4A-506 [30-4A-506]. If the sender receives notice on the day after the execution date, the sender is entitled to one day's interest. If receipt of notice is delayed for more than one day, the sender is entitled to interest for each additional day of delay.

4. Subsection (d) [subsection (4) of this section] treats acceptance and rejection as mutually exclusive. If a payment order has been accepted, rejection of that order becomes impossible. If a payment order has been rejected it cannot be accepted later by the receiving bank. Once notice of rejection has been given, the sender may have acted on the notice by making the payment through other channels. If the receiving bank wants to act on a payment order that it has rejected it has to obtain the consent of the sender. In that case the consent of the sender would amount to the giving of a second payment order that substitutes for the rejected first order. If the receiving bank suspends payments (Section 4-104(1)(k) [30-4-104(1)(k)]), subsection (c) [subsection (3) of this section] provides that unaccepted payment orders are deemed rejected at the time suspension of payments occurs. This prevents acceptance by passage of time under Section 4A-209(b)(3) [30-4A-209(2)(c)].

30-4A-211. Cancellation and amendment of payment order.

Official Comment

Source: Section 4A-211, U.C.C.

Official Comment:

1. This section deals with cancellation and amendment of payment orders. It states the conditions under which cancellation or amendment is both effective and rightful. There is no concept of wrongful cancellation or amendment of a payment order. If the conditions stated in this section are not met the attempted cancellation or amendment is not effective. If the stated conditions are met the cancellation or amendment is effective and rightful. The sender of a payment order may want to withdraw or change the order because the sender has had a change of mind about the transaction or because the payment order was erroneously issued or for any other reason. One common situation is that of multiple transmission of the same order. The sender that mistakenly transmits the same order twice wants to correct the mistake by cancelling the duplicate order. Or, a sender may have intended to order a payment of $1,000,000

but mistakenly issued an order to pay $10,000,000. In this case the sender might try to correct the mistake by cancelling the order and issuing another order in the proper amount. Or, the mistake could be corrected by amending the order to change it to the proper amount. Whether the error is corrected by amendment or cancellation and reissue the net result is the same. This result is stated in the last sentence of subsection (e) [subsection (5) of this section].

2. Subsection (a) [subsection (1) of this section] allows a cancellation or amendment of a payment order to be communicated to the receiving bank "orally, electronically, or in writing." The quoted phrase is consistent with the language of Section 4A-103(a) [30-4A-103(1)] applicable to payment orders. Cancellations and amendments are normally subject to verification pursuant to security procedures to the same extent as payment orders. Subsection (a) [subsection (1) of this section] recognizes this fact by providing that in cases in which there is a security procedure in effect between the sender and the receiving bank the bank is not bound by a communication cancelling or amending an order unless verification has been made. This is necessary to protect the bank because under subsection (b) [subsection (2) of this section] a cancellation or amendment can be effective by unilateral action of the sender. Without verification the bank cannot be sure whether the communication was or was not effective to cancel or amend a previously verified payment order.

3. If the receiving bank has not yet accepted the order, there is no reason why the sender should not be able to cancel or amend the order unilaterally so long as the requirements of subsections (a) and (b) [subsections (1) and (2) of this section] are met. If the receiving bank has accepted the order, it is possible to cancel or amend but only if the requirements of subsection (c) [subsection (3) of this section] are met.

First consider the case of a receiving bank other than the beneficiary's bank. If the bank has not yet accepted the order, the sender can unilaterally cancel or amend. The communication amending or cancelling the payment order must be received in time to allow the bank to act on it before the bank issues its payment order in execution of the sender's order. The time that the sender's communication is received is governed by Section 4A-106 [30-4A-106]. If a payment order does not specify a delayed payment date or execution date, the order will normally be executed shortly after receipt. Thus, as a practical matter, the sender will have very little time in which to instruct cancellation or amendment before acceptance. In addition, a receiving bank will normally have cut-off times for receipt of such communications, and the receiving bank is not obliged to act on communications received after the cut-off hour. Cancellation by the sender after execution of the order by the receiving bank requires the agreement of the bank unless a funds transfer rule otherwise provides. Subsection (c) [subsection (3) of this section]. Although execution of the sender's order by the receiving bank does not itself impose liability on the receiving bank (under Section 4A-402 [30-4A-402] no liability is incurred by the receiving bank to pay its order until it is accepted), it would commonly be the case that acceptance follows shortly after issuance. Thus, as a practical matter, a receiving bank that has executed a payment order will incur a liability to the next bank in the chain before it would be able to act on the cancellation request of its customer. It is unreasonable to impose on the receiving bank a risk of loss with respect to a cancellation request without the consent of the receiving bank.

The statute does not state how or when the agreement of the receiving bank must be obtained for cancellation after execution. The receiving bank's consent could be obtained at the time cancellation occurs or it could be based on a preexisting agreement. Or, a funds transfer system rule could provide that cancellation can be made unilaterally by the sender. By virtue of that rule any receiving bank covered by the rule is bound. Section 4A-501 [30-4A-501]. If the receiving bank has already executed the sender's order, the bank would not consent to cancellation unless the bank to which the receiving bank has issued its payment order consents to cancellation of that order. It makes no sense to allow cancellation of a payment order unless all subsequent payment orders in the funds transfer that were issued because of the cancelled payment order are also cancelled. Under subsection (c)(1) [subsection (3)(a) of this section], if a receiving bank consents to cancellation of the payment order after it has [sic] executed, the cancellation is not effective unless the receiving bank also cancels the payment order issued by the bank.

4. With respect to a payment order issued to the beneficiary's bank, acceptance is particularly important because it creates liability to pay the beneficiary, it defines when the originator pays its obligation to the beneficiary, and it defines when any obligation for which the payment is made is discharged. Since acceptance affects the rights of the originator and the beneficiary it is not appropriate to allow the beneficiary's bank to agree to cancellation or amendment except in unusual cases. Except as provided in subsection (c)(2) [subsection (3)(b) of this section], cancellation or amendment after acceptance by the beneficiary's bank is not possible unless all

parties affected by the order agree. Under subsection (c)(2) [subsection (3)(b) of this section], cancellation or amendment is possible only in the four cases stated. The following examples illustrate subsection (c)(2) [subsection (3)(b) of this section]:

Case #1. Originator's Bank executed a payment order issued in the name of its customer as sender. The order was not authorized by the customer and was fraudulently issued. Beneficiary's Bank accepted the payment order issued by Originator's Bank. Under subsection (c)(2) [subsection (3)(b) of this section] Originator's Bank can cancel the order if Beneficiary's Bank consents. It doesn't make any difference whether the payment order that Originator's Bank accepted was or was not enforceable against the customer under Section 4A-202(b) [30-4A-202(2)]. Verification under that provision is important in determining whether Originator's Bank or the customer has the risk of loss, but it has no relevance under Section 4A-211(c)(2) [30-4A-211(3)(b)]. Whether or not verified, the payment order was not authorized by the customer. Cancellation of the payment order to Beneficiary's Bank causes the acceptance of Beneficiary's Bank to be nullified. Subsection (e) [subsection (5) of this section]. Beneficiary's Bank is entitled to recover payment from the beneficiary to the extent allowed by the law of mistake and restitution. In this kind of case the beneficiary is usually a party to the fraud who has no right to receive or retain payment of the order.

Case #2. Originator owed Beneficiary $1,000,000 and ordered Bank A to pay that amount to the account of Beneficiary in Bank B. Bank A issued a complying order to Bank B, but by mistake issued a duplicate order as well. Bank B accepted both orders. Under subsection (c)(2)(i) [subsection (3)(b)(i)(A) of this section] cancellation of the duplicate order could be made by Bank A with the consent of Bank B. Beneficiary has no right to receive or retain payment of the duplicate payment order if only $1,000,000 was owed by Originator to Beneficiary. If Originator owed $2,000,000 to Beneficiary, the law of restitution might allow Beneficiary to retain the $1,000,000 paid by Bank B on the duplicate order. In that case Bank B is entitled to reimbursement from Bank A under subsection (f) [subsection (6) of this section].

Case #3. Originator owed $1,000,000 to X. Intending to pay X, Originator ordered Bank A to pay $1,000,000 to Y's account in Bank B. Bank A issued a complying payment order to Bank B which Bank B accepted by releasing the $1,000,000 to Y. Under subsection (c)(2)(ii) [subsection (3)(b)(i)(B) of this section] Bank A can cancel its payment order to Bank B with the consent of Bank B if Y was not entitled to receive payment from Originator. Originator can also cancel its order to Bank A with Bank A's consent. Subsection (c) (1) [subsection (3)(a) of this section]. Bank B may recover the $1,000,000 from Y unless the law of mistake and restitution allows Y to retain some or all of the amount paid. If no debt was owed to Y, Bank B should have a right of recovery.

Case #4. Originator owed Beneficiary $10,000. By mistake Originator ordered Bank A to pay $1,000,000 to the account of Beneficiary in Bank B. Bank A issued a complying order to Bank B which accepted by notifying Beneficiary of its right to withdraw $1,000,000. Cancellation is permitted in this case under subsection (c)(2)(iii) [subsection (3)(b)(i)(C) of this section]. If Bank B paid Beneficiary it is entitled to recover the payment except to the extent the law of mistake and restitution allows Beneficiary to retain payment. In this case Beneficiary might be entitled to retain $10,000, the amount of the debt owed to Beneficiary. If Beneficiary may retain $10,000, Bank B would be entitled to $10,000 from Bank A pursuant to subsection (f) [subsection (6) of this section]. In this case Originator also cancelled its order. Thus Bank A would be entitled to $10,000 from Originator pursuant to subsection (f) [subsection (6) of this section].

5. Unless constrained by a funds transfer system rule, a receiving bank may agree to cancellation or amendment of the payment order under subsection (c) [subsection (3) of this section] but is not required to do so regardless of the circumstances. If the receiving bank has incurred liability as a result of its acceptance of the sender's order, there are substantial risks in agreeing to cancellation or amendment. This is particularly true for a beneficiary's bank. Cancellation or amendment after acceptance by the beneficiary's bank can be made only in the four cases stated and the beneficiary's bank may not have any way of knowing whether the requirements of subsection (c) [subsection (3) of this section] have been met or whether it will be able to recover payment from the beneficiary that received payment. Even with indemnity the beneficiary's bank may be reluctant to alienate its customer, the beneficiary, by denying the customer the funds. Subsection (c) [subsection (3) of this section] leaves the decision to the beneficiary's bank unless the consent of the beneficiary's bank is not required under a funds transfer system rule or other interbank agreement. If a receiving bank agrees to cancellation or amendment under subsection (c)(1) or (2) [subsection (3)(a) or (3)(b) of this section], it is automatically entitled to indemnification from the sender under subsection (f) [subsection (6) of this section]. The indemnification provision recognizes that a sender has no right to cancel a payment order after it

is accepted by the receiving bank. If the receiving bank agrees to cancellation, it is doing so as an accommodation to the sender and it should not incur a risk of loss in doing so.

6. Acceptance by the receiving bank of a payment order issued by the sender is comparable to acceptance of an offer under the law of contracts. Under that law the death or legal incapacity of an offeror terminates the offer even though the offeree has no notice of the death or incapacity. Restatement Second, Contracts § 48. Comment a. to that section states that the "rule seems to be a relic of the obsolete view that a contract requires a 'meeting of minds,' and it is out of harmony with the modern doctrine that a manifestation of assent is effective without regard to actual mental assent." Subsection (g) [subsection (7) of this section], which reverses the Restatement rule in the case of a payment order, is similar to Section 4-405(1) [30-4-405(1)] which applies to checks. Subsection (g) [subsection (7) of this section] does not address the effect of the bankruptcy of the sender of a payment order before the order is accepted, but the principle of subsection (g) [subsection (7) of this section] has been recognized in Bank of Marin v. England, 385 U.S. 99 (1966). Although Bankruptcy Code Section 542(c) may not have been drafted with wire transfers in mind, its language can be read to allow the receiving bank to charge the sender's account for the amount of the payment order if the receiving bank executed it in ignorance of the bankruptcy.

7. Subsection (d) [subsection (4) of this section] deals with stale payment orders. Payment orders normally are executed on the execution date or the day after. An order issued to the beneficiary's bank is normally accepted on the payment date or the day after. If a payment order is not accepted on its execution or payment date or shortly thereafter, it is probable that there was some problem with the terms of the order or the sender did not have sufficient funds or credit to cover the amount of the order. Delayed acceptance of such an order is normally not contemplated, but the order may not have been cancelled by the sender. Subsection (d) [subsection (4) of this section] provides for cancellation by operation of law to prevent an unexpected delayed acceptance.

8. A funds transfer system rule can govern rights and obligations between banks that are parties to payment orders transmitted over the system even if the rule conflicts with Article 4A [Title 30, chapter 4A]. In some cases, however, a rule governing a transaction between two banks can affect a third party in an unacceptable way. Subsection (h) [subsection (8) of this section] deals with such a case. A funds transfer system rule cannot allow cancellation of a payment order accepted by the beneficiary's bank if the rule conflicts with subsection (c)(2) [subsection (3)(b) of this section]. Because rights of the beneficiary and the originator are directly affected by acceptance, subsection (c)(2) [subsection (3)(b) of this section] severely limits cancellation. These limitations cannot be altered by funds transfer system rule.

30-4A-212. Liability and duty of receiving bank regarding unaccepted payment order.

Official Comment

Source: Section 4A-212, U.C.C.

Official Comment:

With limited exceptions stated in this Article, the duties and obligations of receiving banks that carry out a funds transfer arise only as a result of acceptance of payment orders or of agreements made by receiving banks. Exceptions are stated in Section 4A-209(b)(3) [30-4A-209(2)(c)] and Section 4A-210(b) [30-4A-210(2)]. A receiving bank is not like a collecting bank under Article 4 [Title 30, chapter 4]. No receiving bank, whether it be an originator's bank, an intermediary bank or a beneficiary's bank, is an agent for any other party in the funds transfer.

Part 3

Execution of Sender's Payment Order by Receiving Bank

30-4A-301. Execution and execution date.

Official Comment

Source: Section 4A-301, U.C.C.

Official Comment:

1. The terms "executed," "execution" and "execution date" are used only with respect to a payment order to a receiving bank other than the beneficiary's bank. The beneficiary's bank can accept the payment order that it receives, but it does not execute the order. Execution refers to the act of the receiving bank in issuing a payment order "intended to carry out" the payment order that the bank received. A receiving bank has executed an order even if the order issued by the bank does not carry out the order received by the bank. For example, the bank may have erroneously issued an order to the wrong beneficiary, or in the wrong amount or to the wrong

beneficiary's bank. In each of these cases execution has occurred but the execution is erroneous. Erroneous execution is covered in Section 4A-303 [30-4A-303].

2. "Execution date" refers to the time a payment order should be executed rather than the day it is actually executed. Normally the sender will not specify an execution date, but most payment orders are meant to be executed immediately. Thus, the execution date is normally the day the order is received by the receiving bank. It is common for the sender to specify a "payment date" which is defined in Section 4A-401 [30-4A-401] as "the day on which the amount of the order is payable to the beneficiary by the beneficiary's bank." Except for automated clearing house transfers, if a funds transfer is entirely within the United States and the payment is to be carried out electronically, the execution date is the payment date unless the order is received after the payment date. If the payment is to be carried out through an automated clearing house, execution may occur before the payment date. In an ACH transfer the beneficiary is usually paid one or two days after issue of the originator's payment order. The execution date is determined by the stated payment date and is a date before the payment date on which execution is reasonably necessary to allow payment on the payment date. A funds transfer system rule could also determine the execution date of orders received by the receiving bank if both the sender and the receiving bank are participants in the funds transfer system. The execution date can be determined by the payment order itself or by separate instructions of the sender or an agreement of the sender and the receiving bank. The second sentence of subsection (b) [subsection (2) of this section] must be read in the light of Section 4A-106 [30-4A-106] which states that if a payment order is received after the cut-off time of the receiving bank it may be treated by the bank as received at the opening of the next funds transfer business day.

3. Execution on the execution date is timely, but the order can be executed before or after the execution date. Section 4A-209(d) [30-4A-209(4)] and Section 4A-402(c) [30-4A-402(3)] state the consequences of early execution and Section 4A-305(a) [30-4A-305(1)] states the consequences of late execution.

30-4A-302. Obligations of receiving bank in execution of payment order.

Official Comment

Source: Section 4A-302, U.C.C.

Official Comment:

1. In the absence of agreement, the receiving bank is not obliged to execute an order of the sender. Section 4A-212 [30-4A-212]. Section 4A-302 [30-4A-302] states the manner in which the receiving bank may execute the sender's order if execution occurs. Subsection (a)(1) [subsection (1)(a) of this section] states the residual rule. The payment order issued by the receiving bank must comply with the sender's order and, unless some other rule is stated in the section, the receiving bank is obliged to follow any instruction of the sender concerning which funds transfer system is to be used, which intermediary banks are to be used, and what means of transmission is to be used. The instruction of the sender may be incorporated in the payment order itself or may be given separately. For example, there may be a master agreement between the sender and receiving bank containing instructions governing payment orders to be issued from time to time by the sender to the receiving bank. In most funds transfers, speed is a paramount consideration. A sender that wants assurance that the funds transfer will be expeditiously completed can specify the means to be used. The receiving bank can follow the instructions literally or it can use an equivalent means. For example, if the sender instructs the receiving bank to transmit by telex, the receiving bank could use telephone instead. Subsection (c) [subsection (3) of this section]. In most cases the sender will not specify a particular means but will use a general term such as "by wire" or "wire transfer" or "as soon as possible." These words signify that the sender wants a same-day transfer. In these cases the receiving bank is required to use a telephonic or electronic communication to transmit its order and is also required to instruct any intermediary bank to which it issues its order to transmit by similar means. Subsection (a)(2) [subsection (1)(b) of this section]. In other cases, such as an automated clearing house transfer, a same-day transfer is not contemplated. Normally the sender's instruction or the context in which the payment order is received makes clear the type of funds transfer that is appropriate. If the sender states a payment date with respect to the payment order, the receiving bank is obliged to execute the order at a time and in a manner to meet the payment date if that is feasible. Subsection (a)(2) [subsection (1)(b) of this section]. This provision would apply to many ACH transfers made to pay recurring debts of the sender. In other cases, involving relatively small amounts, time may not be an important factor and cost may be a more important element. Fast means, such as telephone or electronic transmission, are more expensive than slow means such as mailing. Subsection

(c) [subsection (3) of this section] states that in the absence of instructions the receiving bank is given discretion to decide. It may issue its payment order by first class mail or by any means reasonable in the circumstances. Section 4A-305 [30-4A-305] states the liability of a receiving bank for breach of the obligations stated in Section 4A-302 [30-4A-302].

2. Subsection (b) [subsection (2) of this section] concerns the choice of intermediary banks to be used in completing the funds transfer, and the funds transfer system to be used. If the receiving bank is not instructed about the matter, it can issue an order directly to the beneficiary's bank or can issue an order to an intermediary bank. The receiving bank also has discretion concerning use of a funds transfer system. In some cases it may be reasonable to use either an automated clearing house system or a wire transfer system such as Fedwire or CHIPS. Normally, the receiving bank will follow the instruction of the sender in these matters, but in some cases it may be prudent for the bank not to follow instructions. The sender may have designated a funds transfer system to be used in carrying out the funds transfer, but it may not be feasible to use the designated system because of some impediment such as a computer breakdown which prevents prompt execution of the order. The receiving bank is permitted to use an alternate means of transmittal in a good faith effort to execute the order expeditiously. The same leeway is not given to the receiving bank if the sender designates an intermediary bank through which the funds transfer is to be routed. The sender's designation of that intermediary bank may mean that the beneficiary's bank is expecting to obtain a credit from that intermediary bank and may have relied on that anticipated credit. If the receiving bank uses another intermediary bank the expectations of the beneficiary's bank may not be realized. The receiving bank could choose to route the transfer to another intermediary bank and then to the designated intermediary bank if there were some reason such as a lack of a correspondent-bank relationship or a bilateral credit limitation, but the designated intermediary bank cannot be circumvented. To do so violates the sender's instructions.

3. The normal rule, under subsection (a)(1) [subsection (1)(a) of this section], is that the receiving bank, in executing a payment order, is required to issue a payment order that complies as to amount with that of the sender's order. In most cases the receiving bank issues an order equal to the amount of the sender's order and makes a separate charge for services and expenses in executing the sender's order. In some cases, particularly if it is an intermediary bank that is executing an order, charges are collected by deducting them from the amount of the payment order issued by the executing bank. If that is done, the amount of the payment order accepted by the beneficiary's bank will be slightly less than the amount of the originator's payment order. For example, Originator, in order to pay an obligation of $1,000,000 owed to Beneficiary, issues a payment order to Originator's Bank to pay $1,000,000 to the account of Beneficiary in Beneficiary's Bank. Originator's Bank issues a payment order to Intermediary Bank for $1,000,000 and debits Originator's account for $1,000,010. The extra $10 is the fee of Originator's Bank. Intermediary Bank executes the payment order of Originator's Bank by issuing a payment order to Beneficiary's Bank for $999,990, but under Section 4A-402(c) [30-4A-402(3)] is entitled to receive $1,000,000 from Originator's Bank. The $10 difference is the fee of Intermediary Bank. Beneficiary's Bank credits Beneficiary's account for $999,990. When Beneficiary's Bank accepts the payment order of Intermediary Bank the result is a payment of $999,990 from Originator to Beneficiary. Section 4A-406(a) [30-4A-406(1)]. If that payment discharges the $1,000,000 debt, the effect is that Beneficiary has paid the charges of Intermediary Bank and Originator has paid the charges of Originator's Bank. Subsection (d) of Section 4A-302 [30-4A-302(4)] allows Intermediary Bank to collect its charges by deducting them from the amount of the payment order, but only if instructed to do so by Originator's Bank. Originator's Bank is not authorized to give that instruction to Intermediary Bank unless Originator authorized the instruction. Thus, Originator can control how the charges of Originator's Bank and Intermediary Bank are to be paid. Subsection (d) [subsection (4) of this section] does not apply to charges of Beneficiary's Bank to Beneficiary.

In the case discussed in the preceding paragraph the $10 charge is trivial in relation to the amount of the payment and it may not be important to Beneficiary how the charge is paid. But it may be very important if the $1,000,000 obligation represented the price of exercising a right such as an option favorable to Originator and unfavorable to Beneficiary. Beneficiary might well argue that it was entitled to receive $1,000,000. If the option was exercised shortly before its expiration date, the result could be loss of the option benefit because the required payment of $1,000,000 was not made before the option expired. Section 4A-406(c) [30-4A-406(3)] allows Originator to preserve the option benefit. The amount received by Beneficiary is deemed to be $1,000,000 unless Beneficiary demands the $10 and Originator does not pay it.

30-4A-303. Erroneous execution of payment order.

Official Comment

Source: Section 4A-303, U.C.C.

Official Comment:

1. Section 4A-303 [30-4A-303] states the effect of erroneous execution of a payment order by the receiving bank. Under Section 4A-402(c) [30-4A-402(3)] the sender of a payment order is obliged to pay the amount of the order to the receiving bank if the bank executes the order, but the obligation to pay is excused if the beneficiary's bank does not accept a payment order instructing payment to the beneficiary of the sender's order. If erroneous execution of the sender's order causes the wrong beneficiary to be paid, the sender is not required to pay. If erroneous execution causes the wrong amount to be paid the sender is not obliged to pay the receiving bank an amount in excess of the amount of the sender's order. Section 4A-303 [30-4A-303] takes precedence over Section 4A-402(c) [30-4A-402(3)] and states the liability of the sender and the rights of the receiving bank in various cases of erroneous execution.

2. Subsections (a) and (b) [subsection (1) and (2) of this section] deal with cases in which the receiving bank executes by issuing a payment order in the wrong amount. If Originator ordered Originator's Bank to pay $1,000,000 to the account of Beneficiary in Beneficiary's Bank, but Originator's Bank erroneously instructed Beneficiary's Bank to pay $2,000,000 to Beneficiary's account, subsection (a) [subsection (1) of this section] applies. If Beneficiary's Bank accepts the order of Originator's Bank, Beneficiary's Bank is entitled to receive $2,000,000 from Originator's Bank, but Originator's Bank is entitled to receive only $1,000,000 from Originator. Originator's Bank is entitled to recover the overpayment from Beneficiary to the extent allowed by the law governing mistake and restitution. Originator's Bank would normally have a right to recover the overpayment from Beneficiary, but in unusual cases the law of restitution might allow Beneficiary to keep all or part of the overpayment. For example, if Originator owed $2,000,000 to Beneficiary and Beneficiary received the extra $1,000,000 in good faith in discharge of the debt, Beneficiary may be allowed to keep it. In this case Originator's Bank has paid an obligation of Originator and under the law of restitution, which applies through Section 1-103 [30-1-103], Originator's Bank would be subrogated to Beneficiary's rights against Originator on the obligation paid by Originator's Bank.

If Originator's Bank erroneously executed Originator's order by instructing Beneficiary's Bank to pay less than $1,000,000, subsection (b) [subsection (2) of this section] applies. If Originator's Bank corrects its error by issuing another payment order to Beneficiary's Bank that results in payment of $1,000,000 to Beneficiary, Originator's Bank is entitled to payment of $1,000,000 from Originator. If the mistake is not corrected, Originator's Bank is entitled to payment from Originator only in the amount of the order issued by Originator's Bank.

3. Subsection (a) [subsection (1) of this section] also applies to duplicate payment orders. Assume Originator's Bank properly executes Originator's $1,000,000 payment order and then by mistake issues a second $1,000,000 payment order in execution of Originator's order. If Beneficiary's Bank accepts both orders issued by Originator's Bank, Beneficiary's Bank is entitled to receive $2,000,000 from Originator's Bank but Originator's Bank is entitled to receive only $1,000,000 from Originator. The remedy of Originator's Bank is the same as that of a receiving bank that executes by issuing an order in an amount greater than the sender's order. It may recover the overpayment from Beneficiary to the extent allowed by the law governing mistake and restitution and in a proper case as stated in Comment 2 may have subrogation rights if it is not entitled to recover from Beneficiary.

4. Suppose Originator instructs Originator's Bank to pay $1,000,000 to Account #12345 in Beneficiary's Bank. Originator's Bank erroneously instructs Beneficiary's Bank to pay $1,0000,000 to Account #12346 and Beneficiary's Bank accepted. Subsection (c) [subsection (3) of this section] covers this case. Originator is not obliged to pay its payment order, but Originator's Bank is required to pay $1,000,000 to Beneficiary's Bank. The remedy of Originator's Bank is to recover $1,000,000 from the holder of Account #12346 that received payment by mistake. Recovery based on the law of mistake and restitution is described in Comment 2.

30-4A-304. Duty of sender to report erroneously executed payment order.

Official Comment

Source: Section 4A-304, U.C.C.

Official Comment:

This section is identical in effect to Section 4A-204 [30-4A-204] which applies to unauthorized orders issued in the name of a customer of the receiving bank. The rationale is stated in Comment 2 to Section 4A-204 [30-4A-204].

30-4A-305. Liability for late or improper execution or failure to execute payment order.

Official Comment

Source: Section 4A-305, U.C.C.

Official Comment:

1. Subsection (a) [subsection (1) of this section] covers cases of delay in completion of a funds transfer resulting from an execution by a receiving bank in breach of Section 4A-302(a) [30-4A-302(1)]. The receiving bank is obliged to pay interest on the amount of the order for the period of the delay. The rate of interest is stated in Section 4A-506 [30-4A-506]. With respect to wire transfers (other than ACH transactions) within the United States, the expectation is that the funds transfer will be completed the same day. In those cases, the originator can reasonably expect that the originator's account will be debited on the same day as the beneficiary's account is credited. If the funds transfer is delayed, compensation can be paid either to the originator or to the beneficiary. The normal practice is to compensate the beneficiary's bank to allow that bank to compensate the beneficiary by back-valuing the payment by the number of days of delay. Thus, the beneficiary is in the same position that it would have been in if the funds transfer had been completed on the same day. Assume on Day 1, Originator's Bank issues its payment order to Intermediary Bank which is received on that day. Intermediary Bank does not execute that order until Day 2 when it issues an order to Beneficiary's Bank which is accepted on that day. Intermediary Bank complies with subsection (a) [subsection (1) of this section] by paying one day's interest to Beneficiary's Bank for the account of Beneficiary.

2. Subsection (b) [subsection (2) of this section] applies to cases of breach of Section 4A-302 [30-4A-302] involving more than mere delay. In those cases the bank is liable for damages for improper execution but they are limited to compensation for interest losses and incidental expenses of the sender resulting from the breach, the expenses of the sender in the funds transfer and attorney's fees. This subsection reflects the judgment that imposition of consequential damages on a bank for commission of an error is not justified.

The leading common law case on the subject of consequential damages is Evra Corp. v. Swiss Bank Corp., 673 F.2d 951 (7th Cir. 1982), in which Swiss Bank, an intermediary bank, failed to execute a payment order. Because the beneficiary did not receive timely payment the originator lost a valuable ship charter. The lower court awarded the originator $2.1 million for lost profits even though the amount of the payment order was only $27,000. The Seventh Circuit reversed, in part on the basis of the common law rule of Hadley v. Baxendale that consequential damages may not be awarded unless the defendant is put on notice of the special circumstances giving rise to them. Swiss Bank may have known that the originator was paying the shipowner for the hire of a vessel but did not know that a favorable charter would be lost if the payment was delayed. "Electronic payments are not so unusual as to automatically place a bank on notice of extraordinary consequences if such a transfer goes awry. Swiss Bank did not have enough information to infer that if it lost a $27,000 payment order it would face liability in excess of $2 million." 673 F.2d at 956.

If *Evra* means that consequential damages can be imposed if the culpable bank has notice of particular circumstances giving rise to the damages, it does not provide an acceptable solution to the problem of bank liability for consequential damages. In the typical case transmission of the payment order is made electronically. Personnel of the receiving bank that process payment orders are not the appropriate people to evaluate the risk of liability for consequential damages in relation to the price charged for the wire transfer service. Even if notice is received by higher level management personnel who could make an appropriate decision whether the risk is justified by the price, liability based on notice would require evaluation of payment orders on an individual basis. This kind of evaluation is inconsistent with the high-speed, low-price, mechanical nature of the processing system that characterizes wire transfers. Moreover, in *Evra* the culpable bank was an intermediary bank with which the originator did not deal. Notice to the originator's bank would not bind the intermediary bank, and it seems impractical for the originator's bank to convey notice of this kind to intermediary banks in the funds transfer. The success of the wholesale wire transfer industry has largely been based on its ability to effect payment at low cost and great speed. Both of these essential aspects of the modern wire transfer system would be adversely affected by a rule that imposed on banks liability for consequential damages. A banking industry amicus brief in *Evra* stated: "Whether banks can continue to make EFT services available on a widespread basis, by charging reasonable rates, depends on whether they can do so without incurring unlimited consequential risks. Certainly, no bank would handle for $3.25 a transaction entailing potential liability in the millions of dollars."

As the court in *Evra* also noted, the originator of the funds transfer is in the best position to evaluate the risk that a funds transfer will not be made on time and to manage that risk by issuing a payment order in time to allow monitoring of the transaction. The originator, by asking the beneficiary, can quickly determine if the funds transfer has been completed. If the originator has sent the payment order at a time that allows a reasonable margin for correcting error, no loss is likely to result if the transaction is monitored. The other published cases on this issue reach the *Evra* result. Central Coordinates, Inc. v. Morgan Guaranty Trust Co., 40 U.C.C. Rep. Serv. 1340 (N.Y.Sup.Ct. 1985), and Gatoil (U.S.A.), Inc. v. Forest Hill State Bank, 1 U.C.C. Rep. Serv. 2d 171 (D.Md. 1986).

Subsection (c) [subsection (3) of this section] allows the measure of damages in subsection (b) [subsection (2) of this section] to be increased by an express written agreement of the receiving bank. An originator's bank might be willing to assume additional responsibilities and incur additional liability in exchange for a higher fee.

3. Subsection (d) [subsection (4) of this section] governs cases in which a receiving bank has obligated itself by express agreement to accept payment orders of a sender. In the absence of such an agreement there is no obligation by a receiving bank to accept a payment order. Section 4A-212 [30-4A-212]. The measure of damages for breach of an agreement to accept a payment order is the same as that stated in subsection (b) [subsection (2) of this section]. As in the case of subsection (b) [subsection (2) of this section], additional damages, including consequential damages, may be recovered to the extent stated in an express written agreement of the receiving bank.

4. Reasonable attorney's fees are recoverable only in cases in which damages are limited to statutory damages stated in subsections (a), (b) and (d) [subsections (1), (2), and (4) of this section]. If additional damages are recoverable because provided for by an express written agreement, attorney's fees are not recoverable. The rationale is that there is no need for statutory attorney's fees in the latter case, because the parties have agreed to a measure of damages which may or may not provide for attorney's fees.

5. The effect of subsection (f) [subsection (6) of this section] is to prevent reduction of a receiving bank's liability under Section 4A-305 [30-4A-305].

Part 4
Payment

30-4A-401. Payment date.

Official Comment

Source: Section 4A-401, U.C.C.

Official Comment:

"Payment date" refers to the day the beneficiary's bank is to pay the beneficiary. The payment date may be expressed in various ways so long as it indicates the day the beneficiary is to receive payment. For example, in ACH transfers the payment date is the equivalent of "settlement date" or "effective date." Payment date applies to the payment order issued to the beneficiary's bank, but a payment order issued to a receiving bank other than the beneficiary's bank may also state a date for payment to the beneficiary. In the latter case, the statement of a payment date is to instruct the receiving bank concerning time of execution of the sender's order. Section 4A-301(b) [30-4A-301(2)].

30-4A-402. Obligation of sender to pay receiving bank.

Official Comment

Source: Section 4A-402, U.C.C.

Official Comment:

1. Subsection (b) [subsection (2) of this section] states that the sender of a payment order to the beneficiary's bank must pay the order when the beneficiary's bank accepts the order. At that point the beneficiary's bank is obliged to pay the beneficiary. Section 4A-404(a) [30-4A-404(1)]. The last clause of subsection (b) [subsection (2) of this section] covers a case of premature acceptance by the beneficiary's bank. In some funds transfers, notably automated clearing house transfers, a beneficiary's bank may receive a payment order with a payment date after the day the order is received. The beneficiary's bank might accept the order before the payment date by notifying the beneficiary of receipt of the order. Although the acceptance obliges the beneficiary's bank to pay the beneficiary, payment is not due until the payment date. The last clause of subsection (b) [subsection (2) of this section] is consistent with that result. The beneficiary's bank is also not entitled to payment from the sender until the payment date.

2. Assume that Originator instructs Bank A to order immediate payment to the account of Beneficiary in Bank B. Execution of Originator's payment order by Bank A is acceptance under Section 4A-209(a) [30-4A-209(1)]. Under the second sentence of Section 4A-402(c) [30-4A-402(3)] the acceptance creates an obligation of Originator to pay Bank A the amount of the order. The last clause of that sentence deals with attempted funds transfers that are not completed. In that event the obligation of the sender to pay its payment order is excused. Originator makes payment to Beneficiary when Bank B, the beneficiary's bank, accepts a payment order for the benefit of Beneficiary. Section 4A-406(a) [30-4A-406(1)]. If that acceptance by Bank B does not occur, the funds transfer has miscarried because Originator has not paid Beneficiary. Originator doesn't have to pay its payment order, and if it has already paid it is entitled to refund of the payment with interest. The rate of interest is stated in Section 4A-506 [30-4A-506]. This "money-back guarantee" is an important protection of Originator. Originator is assured that it will not lose its money if something goes wrong in the transfer. For example, risk of loss resulting from payment to the wrong beneficiary is borne by some bank, not by Originator. The most likely reason for noncompletion is a failure to execute or an erroneous execution of a payment order by Bank A or an intermediary bank. Bank A may have issued its payment order to the wrong bank or it may have identified the wrong beneficiary in its order. The money-back guarantee is particularly important to Originator if noncompletion of the funds transfer is due to the fault of an intermediary bank rather than Bank A. In that case Bank A must refund payment to Originator, and Bank A has the burden of obtaining refund from the intermediary bank that it paid.

Subsection (c) [subsection (3) of this section] can result in loss if an intermediary bank suspends payments. Suppose Originator instructs Bank A to pay to Beneficiary's account in Bank B and to use Bank C as an intermediary bank. Bank A executes Originator's order by issuing a payment order to Bank C. Bank A pays Bank C. Bank C fails to execute the order of Bank A and suspends payments. Under subsections (c) and (d) [subsections (3) and (4) of this section], Originator is not obliged to pay Bank A and is entitled to refund from Bank A of any payment that it may have made. Bank A is entitled to a refund from Bank C, but Bank C is insolvent. Subsection (e) [subsection (5) of this section] deals with this case. Bank A was required to issue its payment order to Bank C because Bank C was designated as an intermediary bank by Originator. Section 4A-302(a)(1) [30-4A-302(1)(a)]. In this case Originator takes the risk of insolvency of Bank C. Under subsection (e) [subsection (5) of this section], Bank A is entitled to payment from Originator and Originator is subrogated to the right of Bank A under subsection (d) [subsection (4) of this section] to refund of payment from Bank C.

3. A payment order is not like a negotiable instrument on which the drawer or maker has liability. Acceptance of the order by the receiving bank creates an obligation of the sender to pay the receiving bank the amount of the order. That is the extent of the sender's liability to the receiving bank and no other person has any rights against the sender with respect to the sender's order.

30-4A-403. Payment by sender to receiving bank.

Official Comment

Source: Section 4A-403, U.C.C.

Official Comment:

1. This section defines when a sender pays the obligation stated in Section 4A-402 [30-4A-402]. If a group of two or more banks engage in funds transfers with each other, the participating banks will sometimes be senders and sometimes receiving banks. With respect to payment orders other than Fedwires, the amounts of the various payment orders may be credited and debited to accounts of one bank with another or to a clearing house account of each bank and amounts owed and amounts due are netted. Settlement is made through a Federal Reserve Bank by charges to the Federal Reserve accounts of the net debtor banks and credits to the Federal Reserve accounts of the net creditor banks. In the case of Fedwires the sender's obligation is settled by a debit to the Federal Reserve account of the sender and a credit to the Federal Reserve account of the receiving bank at the time the receiving bank receives the payment order. Both of these cases are covered by subsection (a)(1) [subsection (1)(a) of this section]. When the Federal Reserve settlement becomes final the obligation of the sender under Section 4A-402 [30-4A-402] is paid.

2. In some cases a bank does not settle an obligation owed to another bank through a Federal Reserve Bank. This is the case if one of the banks is a foreign bank without access to the Federal Reserve payment system. In this kind of case, payment is usually made by credits or debits to accounts of the two banks with each other or to accounts of the two banks in a third bank. Suppose

Bank B has an account in Bank A. Bank A advises Bank B that its account in Bank A has been credited $1,000,000 and that the credit is immediately withdrawable. Bank A also instructs Bank B to pay $1,000,000 to the account of Beneficiary in Bank B. This case is covered by subsection (a)(2) [subsection (1)(b) of this section]. Bank B may want to immediately withdraw this credit. For example, it might do so by instructing Bank A to debit the account and pay some third party. Payment by Bank A to Bank B of Bank A's payment order occurs when the withdrawal is made. Suppose Bank B does not withdraw the credit. Since Bank B is the beneficiary's bank, one of the effects of receipt of payment by Bank B is that acceptance of Bank A's payment order automatically occurs at the time of payment. Section 4A-209(b)(2) [30-4A-209(2)(b)]. Acceptance means that Bank B is obliged to pay $1,000,000 to Beneficiary. Section 4A-404(a) [30-4A-404(1)]. Subsection (a)(2) of Section 4A-403 [30-4A-403(1)(b)] states that payment does not occur until midnight if the credit is not withdrawn. This allows Bank B an opportunity to reject the order if it does not have time to withdraw the credit to its account and it is not willing to incur the liability to Beneficiary before it has use of the funds represented by the credit.

3. Subsection (a)(3) [subsection (1)(c) of this section] applies to a case in which the sender (bank or nonbank) has a funded account in the receiving bank. If Sender has an account in Bank and issues a payment order to Bank, Bank can obtain payment from Sender by debiting the account of Sender, which pays its Section 4A-402 [30-4A-402] obligation to Bank when the debit is made.

4. Subsection (b) [subsection (2) of this section] deals with multilateral settlements made through a funds transfer system and is based on the CHIPS settlement system. In a funds transfer system such as CHIPS, which allows the various banks that transmit payment orders over the system to settle obligations at the end of each day, settlement is not based on individual payment orders. Each bank using the system engages in funds transfers with many other banks using the system. Settlement for any participant is based on the net credit or debit position of that participant with all other banks using the system. Subsection (b) [subsection (2) of this section] is designed to make clear that the obligations of any sender are paid when the net position of that sender is settled in accordance with the rules of the funds transfer system. This provision is intended to invalidate any argument, based on common-law principles, that multilateral netting is not valid because mutuality of obligation is not present. Subsection (b) [subsection (2) of this section] dispenses with any mutuality of obligation requirements. Subsection (c) [subsection (3) of this section] applies to cases in which two banks send payment orders to each other during the day and settle with each other at the end of the day or at the end of some other period. It is similar to subsection (b) [subsection (2) of this section] in that it recognizes that a sender's obligation to pay a payment order is satisfied by a setoff. The obligations of each bank as sender to the other as receiving bank are obligations of the bank itself and not as representative of customers. These two sections are important in the case of insolvency of a bank. They make clear that liability under Section 4A-402 [30-4A-402] is based on the net position of the insolvent bank after setoff.

5. Subsection (d) [subsection (4) of this section] relates to the uncommon case in which the sender doesn't have an account relationship with the receiving bank and doesn't settle through a Federal Reserve Bank. An example would be a customer that pays over the counter for a payment order that the customer issues to the receiving bank. Payment would normally be by cash, check or bank obligation. When payment occurs is determined by law outside Article 4A [Title 30, chapter 4A].

30-4A-404. Obligation of beneficiary's bank to pay and give notice to beneficiary.

Official Comment

Source: Section 4A-404, U.C.C.

Official Comment:

1. The first sentence of subsection (a) [subsection (1) of this section] states the time when the obligation of the beneficiary's bank arises. The second and third sentences state when the beneficiary's bank must make funds available to the beneficiary. They also state the measure of damages for failure, after demand, to comply. Since the Expedited Funds Availability Act, 12 U.S.C. 4001 et seq., also governs funds availability in a funds transfer, the second and third sentences of subsection (a) [subsection (1) of this section] may be subject to preemption by that Act.

2. Subsection (a) [subsection (1) of this section] provides that the beneficiary of an accepted payment order may recover consequential damages if the beneficiary's bank refuses to pay the order after demand by the beneficiary if the bank at that time had notice of the particular circumstances giving rise to the damages. Such damages are recoverable only to the extent the

bank had "notice of the damages." The quoted phrase requires that the bank have notice of the general type or nature of the damages that will be suffered as a result of the refusal to pay and their general magnitude. There is no requirement that the bank have notice of the exact or even the approximate amount of the damages, but if the amount of damages is extraordinary the bank is entitled to notice of that fact. For example, in Evra Corp. v. Swiss Bank Corp., 673 F.2d 951 (7th Cir. 1982), failure to complete a funds transfer of only $27,000 required to retain rights to a very favorable ship charter resulted in a claim for more than $2,000,000 of consequential damages. Since it is not reasonably foreseeable that a failure to make a relatively small payment will result in damages of this magnitude, notice is not sufficient if the beneficiary's bank has notice only that the $27,000 is necessary to retain rights on a ship charter. The bank is entitled to notice that an exceptional amount of damages will result as well. For example, there would be adequate notice if the bank had been made aware that damages of $1,000,000 or more might result.

3. Under the last clause of subsection (a) [subsection (1) of this section] the beneficiary's bank is not liable for damages if its refusal to pay was "because of a reasonable doubt concerning the right of the beneficiary to payment." Normally there will not be any question about the right of the beneficiary to receive payment. Normally, the bank should be able to determine whether it has accepted the payment order and, if it has been accepted, the first sentence of subsection (a) [subsection (1) of this section] states that the bank is obliged to pay. There may be uncommon cases, however, in which there is doubt whether acceptance occurred. For example, if acceptance is based on receipt of payment by the beneficiary's bank under Section 4A-403 (a)(1) or (2) [30-4A-403(1)(a) or (1)(b)], there may be cases in which the bank is not certain that payment has been received. There may also be cases in which there is doubt about whether the person demanding payment is the person identified in the payment order as beneficiary of the order.

The last clause of subsection (a) [subsection (1) of this section] does not apply to cases in which a funds transfer is being used to pay an obligation and a dispute arises between the originator and the beneficiary concerning whether the obligation is in fact owed. For example, the originator may try to prevent payment to the beneficiary by the beneficiary's bank by alleging that the beneficiary is not entitled to payment because of fraud against the originator or a breach of contract relating to the obligation. The fraud or breach of contract claim of the originator may be grounds for recovery by the originator from the beneficiary after the beneficiary is paid, but it does not affect the obligation of the beneficiary's bank to pay the beneficiary. Unless the payment order has been cancelled pursuant to Section 4A-211(c) [30-4A-211(3)], there is no excuse for refusing to pay the beneficiary and, in a proper case, the refusal may result in consequential damages. Except in the case of a book transfer, in which the beneficiary's bank is also the originator's bank, the originator of a funds transfer cannot cancel a payment order to the beneficiary's bank, with or without the consent of that bank, because the originator is not the sender of that order. Thus, the beneficiary's bank may safely ignore any instruction by the originator to withhold payment to the beneficiary.

4. Subsection (b) [subsection (2) of this section] states the duty of the beneficiary's bank to notify the beneficiary of receipt of the order. If acceptance occurs under Section 4A-209(b)(1) [30-4A-209(2)(a)] the beneficiary is normally notified. Thus, subsection (b) [subsection (2) of this section] applies primarily to cases in which acceptance occurs under Section 4A-209(b)(2) or (3) [30-4A-209(2)(b) or (2)(c). Notice under subsection (b) [subsection (2) of this section] is not required if the person entitled to the notice agrees or a funds transfer system rule provides that notice is not required and the beneficiary is given notice of the rule. In ACH transactions the normal practice is not to give notice to the beneficiary unless notice is requested by the beneficiary. This practice can be continued by adoption of a funds transfer system rule. Subsection (a) [subsection (1) of this section] is not subject to variation by agreement or by a funds transfer system rule.

30-4A-405. Payment by beneficiary's bank to beneficiary.

Official Comment

Source: Section 4A-405, U.C.C.

Official Comment:

1. This section defines when the beneficiary's bank pays the beneficiary and when the obligation of the beneficiary's bank under Section 4A-404 [30-4A-404] to pay the beneficiary is satisfied. In almost all cases the bank will credit an account of the beneficiary when it receives a payment order. In the typical case the beneficiary is paid when the beneficiary is given notice of the right to withdraw the credit. Subsection (a)(i) [subsection (1)(a) of this section]. In some cases payment might be made to the beneficiary not by releasing funds to the beneficiary, but by

applying the credit to a debt of the beneficiary. Subsection (a)(ii) [subsection (1)(b) of this section]. In this case the beneficiary gets the benefit of the payment order because a debt of the beneficiary has been satisfied. The two principal cases in which payment will occur in this manner are setoff [sic] by the beneficiary's bank and payment of the proceeds of the payment order to a garnishing creditor of the beneficiary. These cases are discussed in Comment 2 to Section 4A-502 [30-4A-502].

2. If a beneficiary's bank releases funds to the beneficiary before it receives payment from the sender of the payment order, it assumes the risk that the sender may not pay the sender's order because of suspension of payments or other reason. Subsection (c) [subsection (3) of this section]. As stated in Comment 5 to Section 4A-209 [30-4A-209], the beneficiary's bank can protect itself against this risk by delaying acceptance. But if the bank accepts the order it is obliged to pay the beneficiary. If the beneficiary's bank has given the beneficiary notice of the right to withdraw a credit made to the beneficiary's account, the beneficiary has received payment from the bank. Once payment has been made to the beneficiary with respect to an obligation incurred by the bank under Section 4A-404(a) [30-4A-404(1)], the payment cannot be recovered by the beneficiary's bank unless subsection (d) or (e) [subsection (4) or (5) of this section] applies. Thus, a right to withdraw a credit cannot be revoked if the right to withdraw constituted payment of the bank's obligation. This principle applies even if funds were released as a "loan" (see Comment 5 to Section 4A-209 [30-4A-209]), or were released subject to a condition that they would be repaid in the event the bank does not receive payment from the sender of the payment order, or the beneficiary agreed to return the payment if the bank did not receive payment from the sender.

3. Subsection (c) [subsection (3) of this section] is subject to an exception stated in subsection (d) [subsection (4) of this section] which is intended to apply to automated clearing house transfers. ACH transfers are made in batches. A beneficiary's bank will normally accept, at the same time and as part of a single batch, payment orders with respect to many different originator's banks. Comment 2 to Section 4A-206 [30-4A-206]. The custom in ACH transactions is to release funds to the beneficiary early on the payment date even though settlement to the beneficiary's bank does not occur until later in the day. The understanding is that payments to beneficiaries are provisional until the beneficiary's bank receives settlement. This practice is similar to what happens when a depositary bank releases funds with respect to a check forwarded for collection. If the check is dishonored the bank is entitled to recover the funds from the customer. ACH transfers are widely perceived as check substitutes. Section 4A-405(d) [30-4A-405(4)] allows the funds transfer system to adopt a rule making payments to beneficiaries provisional. If such a rule is adopted, a beneficiary's bank that releases funds to the beneficiary will be able to recover the payment if it doesn't receive payment of the payment order that it accepted. There are two requirements with respect to the funds transfer system rule. The beneficiary, the beneficiary's bank and the originator's bank must all agree to be bound by the rule and the rule must require that both the beneficiary and the originator be given notice of the provisional nature of the payment before the funds transfer is initiated. There is no requirement that the notice be given with respect to a particular funds transfer. Once notice of the provisional nature of the payment has been given, the notice is effective for all subsequent payments to or from the person to whom the notice was given. Subsection (d) [subsection (4) of this section] provides only that the funds transfer system rule must require notice to the beneficiary and the originator. The beneficiary's bank will know what the rule requires, but it has no way of knowing whether the originator's bank complied with the rule. Subsection (d) [subsection (4) of this section] does not require proof that the originator received notice. If the originator's bank failed to give the required notice and the originator suffered as a result, the appropriate remedy is an action by the originator against the originator's bank based on that failure. But the beneficiary's bank will not be able to get the benefit of subsection (d) [subsection (4) of this section] unless the beneficiary had notice of the provisional nature of the payment because subsection (d) [subsection (4) of this section] requires an agreement by the beneficiary to be bound by the rule. Implicit in an agreement to be bound by a rule that makes a payment provisional is a requirement that notice be given of what the rule provides. The notice can be part of the agreement or separately given. For example, notice can be given by providing a copy of the system's operating rules.

With respect to ACH transfers made through a Federal Reserve Bank acting as an intermediary bank, the Federal Reserve Bank is obliged under Section 4A-402(b) [30-4A-402(2)] to pay a beneficiary's bank that accepts the payment order. Unlike Fedwire transfers, under current ACH practice a Federal Reserve Bank that processes a payment order does not obligate itself to pay if the originator's bank fails to pay the Federal Reserve Bank. It is assumed that the Federal Reserve will use its right of preemption which is recognized in Section 4A-107 [30-4A-107] to disclaim the Section 4A-402(b) [30-4A-402(2)] obligation in ACH transactions if it decides to retain the provisional payment rule.

4. Subsection (e) [subsection (5) of this section] is another exception to subsection (c) [subsection (3) of this section]. It refers to funds transfer systems having loss-sharing rules described in the subsection. CHIPS has proposed a rule that fits the description. Under the CHIPS loss-sharing rule the CHIPS banks will have agreed to contribute funds to allow the system to settle for payment orders sent over the system during the day in the event that one or more banks are unable to meet their settlement obligations. Subsection (e) [subsection (5) of this section] applies only if CHIPS fails to settle despite the loss-sharing rule. Since funds under the loss-sharing rule will be instantly available to CHIPS and will be in an amount sufficient to cover any failure that can be reasonably anticipated, it is extremely unlikely that CHIPS would ever fail to settle. Thus, subsection (e) [subsection (5) of this section] addresses an event that should never occur. If that event were to occur, all payment orders made over the system would be cancelled under the CHIPS rule. Thus, no bank would receive settlement, whether or not a failed bank was involved in a particular funds transfer. Subsection (e) [subsection (5) of this section] provides that each funds transfer in which there is a payment order with respect to which there is a settlement failure is unwound. Acceptance by the beneficiary's bank in each funds transfer is nullified. The consequences of nullification are that the beneficiary has no right to receive or retain payment by the beneficiary's bank, no payment is made by the originator to the beneficiary and each sender in the funds transfer is, subject to Section 4A-402(e) [30-4A-402(5)], not obliged to pay its payment order and is entitled to refund under Section 4A-402(d) [30-4A-402(4)] if it has already paid.

30-4A-406. Payment by originator to beneficiary — discharge of underlying obligation.

Official Comment

Source: Section 4A-406, U.C.C.

Official Comment:

1. Subsection (a) [subsection (1) of this section] states the fundamental rule of Article 4A [Title 30, chapter 4A] that payment by the originator to the beneficiary is accomplished by providing to the beneficiary the obligation of the beneficiary's bank to pay. Since this obligation arises when the beneficiary's bank accepts a payment order, the originator pays the beneficiary at the time of acceptance and in the amount of the payment order accepted.

2. In a large percentage of funds transfers, the transfer is made to pay an obligation of the originator. Subsection (a) [subsection (1) of this section] states that the beneficiary is paid by the originator when the beneficiary's bank accepts a payment order for the benefit of the beneficiary. When that happens the effect under subsection (b) [subsection (2) of this section] is to substitute the obligation of the beneficiary's bank for the obligation of the originator. The effect is similar to that under Article 3 [Title 30, chapter 3] if a cashier's check payable to the beneficiary had been taken by the beneficiary. Normally, payment by funds transfer is sought by the beneficiary because it puts money into the hands of the beneficiary more quickly. As a practical matter the beneficiary and the originator will nearly always agree to the funds transfer in advance. Under subsection (b) [subsection (2) of this section] acceptance by the beneficiary's bank will result in discharge of the obligation for which payment was made unless the beneficiary had made a contract with respect to the obligation which did not permit payment by the means used. Thus, if there is no contract of the beneficiary with respect to the means of payment of the obligation, acceptance by the beneficiary's bank of a payment order to the account of the beneficiary can result in discharge.

3. Suppose Beneficiary's contract stated that payment of an obligation owed by Originator was to be made by a cashier's check of Bank A. Instead, Originator paid by a funds transfer to Beneficiary's account in Bank B. Bank B accepted a payment order for the benefit of Beneficiary by immediately notifying Beneficiary that the funds were available for withdrawal. Before Beneficiary had a reasonable opportunity to withdraw the funds Bank B suspended payments. Under the unless clause of subsection (b) [subsection (2) of this section] Beneficiary is not required to accept the payment as discharging the obligation owed by Originator to Beneficiary if Beneficiary's contract means that Beneficiary was not required to accept payment by wire transfer. Beneficiary could refuse the funds transfer as payment of the obligation and could resort to rights under the underlying contract to enforce the obligation. The rationale is that Originator cannot impose the risk of Bank B's insolvency on Beneficiary if Beneficiary had specified another means of payment that did not entail that risk. If Beneficiary is required to accept Originator's payment, Beneficiary would suffer a loss that would not have occurred if payment had been made

by a cashier's check on Bank A, and Bank A has not suspended payments. In this case Originator will have to pay twice. It is obliged to pay the amount of its payment order to the bank that accepted it and has to pay the obligation it owes to Beneficiary which has not been discharged. Under the last sentence of subsection (b) [subsection (2) of this section] Originator is subrogated to Beneficiary's right to receive payment from Bank B under Section 4A-404(a) [30-4A-404(1)].

4. Suppose Beneficiary's contract called for payment by a Fedwire transfer to Bank B, but the payment order accepted by Bank B was not a Fedwire transfer. Before the funds were withdrawn by Beneficiary, Bank B suspended payments. The sender of the payment order to Bank B paid the amount of the order to Bank B. In this case the payment by Originator did not comply with Beneficiary's contract, but the noncompliance did not result in a loss to Beneficiary as required by subsection (b)(iv) [subsection (2)(a)(iv) of this section]. A Fedwire transfer avoids the risk of insolvency of the sender of the payment order to Bank B, but it does not affect the risk that Bank B will suspend payments before withdrawal of the funds by Beneficiary. Thus, the unless clause of subsection (b) [subsection (2) of this section] is not applicable and the obligation owed to Beneficiary is discharged.

5. Charges of receiving banks in a funds transfer normally are nominal in relationship to the amount being paid by the originator to the beneficiary. Wire transfers are normally agreed to in advance and the parties may agree concerning how these charges are to be divided between the parties. Subsection (c) [subsection (3) of this section] states a rule that applies in the absence of agreement. In some funds transfers charges of banks that execute payment orders are collected by deducting the charges from the amount of the payment order issued by the bank, i.e. the bank issues a payment order that is slightly less than the amount of the payment order that is being executed. The process is described in Comment 3 to Section 4A-302 [30-4A-302]. The result in such a case is that the payment order accepted by the beneficiary's bank will be slightly less than the amount of the originator's order. Subsection (c) [subsection (3) of this section] recognizes the principle that a beneficiary is entitled to full payment of a debt paid by wire transfer as a condition to discharge. On the other hand, subsection (c) [subsection (3) of this section] prevents a beneficiary from denying the originator the benefit of the payment by asserting that discharge did not occur because deduction of bank charges resulted in less than full payment. The typical case is one in which the payment is made to exercise a valuable right such as an option which is unfavorable to the beneficiary. Subsection (c) [subsection (3) of this section] allows discharge notwithstanding the deduction unless the originator fails to reimburse the beneficiary for the deducted charges after demand by the beneficiary.

Part 5
Miscellaneous Provisions

30-4A-501. Variation by agreement and effect of funds-transfer system rule.

Official Comment

Source: Section 4A-501, U.C.C.

Official Comment:

1. This section is designed to give some flexibility to Article 4A [Title 30, chapter 4A]. Funds transfer system rules govern rights and obligations between banks that use the system. They may cover a wide variety of matters such as form and content of payment orders, security procedures, cancellation rights and procedures, indemnity rights, compensation rules for delays in completion of a funds transfer, time and method of settlement, credit restrictions with respect to senders of payment orders and risk allocation with respect to suspension of payments by a participating bank. Funds transfer system rules can be very effective in supplementing the provisions of Article 4A [Title 30, chapter 4A] and in filling gaps that may be present in Article 4A [Title 30, chapter 4A]. To the extent they do not conflict with Article 4A [Title 30, chapter 4A] there is no problem with respect to their effectiveness. In that case they merely supplement Article 4A [Title 30, chapter 4A]. Section 4A-501 [30-4A-501] goes further. It states that unless the contrary is stated, funds transfer system rules can override provisions of Article 4A [Title 30, chapter 4A]. Thus, rights and obligations of a sender bank and a receiving bank with respect to each other can be different from that stated in Article 4A [Title 30, chapter 4A] to the extent a funds transfer system rule applies. Since funds transfer system rules are defined as those governing the relationship between participating banks, a rule can have a direct effect only on participating banks. But a rule that affects the conduct of a participating bank may indirectly affect the rights of nonparticipants such as the originator or beneficiary of a funds transfer, and such a rule can be effective even though it may affect nonparticipants without their consent.

For example, a rule might prevent execution of a payment order or might allow cancellation of a payment order with the result that a funds transfer is not completed or is delayed. But a rule purporting to define rights and obligations of nonparticipants in the system would not be effective to alter Article 4A [Title 30, chapter 4A] rights because the rule is not within the definition of funds transfer system rule. Rights and obligations arising under Article 4A [Title 30, chapter 4A] may also be varied by agreement of the affected parties, except to the extent Article 4A [Title 30, chapter 4A] otherwise provides. Rights and obligations arising under Article 4A [Title 30, chapter 4A] can also be changed by Federal Reserve regulations and operating circulars of Federal Reserve Banks. Section 4A-107 [30-4A-107].

2. Subsection (b)(ii) [subsection (2)(a)(ii) of this section] refers to ACH transfers. Whether an ACH transfer is made through an automated clearing house of a Federal Reserve Bank or through an automated clearing house of another association of banks, the rights and obligations of the originator's bank and the beneficiary's bank are governed by uniform rules adopted by various associations of banks in various parts of the nation. With respect to transfers in which a Federal Reserve Bank acts as intermediary bank these rules may be incorporated, in whole or in part, in operating circulars of the Federal Reserve Bank. Even if not so incorporated these rules can still be binding on the association banks. If a transfer is made through a Federal Reserve Bank, the rules are effective under subsection (b)(ii) [subsection (2)(a)(ii) of this section]. If the transfer is not made through a Federal Reserve Bank, the association rules are effective under subsection (b)(i) [subsection (2)(a)(i) of this section].

30-4A-502. Creditor process served on receiving bank — setoff by beneficiary's bank.

Official Comment

Source: Section 4A-502, U.C.C.

Official Comment:

1. When a receiving bank accepts a payment order, the bank normally receives payment from the sender by debiting an authorized account of the sender. In accepting the sender's order the bank may be relying on a credit balance in the account. If creditor process is served on the bank with respect to the account before the bank accepts the order but the bank employee responsible for the acceptance was not aware of the creditor process at the time the acceptance occurred, it is unjust to the bank to allow the creditor process to take the credit balance on which the bank may have relied. Subsection (b) [subsection (2) of this section] allows the bank to obtain payment from the sender's account in this case. Under that provision, the balance in the sender's account to which the creditor process applies is deemed to be reduced by the amount of the payment order unless there was sufficient time for notice of the service of creditor process to be received by personnel of the bank responsible for the acceptance.

2. Subsection (c) [subsection (3) of this section] deals with payment orders issued to the beneficiary's bank. The bank may credit the beneficiary's account when the order is received, but under Section 4A-404(a) [30-4A-404(1)] the bank incurs no obligation to pay the beneficiary until the order is accepted pursuant to Section 4A-209(b) [30-4A-209(2)]. Thus, before acceptance, the credit to the beneficiary's account is provisional. But under Section 4A-209(b) [30-4A-209(2)] acceptance occurs if the beneficiary's bank pays the beneficiary pursuant to Section 4A-405(a) [30-4A-405(1)]. Under that provision, payment occurs if the credit to the beneficiary's account is applied to a debt of the beneficiary. Subsection (c)(1) [subsection (3)(a) of this section] allows the bank to credit the beneficiary's account with respect to a payment order and to accept the order by setting off the credit against an obligation owed to the bank or applying the credit to creditor process with respect to the account.

Suppose a beneficiary's bank receives a payment order for the benefit of a customer. Before the bank accepts the order, the bank learns that creditor process has been served on the bank with respect to the customer's account. Normally there is no reason for a beneficiary's bank to reject a payment order, but if the beneficiary's account is garnished, the bank may be faced with a difficult choice. If it rejects the order, the garnishing creditor's potential recovery of funds of the beneficiary is frustrated. It may be faced with a claim by the creditor that the rejection was a wrong to the creditor. If the bank accepts the order, the effect is to allow the creditor to seize funds of its customer, the beneficiary. Subsection (c)(3) [subsection (3)(c) of this section] gives the bank no choice in this case. It provides that it may not favor its customer over the creditor by rejecting the order. The beneficiary's bank may rightfully reject only if there is an independent basis for rejection.

3. Subsection (c)(2) [subsection (3)(b) of this section] is similar to subsection (b) [subsection (2) of this section]. Normally the beneficiary's bank will release funds to the beneficiary shortly after acceptance or it will accept by releasing funds. Since the bank is bound by a garnishment

order served before funds are released to the beneficiary, the bank might suffer a loss if funds were released without knowledge that a garnishment order had been served. Subsection (c)(2) [subsection (3)(b) of this section] protects the bank if it did not have adequate notice of the garnishment when the funds were released.

4. A creditor may want to reach funds involved in a funds transfer. The creditor may try to do so by serving process on the originator's bank, an intermediary bank or the beneficiary's bank. The purpose of subsection (d) [subsection (4) of this section] is to guide the creditor and the court as to the proper method of reaching the funds involved in a funds transfer. A creditor of the originator can levy on the account of the originator in the originator's bank before the funds transfer is initiated, but that levy is subject to the limitations stated in subsection (b) [subsection (2) of this section]. The creditor of the originator cannot reach any other funds because no property of the originator is being transferred. A creditor of the beneficiary cannot levy on property of the originator and until the funds transfer is completed by acceptance by the beneficiary's bank of a payment order for the benefit of the beneficiary, the beneficiary has no property interest in the funds transfer which the beneficiary's creditor can reach. A creditor of the beneficiary that wants to reach the funds to be received by the beneficiary must serve creditor process on the beneficiary's bank to reach the obligation of the beneficiary's bank to pay the beneficiary which arises upon acceptance by the beneficiary's bank under Section 4A-404(a) [30-4A-404(1)].

5. "Creditor process" is defined in subsection (a) [subsection (1) of this section] to cover a variety of devices by which a creditor of the holder of a bank account or a claimant to a bank account can seize the account. Procedure and nomenclature varies widely from state to state. The term used in Section 4A-502 [30-4A-502] is a generic term.

30-4A-503. Injunction or restraining order with respect to funds transfer.

Official Comment

Source: Section 4A-503, U.C.C.

Official Comment:

This section is related to Section 4A-502(d) [30-4A-502(4)] and to Comment 4 to Section 4A-502 [30-4A-502]. It is designed to prevent interruption of a funds transfer after it has been set in motion. The initiation of a funds transfer can be prevented by enjoining the originator or the originator's bank from issuing a payment order. After the funds transfer is completed by acceptance of a payment order by the beneficiary's bank, that bank can be enjoined from releasing funds to the beneficiary or the beneficiary can be enjoined from withdrawing the funds. No other injunction is permitted. In particular, intermediary banks are protected, and injunctions against the originator and the originator's bank are limited to issuance of a payment order. Except for the beneficiary's bank, nobody can be enjoined from paying a payment order, and no receiving bank can be enjoined from receiving payment from the sender of the order that it accepted.

30-4A-504. Order in which items and payment orders may be charged to account — order of withdrawals from account.

Official Comment

Source: Section 4A-504, U.C.C.

Official Comment:

Subsection (a) [subsection (1) of this section] concerns priority among various obligations that are to be paid from the same account. A customer may have written checks on its account with the receiving bank and may have issued one or more payment orders payable from the same account. If the account balance is not sufficient to cover all of the checks and payment orders, some checks may be dishonored and some payment orders may not be accepted. Although there is no concept of wrongful dishonor of a payment order in Article 4A [Title 30, chapter 4A] in the absence of an agreement to honor by the receiving bank, some rights and obligations may depend on the amount in the customer's account. Section 4A-209(b)(3) [30-4A-209(2)(c)] and Section 4A-210(b) [30-4A-210(2)]. Whether dishonor of a check is wrongful also may depend upon the balance in the customer's account. Under subsection (a) [subsection (1) of this section], the bank is not required to consider the competing items and payment orders in any particular order. Rather it may charge the customer's account for the various items and orders in any order. Suppose there is $12,000 in the customer's account. If a check for $5,000 is presented for payment and the bank receives a $10,000 payment order from the customer, the bank could dishonor the check and accept the payment order. Dishonor of the check is not wrongful because the account balance was less than the amount of the check after the bank charged the account $10,000 on account of the payment order. Or, the bank could pay the check and not execute the payment order because the amount of the order is not covered by the balance in the account.

30-4A-505. Preclusion of objection to debit of customer's account.

Official Comment

Source: Section 4A-505, U.C.C.

Official Comment:

This section is in the nature of a statute of repose for objecting to debits made to the customer's account. A receiving bank that executes payment orders of a customer may have received payment from the customer by debiting the customer's account with respect to a payment order that the customer was not required to pay. For example, the payment order may not have been authorized or verified pursuant to Section 4A-202 [30-4A-202] or the funds transfer may not have been completed. In either case the receiving bank is obliged to refund the payment to the customer and this obligation to refund payment cannot be varied by agreement. Section 4A-204 [30-4A-204] and Section 4A-402 [30-4A-402]. Refund may also be required if the receiving bank is not entitled to payment from the customer because the bank erroneously executed a payment order. Section 4A-303 [30-4A-303]. A similar analysis applies to that case. Section 4A-402(d) and (f) [30-4A-402(4) and (6)] require refund and the obligation to refund may not be varied by agreement. Under 4A-505 [30-4A-505], however, the obligation to refund may not be asserted by the customer if the customer has not objected to the debiting of the account within one year after the customer received notification of the debit.

30-4A-506. Rate of interest.

Official Comment

Source: Section 4A-506, U.C.C.

Official Comment:

1. A receiving bank is required to pay interest on the amount of a payment order received by the bank in a number of situations. Sometimes the interest is payable to the sender and in other cases it is payable to either the originator or the beneficiary of the funds transfer. The relevant provisions are Section 4A-204(a) [30-4A-204(1)], Section 4A-209(b)(3) [30-4A-209(2)(c)], Section 4A-210(b) [30-4A-210(2)], Section 4A-305(a) [30-4A-305(1)], Section 4A-402(d) [30-4A-402(4)] and Section 4A-404(b) [30-4A-404(2)]. The rate of interest may be governed by a funds transfer system rule or by agreement as stated in subsection (a) [subsection (1) of this section]. If subsection (a) [subsection (1) of this section] doesn't apply, the rate is determined under subsection (b) [subsection (2) of this section]. Subsection (b) [subsection (2) of this section] is illustrated by the following example. A bank is obliged to pay interest on $1,000,000 for three days, July 3, July 4, and July 5. The published Fed Funds rate is .082 for July 3 and .081 for July 5. There is no published rate for July 4 because that day is not a banking day. The rate for July 3 applies to July 4. The applicable Fed Funds rate is .08167 (the average of .082, .082, and .081) divided by 360 which equals .0002268. The amount of interest payable is $1,000,000 X .0002268 X 3 = $680.40.

2. In some cases, interest is payable in spite of the fact that there is no fault by the receiving bank. The last sentence of subsection (b) [subsection (2) of this section] applies to those cases. For example, a funds transfer might not be completed because the beneficiary's bank rejected the payment order issued to it by the originator's bank or an intermediary bank. Section 4A-402(c) [30-4A-402(3)] provides that the originator is not obliged to pay its payment order and Section 4A-402(d) [30-4A-402(4)] provides that the originator's bank must refund any payment received plus interest. The requirement to pay interest in this case is not based on fault by the originator's bank. Rather, it is based on restitution. Since the originator's bank had the use of the originator's money, it is required to pay the originator for the value of that use. The value of that use is not determined by multiplying the interest rate by the refundable amount because the originator's bank is required to deposit with the Federal Reserve a percentage of the bank's deposits as a reserve requirement. Since that deposit does not bear interest, the bank had use of the refundable amount reduced by a percentage equal to the reserve requirement. If the reserve requirement is 12%, the amount of interest payable by the bank under the formula stated in subsection (b) [subsection (2) of this section] is reduced by 12%.

30-4A-507. Choice of law.

Official Comment

Source: Section 4A-507, U.C.C.

Official Comment:

1. Funds transfers are typically interstate or international in character. If part of a funds transfer is governed by Article 4A [Title 30, chapter 4A] and another part is governed by other law, the rights and obligations of parties to the funds transfer may be unclear because there is

no clear consensus in various jurisdictions concerning the juridical nature of the transaction. Unless all of a funds transfer is governed by a single law it may be very difficult to predict the result if something goes wrong in the transfer. Section 4A-507 [30-4A-507] deals with this problem. Subsection (b) [subsection (2) of this section] allows parties to a funds transfer to make a choice-of-law agreement. Subsection (c) [subsection (3) of this section] allows a funds transfer system to select the law of a particular jurisdiction to govern funds transfers carried out by means of the system. Subsection (a) [subsection (1) of this section] states residual rules if no choice of law has occurred under subsection (b) [subsection (2) of this section] or subsection (c) [subsection (3) of this section].

2. Subsection (a) [subsection (1) of this section] deals with three sets of relationships. Rights and obligations between the sender of a payment order and the receiving bank are governed by the law of the jurisdiction in which the receiving bank is located. If the receiving bank is the beneficiary's bank the rights and obligations of the beneficiary are also governed by the law of the jurisdiction in which the receiving bank is located. Suppose Originator, located in Canada, sends a payment order to Originator's Bank located in a state in which Article 4A [Title 30, chapter 4A] has been enacted. The order is for payment to an account of Beneficiary in a bank in England. Under subsection (a)(1) [subsection (1)(a) of this section], the rights and obligations of Originator and Originator's Bank toward each other are governed by Article 4A [Title 30, chapter 4A] if an action is brought in a court in the Article 4A [Title 30, chapter 4A] state. If an action is brought in a Canadian court, the conflict of laws issue will be determined by Canadian law which might or might not apply the law of the state in which Originator's Bank is located. If that law is applied, the execution of Originator's order will be governed by Article 4A [Title 30, chapter 4A], but with respect to the payment order of Originator's Bank to the English bank, Article 4A [Title 30, chapter 4A] may or may not be applied with respect to the rights and obligations between the two banks. The result may depend upon whether action is brought in a court in the state in which Originator's Bank is located or in an English court. Article 4A [Title 30, chapter 4A] is binding only on a court in a state that enacts it. It can have extraterritorial effect only to the extent courts of another jurisdiction are willing to apply it. Subsection (c) [subsection (3) of this section] also bears on the issues discussed in this Comment.

Under Section 4A-406 [30-4A-406] payment by the originator to the beneficiary of the funds transfer occurs when the beneficiary's bank accepts a payment order for the benefit of the beneficiary. A jurisdiction in which Article 4A [Title 30, chapter 4A] is not in effect may follow a different rule or it may not have a clear rule. Under Section 4A-507(a)(3) [30-4A-507(1)(c)] the issue is governed by the law of the jurisdiction in which the beneficiary's bank is located. Since the payment to the beneficiary is made through the beneficiary's bank it is reasonable that the issue of when payment occurs be governed by the law of the jurisdiction in which the bank is located. Since it is difficult in many cases to determine where a beneficiary is located, the location of the beneficiary's bank provides a more certain rule.

3. Subsection (b) [subsection (2) of this section] deals with choice-of-law agreements and it gives maximum freedom of choice. Since the law of funds transfers is not highly developed in the case law there may be a strong incentive to choose the law of a jurisdiction in which Article 4A [Title 30, chapter 4A] is in effect because it provides a greater degree of certainly with respect to the rights of various parties. With respect to commercial transactions, it is often said that "[u]niformity and predictability based upon commercial convenience are the prime considerations in making the choice of governing law . . . ." R. Leflar, American Conflicts Law, § 185 (1977). Subsection (b) [subsection (2) of this section] is derived in part from recently enacted choice-of-law rules in the States of New York and California. N.Y. Gen. Obligations Law 5-1401 (McKinney's 1989 Supp.) and California Civil Code § 1646.5. This broad endorsement of freedom of contract is an enhancement of the approach taken by Restatement (Second) of Conflict of Laws § 187(b) (1971). The Restatement recognizes the basic right of freedom of contract, but the freedom granted the parties may be more limited than the freedom granted here. Under the formulation of the Restatement, if there is no substantial relationship to the jurisdiction whose law is selected and there is no "other" reasonable basis for the parties' choice, then the selection of the parties need not be honored by a court. Further, if the choice is violative of a fundamental policy of a state which has a materially greater interest than the chosen state, the selection could be disregarded by a court. Those limitations are not found in subsection (b) [subsection (2) of this section].

4. Subsection (c) [subsection (3) of this section] may be the most important provision in regard to creating uniformity of law in funds transfers. Most rights stated in Article 4A [Title 30, chapter 4A] regard parties who are in privity of contract such as originator and beneficiary,

sender and receiving bank, and beneficiary's bank and beneficiary. Since they are in privity they can make a choice of law by agreement. But that is not always the case. For example, an intermediary bank that improperly executes a payment order is not in privity with either the originator or the beneficiary. The ability of a funds transfer system to make a choice of law by rule is a convenient way of dispensing with individual agreements and to cover cases in which agreements are not feasible. It is probable that funds transfer systems will adopt a governing law to increase the certainty of commercial transactions that are effected over such systems. A system rule might adopt the law of an Article 4A [Title 30, chapter 4A] state to govern transfers on the system in order to provide a consistent, unitary, law governing all transfers made on the system. To the extent such system rules develop, individual choice-of-law agreements become unnecessary.

Subsection (c) [subsection (3) of this section] has broad application. A system choice of law applies not only to rights and obligations between banks that use the system, but may also apply to other parties to the funds transfer so long as some part of the transfer was carried out over the system. The originator and any other sender or receiving bank in the funds transfer is bound if at the time it issues or accepts a payment order it had notice that the funds transfer involved use of the system and that the system chose the law of a particular jurisdiction. Under Section 4A-107 [30-4A-107], the Federal Reserve by regulation could make a similar choice of law to govern funds transfers carried out by use of Federal Reserve Banks. Subsection (d) [subsection (4) of this section] is a limitation on subsection (c) [subsection (3) of this section]. If parties have made a choice-of-law agreement that conflicts with a choice of law made under subsection (c) [subsection (3) of this section], the agreement prevails.

5. Subsection (e) [subsection (5) of this section] addresses the case in which a funds transfer involves more than one funds transfer system and the systems adopt conflicting choice-of-law rules. The rule that has the most significant relationship to the matter at issue prevails. For example, each system should be able to make a choice of law governing payment orders transmitted over that system with regard to a choice of law made by another system.

CHAPTER 5
UNIFORM COMMERCIAL CODE
LETTERS OF CREDIT

Chapter Official Comment

Reporter's Prefatory Note to 1997 Revision:

Reason for Revision

When the original Article 5 [Title 30, chapter 5] was drafted 40 years ago, it was written for paper transactions and before many innovations in letters of credit. Now electronic and other media are used extensively. Since the 50's, standby letters of credit have developed and now nearly $500 billion standby letters of credit are issued annually worldwide, of which $250 billion are issued in the United States. The use of deferred payment letters of credit has also greatly increased. The customs and practices for letters of credit have evolved and are reflected in the Uniform Customs and Practice (UCP), usually incorporated into letters of credit, particularly international letters of credit, which have seen four revisions since the 1950's; the current version became effective in 1994 (UCP 500). Lastly, in a number of areas, court decisions have resulted in conflicting rules.

Prior to the appointment of a drafting committee, the ABA UCC Committee appointed a Task Force composed of knowledgeable practitioners and academics. The ABA Task Force studied the case law, evolving technologies and the changes in customs and practices. The Task Force identified a large number of issues which they discussed at some length, and made recommendations for revisions to Article 5 [Title 30, chapter 5]. The Task Force stated in a foreword:

"As a result of these increases and changes in usage, practice, players, and pressure, it comes as no surprise that there has been a sizable increase in litigation. Indeed, the approximately 62 cases reported in the United States in 1987 constituted double the cumulative reported cases up to 1965 . . . .

Moreover, almost forty years of hard use have revealed weaknesses, gaps and errors in the original statute which compromise its relevance. U.C.C. Article 5 [Title 30, chapter 5] was one of the few areas of the Uniform Commercial Code which did not benefit from prior codification and it should come as no surprise that it may require some revision . . . .

Measured in terms of these areas which are vital to any system of commercial law, the current combination of statute and case law is found wanting in major respects both as to predictability and certainty. What is at issue here are not matters of sophistry but important issues of substance which have not been resolved by the current case law/code method and which admit of little likelihood of such resolution." (45 Bus. Lawyer 1521, at 1532, 1535-6)

The Drafting Committee began its deliberations with the Task Force Report in hand. The final work of the Drafting Committee varies from many of the suggestions of the Task Force.

Need for Uniformity

Letters of Credit are a major instrument in international trade, as well as domestic transactions. To facilitate its usefulness and competitiveness, it is essential that U.S. law be in harmony with international rules and practices, as well as flexible enough to accommodate changes in technology and practices that have, and are, evolving. Not only should the rules be consistent within the United States, but they need to be substantively and procedurally consistent with international practices.

Thus, the goals of the drafting effort were:

- conforming the Article 5 [Title 30, chapter 5] rules to current customs and practices;
- accommodating new forms of Letters of Credit, changes in customs and practices, and evolving technology, particularly the use of electronic media;
- maintaining Letters of Credit as an inexpensive and efficient instrument facilitating trade; and
- resolving conflicts among reported decisions.

Process of Achieving Uniformity

The essence of uniform law revision is to obtain a sufficient consensus and balance among the interests of the various participants so that universal and uniform enactment by the various States may be achieved.

In part this is accomplished by extensive consultation on and broad circulation of the drafts from 1990, when the project began, until approval of the final draft by the American law Institute (ALI) and the National Conference of Commissioners on Uniform State Laws (NCCUSL).

Hundreds of groups were invited to participate in the drafting process. Twenty Advisors were appointed, representing a cross-section of interested parties. In addition 20 Observers regularly attended drafting meetings and over 100 were on the mailing list to receive all drafts of the revision.

The Drafting Committee meetings were open and all those who attended were afforded full opportunity to express their views and participate in the dialogue. The Advisors and Observers were a balanced group with ten representatives of users (Beneficiaries and Applicants); five representatives of governmental agencies; five representatives of the U.S. Council on International Banking (USCIB); seven from major banks in letter of credit transactions; eight from regional banks; and seven law professors who teach and write on Letters of Credit.

Nine Drafting Committee meetings were held that began Friday morning and ended Sunday noon. In addition, the draft was twice debated in full by NCCUSL, once by the ALI Council, once considered by the ALI Consultative Group and once by an ad hoc Committee of the Council; and reviewed and discussed by the ABA Subcommittee on Letters of Credit semi-annually and by several state and city bar association committees.

The drafts were regularly reviewed and discussed in The Business Lawyer, Letter of Credit Update, and in other publications.

Balance of Benefits

Uniform laws can be enacted only if there is a consensus that the benefits achieved advance the public interest in a manner that can be embraced by all users of the law. It appears that as drafted, Revised Article 5 [Title 30, chapter 5] will enjoy substantial support by the participating interests in letter of credit transactions.

Benefits of Revised Article 5 [Title 30, chapter 5] in General

Independence Principle. Revised Article 5 [Title 30, chapter 5] clearly and forcefully states the independence of the letter of credit obligations from the underlying transactions that was unexpressed in, but was a fundamental predicate for, the original Article 5 [Title 30, chapter 5] (Sections 5-103(d) and 5-108(f) [former 30-5-103(4) and 30-5-108(6)]). Certainty of payment, independent of other claims, setoffs or other causes of action, is a core element of the commercial utility of letters of credit.

Clarifications. The revision authorizes the use of electronic technology (Sections 5-102(a)(14) and 5-104 [30-5-122(1)(n) and 30-5-124]); expressly permits deferred payment letters of credit (Section 5-102(a)(8) [30-5-122(1)(h))] and two party letters of credit (Section 5-102(a)(10) [30-5-122(1)(j)]); provides rules for unstated expiry dates (Section 5-106(c) [30-5-126(3)]), perpetual letters of credit (Section 5-106(d) [30-5-126(4)]), and non-documentary conditions (Section 5-108(g) [30-5-128(7)]); clarifies and establishes rules for successors by operation of law (Sections 5-102(a)(15) and 5-113 [30-5-122 (1)(o) and 30-5-133]); conforms to existing practice for assignment of proceeds (Section 5-114 [30-5-134]); and clarifies the rules where decisions have been in conflict (Section 5-106 [30-5-126], Comment 1; Section 5-108 [30-5-128], Comments 1, 3, 4, 7, and 9; Section 5-109 [30-5-129], Comments 1 and 3; Section 5-113 [30-5-133], Comment 1; and Section 5-117 [30-5-137], Comment 1).Harmonizes with International Practice

The UCP is used in most international letters of credit and in many domestic letters of credit. These international practices are well known and employed by the major issuers and users of letters of credit. Revisions have been made to Article 5 [Title 30, chapter 5] to coordinate the Article 5 [Title 30, chapter 5] rules with current international practice (e.g., deferred payment obligations, reasonable time to examine documents, preclusion, non-documentary conditions, return of documents, and irrevocable unless stated to be revocable).

Benefits of Revised Article 5 [Title 30, chapter 5] to Issuers

Consequential Damages. Section 5-111 [30-5-131] precludes consequential and punitive damages. It, however, provides strong incentives for Issuers to honor, including provisions for attorneys fees and expenses of litigation, interest, and specific performance. If consequential and punitive damages were allowed, the cost of letters of credit could rise substantially.

Statute of Limitation. Section 5-115 [30-5-135] establishes a one year statute of limitation from the expiration date or from accrual of the cause of action, whichever occurs later. Because it is usually obvious to all when there has been a breach, a short limitation period is fair to potential plaintiffs.

Choice of Law. Section 5-116 [30-5-136] permits the issuer (or nominated party or adviser) to choose the law of the jurisdiction that will govern even if that law bears no relation to the transaction. Absent agreement, Section 5-116 [30-5-136] states choice of law rules.

Assignment of Proceeds. Section 5-114 [30-5-134] conforms more fully to existing practice and provides an orderly procedure for recording and accommodating assignments by consent of the issuer (or nominated party).

Subrogation. Section 5-117 [30-5-137] clarifies the subrogation rights of an Issuer who has honored a letter of credit. These rights of subrogation also extend to an applicant who reimburses and a nominated party who pays or gives value.

Recognition of UCP. Section 5-116(c) [30-5-136(3)] expressly recognizes that if the UCP is incorporated by reference into the letter of credit, the agreement varies the provisions of Article 5 [Title 30, chapter 5] with which it may conflict except for the non-variable provisions of Article 5 [Title 30, chapter 5].Benefits of Revised Article 5 [Title 30, chapter 5] to Applicants

Warranties. Section 5-110 [30-5-130] specifies the warranties made by a beneficiary. It gives the applicant on a letter of credit which has been honored a direct cause of action if a drawing is fraudulent or forged or if a drawing violates any agreement augmented by a letter of credit.

Strict Compliance. Absent agreement to the contrary, the issuer must dishonor a presentation that does not strictly comply under standard practice with the terms and conditions of the letter of credit (Section 5-108 [30-5-128]).

Subrogation. New Section 5-117 [30-5-137] clarifies the parties rights of subrogation if the letter of credit is honored.

Limitations on General Disclaimers and Waivers. Section 5-103(c) [30-5-123(3)] limits the effect of general disclaimers and waivers in a letter of credit, or reimbursement or other agreement.Benefits of Revised Article 5 [Title 30, chapter 5] to Beneficiaries

Irrevocable. A letter of credit is irrevocable unless the letter of credit expressly provides it is revocable (Section 5-106(a) [30-5-126(1)]).

Preclusion. Section 5-108(c) [30-5-128(3)] now provides that the Issuer is precluded from asserting any discrepancy not stated in its notice timely given, except for fraud, forgery or expiration.

Timely Examination. Section 5-108(b) [30-5-128(2)] requires examination and notice of any discrepancies within a reasonable time not to exceed the 7th business day after presentation of the documents.

Transfers by Operation of Law. New Section 5-113 [30-5-133] allows a successor to a beneficiary by operation of law to make presentation and receive payment or acceptance.

Damages. The damages provided are expanded and clarified. They include attorneys fees and expenses of litigation and payment of the full amount of the wrongfully dishonored or repudiated demand, with interest, without an obligation of the beneficiary to mitigate damages (Section 5-111 [30-5-131]).Revisions for Article 9 [Title 30, chapter 9A] and Transition Provisions

The draft includes suggested revisions to conform Article 9 [Title 30, chapter 9A] to the Article 5 [Title 30, chapter 5] changes. Article 9 [Title 30, chapter 9A] itself is under revision and the interface with Revised Article 5 [Title 30, chapter 5] will be more fully examined by the Article 9 [Title 30, chapter 9A] drafting committee, as well, in light of changes to Article 9 [Title 30, chapter 9A]. The Article 9 [Title 30, chapter 9A] revisions will probably not be completed until 1998-9. Revised Article 8 (1994) [Title 30, chapter 8] also makes changes to Article 9 [Title 30, chapter 9A] so care should be taken to coordinate the changes of both Revised Articles 5 and 8 [Title 30, chapters 5 and 8] within each State.

The draft also includes transition provisions and some cross reference changes in other Articles of the UCC.

Chapter Compiler's Comments

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Part 1
Letters of Credit

30-5-101. Short title.

Official Comment

Source: Section 5-101, U.C.C.

Official Comment: The Official Comment to the original Section 5-101 [30-5-101] was a remarkably brief inaugural address. Noting that letters of credit had not been the subject of statutory enactment and that the law concerning them had been developed in the cases, the Comment stated that Article 5 [Title 30, chapter 5] was intended "within its limited scope" to set an independent theoretical frame for the further development of letters of credit. That statement addressed accurately conditions as they existed when the statement was made, nearly half a century ago. Since Article 5 [Title 30, chapter 5] was originally drafted, the use of letters of credit has expanded and developed, and the case law concerning these developments is, in some respects, discordant.

Revision of Article 5 [Title 30, chapter 5] therefore has required reappraisal both of the statutory goals and of the extent to which particular statutory provisions further or adversely affect achievement of those goals.

The statutory goal of Article 5 [Title 30, chapter 5] was originally stated to be: (1) to set a substantive theoretical frame that describes the function and legal nature of letters of credit; and (2) to preserve procedural flexibility in order to accommodate further development of the efficient use of letters of credit. A letter of credit is an idiosyncratic form of undertaking that supports performance of an obligation incurred in a separate financial, mercantile, or other transaction or arrangement. The objectives of the original and revised Article 5 [Title 30, chapter 5] are best achieved (1) by defining the peculiar characteristics of a letter of credit that distinguish it and the legal consequences of its use from other forms of assurance such as secondary guarantees, performance bonds, and insurance policies, and from ordinary contracts, fiduciary engagements, and escrow arrangements; and (2) by preserving flexibility through variation by agreement in order to respond to and accommodate developments in custom and usage that are not inconsistent with the essential definitions and substantive mandates of the statute. No statute can, however, prescribe the manner in which such substantive rights and duties are to be enforced or imposed without risking stultification of wholesome developments in the letter of credit mechanism. Letter of credit law should remain responsive to commercial reality and in particular to the customs and expectations of the international banking and mercantile community. Courts should read the terms of this article [chapter] in a manner consistent with these customs and expectations.

The subject matter in Article 5 [Title 30, chapter 5], letters of credit, may also be governed by an international convention that is now being drafted by UNCITRAL, the draft Convention on Independent Guarantees and Standby Letters of Credit. The Uniform Customs and Practice is an international body of trade practice that is commonly adopted by international and domestic letters of credit and as such is the "law of the transaction" by agreement of the parties. Article 5 [Title 30, chapter 5] is consistent with and was influenced by the rules in the existing version of the UCP. In addition to the UCP and the international convention, other bodies of law apply to letters of credit. For example, the federal bankruptcy law applies to letters of credit with respect to applicants and beneficiaries that are in bankruptcy; regulations of the Federal Reserve Board and the Comptroller of the Currency lay out requirements for banks that issue letters of credit and describe how letters of credit are to be treated for calculating asset risk and for the purpose of loan limitations. In addition there is an array of anti-boycott and other similar laws that may affect the issuance and performance of letters of credit. All of these laws are beyond the scope of Article 5 [Title 30, chapter 5], but in certain circumstances they will override Article 5 [Title 30, chapter 5].

30-5-118. Security interest of issuer or nominated person.

Official Comments

[*Purpose:*]

1. This section gives the issuer of a letter of credit or a nominated person thereunder an automatic perfected security interest in a "document" (as that term is defined in Section 5-102(a)(6) [30-5-122(1)(f)]). The security interest arises only if the document is presented to the issuer or nominated person under the letter of credit and only to the extent of the value that is given. This security interest is analogous to that awarded to a collecting bank under Section 4-210 [30-4-210]. Subsection (b) [subsection 2] contains special rules governing the security interest arising under this section. In all other respects, a security interest arising under this section is subject to Article 9 [Title 30, chapter 9A]. See Section 9-109 [30-9A-109]. Thus, for example, a security interest arising under this section may give rise to a security interest in proceeds under Section 9-315 [30-9A-315].

2. Subsection (b)(1) [subsection (2)(a)] makes a security agreement unnecessary to the creation of a security interest under this section. Under subsection (b)(2) [subsection (2)(b)], a security interest arising under this section is perfected if the document is presented in a medium other than a written or tangible medium. Documents that are written and that are not an otherwise-defined type of collateral under Article 9 [Title 30, chapter 9A] (e.g., an invoice or inspection certificate) may be goods, in which an issuer or nominated person could perfect its security interest by possession. Because the definition of document in Section 5-102(a)(6) [30-5-122(1)(f)] includes records (e.g., electronic records) that may not be goods, subsection (b)(2) [subsection (2)(b)] provides for automatic perfection (i.e., without filing or possession).

Under subsection (b)(3) [subsection (2)(c)], if the document (i) is in a written or tangible medium, (ii) is not a certificated security, chattel paper, a document of title, an instrument, or a letter of credit, and (iii) is not in the debtor's possession, the security interest is perfected and has priority over a conflicting security interest. If the document is a type of tangible collateral that subsection (b)(3) [subsection (2)(c)] excludes from its perfection and priority rules, the issuer or nominated person must comply with the normal method of perfection (e.g., possession of an instrument) and is subject to the applicable Article 9 [Title 30, chapter 9A] priority rules. Documents to which subsection (b)(3) [subsection (2)(c)] applies may be important to an issuer or nominated person. For example, a confirmer who pays the beneficiary must be assured that its rights to all documents are not impaired. It will find it necessary to present all of the required documents to the issuer in order to be reimbursed. Moreover, when a nominated person sends documents to an issuer in connection with the nominated person's reimbursement, that activity is not a collection, enforcement, or disposition of collateral under Article 9 [Title 30, chapter 9A].

One purpose of this section is to protect an issuer or nominated person from claims of a beneficiary's creditors. It is a fallback provision inasmuch as issuers and nominated persons frequently may obtain and perfect security interests under the usual Article 9 [Title 30, chapter 9A] rules, and, in many cases, the documents will be owned by the issuer, nominated person, or applicant.

30-5-122. Definitions.

Official Comment

[*Corresponding U.C.C. Section:* Section 5-102, U.C.C.]

Source: Section 5-102, U.C.C.

Official Comment: 1. Since no one can be a confirmer unless that person is a nominated person as defined in Section 5-102(a)(11) [30-5-122(1)(k)], those who agree to "confirm" without the designation or authorization of the issuer are not confirmers under Article 5 [Title 30, chapter 5]. Nonetheless, the undertakings to the beneficiary of such persons may be enforceable by the beneficiary as letters of credit issued by the "confirmer" for its own account or as guarantees or contracts outside of Article 5 [Title 30, chapter 5].

2. The definition of "document" contemplates and facilitates the growing recognition of electronic and other nonpaper media as "documents," however, for the time being, data in those media constitute documents only in certain circumstances. For example, a facsimile received by an issuer would be a document only if the letter of credit explicitly permitted it, if the standard practice authorized it and the letter did not prohibit it, or the agreement of the issuer and beneficiary permitted it. The fact that data transmitted in a nonpaper (unwritten) medium can be recorded on paper by a recipient's computer printer, facsimile machine, or the like does not under current practice render the data so transmitted a "document." A facsimile or S.W.I.F.T. message received directly by the issuer is in an electronic medium when it crosses the boundary of the issuer's place of business. One wishing to make a presentation by facsimile (an electronic medium) will have to procure the explicit agreement of the issuer (assuming that the standard practice does not authorize it). Article 5 [Title 30, chapter 5] contemplates that electronic documents may be presented under a letter of credit and the provisions of this Article [Title 30, chapter 5] should be read to apply to electronic documents as well as tangible documents. An electronic document of title is delivered through the voluntary transfer of control. Article 1, Section 1-201 [30-1-201] (definition of "delivery"). See Article 7, Section 7-106 [30-7-107] on control of an electronic document. Where electronic transmissions are authorized neither by the letter of credit nor by the practice, the beneficiary may transmit the data electronically to its agent who may be able to put it in written form and make a conforming presentation. Cf. Article 7, Section 7-105 [30-7-106] on reissuing an electronic document in a tangible medium.

3. "Good faith" continues in revised Article 5 [Title 30, chapter 5] to be defined as "honesty in fact." "Observance of reasonable standards of fair dealing" has not been added to the definition. The narrower definition of "honesty in fact" reinforces the "independence principle" in the treatment of "fraud," "strict compliance," "preclusion," and other tests affecting the performance of obligations that are unique to letters of credit. This narrower definition — which does not include "fair dealing" — is appropriate to the decision to honor or dishonor a presentation of documents specified in a letter of credit. The narrower definition is also appropriate for other parts of revised Article 5 [Title 30, chapter 5] where greater certainty of obligations is necessary and is consistent with the goals of speed and low cost. It is important that U.S. letters of credit have continuing vitality and competitiveness in international transactions.

For example, it would be inconsistent with the "independence" principle if any of the following occurred: (i) the beneficiary's failure to adhere to the standard of "fair dealing" in the underlying transaction or otherwise in presenting documents were to provide applicants and issuers with an "unfairness" defense to dishonor even when the documents complied with the terms of the letter of credit; (ii) the issuer's obligation to honor in "strict compliance in accordance with standard practice" were changed to "reasonable compliance" by use of the "fair dealing" standard, or (iii) the preclusion against the issuer (Section 5-108(d) [30-5-128(4)]) were modified under the "fair dealing" standard to enable the issuer later to raise additional deficiencies in the presentation. The rights and obligations arising from presentation, honor, dishonor and reimbursement, are independent and strict, and thus "honesty in fact" is an appropriate standard.

The contract between the applicant and beneficiary is not governed by Article 5 [Title 30, chapter 5], but by applicable contract law, such as Article 2 [Title 30, chapter 2] or the general law of contracts. "Good faith" in that contract is defined by other law, such as Section 2-103(1)(b) [30-2-103(1)(b)] or Restatement of Contracts 2d, § 205, which incorporate the principle of "fair dealing" in most cases, or a State's common law or other statutory provisions that may apply to that contract.

The contract between the applicant and the issuer (sometimes called the "reimbursement" agreement) is governed in part by this article [chapter] (e.g., Sections 5-108(i) [30-5-128(9)], 5-111(b) [30-5-131(2)], and 5-103(c) [30-5-123(3)]) and partly by other law (e.g., the general law of contracts). The definition of good faith in Section 5-102(a)(7) [30-5-122(1)(g)] applies only to the extent that the reimbursement contract is governed by provisions in this article [chapter]; for other purposes good faith is defined by other law.

4. Payment and acceptance are familiar modes of honor. A third mode of honor, incurring an unconditional obligation, has legal effects similar to an acceptance of a time draft but does not technically constitute an acceptance. The practice of making letters of credit available by "deferred payment undertaking" as now provided in UCP 500 has grown up in other countries and spread to the United States. The definition of "honor" will accommodate that practice.

5. The exclusion of consumers from the definition of "issuer" is to keep creditors from using a letter of credit in consumer transactions in which the consumer might be made the issuer and the creditor would be the beneficiary. If that transaction were recognized under Article 5 [Title 30, chapter 5], the effect would be to leave the consumer without defenses against the creditor. That outcome would violate the policy behind the Federal Trade Commission Rule in 16 CFR Part 433. In a consumer transaction, an individual cannot be an issuer where that person would otherwise be either the principal debtor or a guarantor.

6. The label on a document is not conclusive; certain documents labelled "guarantees" in accordance with European (and occasionally, American) practice are letters of credit. On the other hand, even documents that are labelled "letter of credit" may not constitute letters of credit under the definition in Section 5-102(a) [30-5-122(1)]. When a document labelled a letter of credit requires the issuer to pay not upon the presentation of documents, but upon the determination of an extrinsic fact such as applicant's failure to perform a construction contract, and where that condition appears on its face to be fundamental and would, if ignored, leave no obligation to the issuer under the document labelled letter of credit, the issuer's undertaking is not a letter of credit. It is probably some form of suretyship or other contractual arrangement and may be enforceable as such. See Sections 5-102(a)(10) [30-5-122(1)(j)] and 5-103(d) [30-5-123(4)]. Therefore, undertakings whose fundamental term requires an issuer to look beyond documents and beyond conventional reference to the clock, calendar, and practices concerning the form of various documents are not governed by Article 5 [Title 30, chapter 5]. Although Section 5-108(g) [30-5-128(7)] recognizes that certain nondocumentary conditions can be included in a letter of credit without denying the undertaking the status of letter of credit, that section does not apply to cases where the nondocumentary condition is fundamental to the issuer's obligation. The rules in Sections 5-102(a)(10) [30-5-122(1)(j)], 5-103(d) [30-5-123(4)], and 5-108(g) [30-5-128(7)] approve the conclusion in Wichita Eagle & Beacon Publishing Co. v. Pacific Nat. Bank, 493 F.2d 1285 (9th Cir. 1974).

The adjective "definite" is taken from the UCP. It approves cases that deny letter of credit status to documents that are unduly vague or incomplete. See, e.g., Transparent Products Corp. v. Paysaver Credit Union, 864 F.2d 60 (7th Cir. 1988). Note, however, that no particular phrase or label is necessary to establish a letter of credit. It is sufficient if the undertaking of the issuer shows that it is intended to be a letter of credit. In most cases the parties' intention will be indicated by a label on the undertaking itself indicating that it is a "letter of credit," but no such language is necessary.

A financial institution may be both the issuer and the applicant or the issuer and the beneficiary. Such letters are sometimes issued by a bank in support of the bank's own lease obligations or on behalf of one of its divisions as an applicant or to one of its divisions as beneficiary, such as an overseas branch. Because wide use of letters of credit in which the issuer and the applicant or the issuer and the beneficiary are the same would endanger the unique status of letters of credit, only financial institutions are authorized to issue them.

In almost all cases the ultimate performance of the issuer under a letter of credit is the payment of money. In rare cases the issuer's obligation is to deliver stock certificates or the like. The definition of letter of credit in Section 5-102(a)(10)[30-5-122(1)(j)] contemplates those cases.

7. Under the UCP any bank is a nominated bank where the letter of credit is "freely negotiable." A letter of credit might also nominate by the following: "We hereby engage with the drawer, indorsers, and bona fide holders of drafts drawn under and in compliance with the terms of this credit that the same will be duly honored on due presentation" or "available with any bank by negotiation." A restricted negotiation credit might be "available with x bank by negotiation" or the like.

Several legal consequences may attach to the status of nominated person. First, when the issuer nominates a person, it is authorizing that person to pay or give value and is authorizing the beneficiary to make presentation to that person. Unless the letter of credit provides otherwise, the beneficiary need not present the documents to the issuer before the letter of credit expires; it need only present those documents to the nominated person. Secondly, a nominated person that gives value in good faith has a right to payment from the issuer despite fraud. Section 5-109(a)(1) [30-5-129(1)(a)].

8. A "record" must be in or capable of being converted to a perceivable form. For example, an electronic message recorded in a computer memory that could be printed from that memory could constitute a record. Similarly, a tape recording of an oral conversation could be a record.

9. Absent a specific agreement to the contrary, documents of a beneficiary delivered to an issuer or nominated person are considered to be presented under the letter of credit to which

they refer, and any payment or value given for them is considered to be made under that letter of credit. As the court held in Alaska Textile Co. v. Chase Manhattan Bank, N.A., 982 F.2d 813, 820 (2d Cir. 1992), it takes a "significant showing" to make the presentation of a beneficiary's documents for "collection only" or otherwise outside letter of credit law and practice.

10. Although a successor of a beneficiary is one who succeeds "by operation of law," some of the successions contemplated by Section 5-102(a)(15) [30-5-122(1)(o)] will have resulted from voluntary action of the beneficiary such as merger of a corporation. Any merger makes the successor corporation the "successor of a beneficiary" even though the transfer occurs partly by operation of law and partly by the voluntary action of the parties. The definition excludes certain transfers, where no part of the transfer is "by operation of law" — such as the sale of assets by one company to another.

11. "Draft" in Article 5 [Title 30, chapter 5] does not have the same meaning it has in Article 3 [Title 30, chapter 3]. For example, a document may be a draft under Article 5 [Title 30, chapter 5] even though it would not be a negotiable instrument, and therefore would not qualify as a draft under Section 3-104(e) [30-3-104(5)].

Case Notes

Letter of Credit — Guaranty Distinguished: Plaintiff agreed to lend Prospect Associates, Inc. (Prospect) money to finance construction of a subdivision. As part of the security for the loan, Prospect was required to obtain a letter of credit with plaintiff as beneficiary. Prospect defaulted on the promissory note evidencing the loan. Defendant refused payment on the letter of credit, contending it was a guaranty on which it was not primarily liable. The District Court granted summary judgment to plaintiff, and defendant appealed. The Supreme Court affirmed the decision, saying the document was clearly entitled a letter of credit and its intent was to hold the bank primarily liable upon nonperformance of one of the named instruments, as opposed to secondarily liable as under a guaranty. Sherwood & Roberts, Inc. v. First Security Bank, 209 M 402, 682 P2d 149, 41 St. Rep. 787 (1984).

Letter of Credit — What Constitutes: The Court found that an instrument entitled "letter of instruction and joint assignment of funds" was not a letter of credit because it did not meet the definition in 30-5-103 (substance now in 30-5-122) and its terms had not been met. The issuing bank had not agreed to be primarily liable. Boise Cascade Corp. v. First Sec. Bank of Anaconda, 183 M 378, 600 P2d 173 (1979).

30-5-123. Scope.

Official Comment

Source: Section 5-103, U.C.C.

Official Comment:

1. Sections 5-102(a)(10) [30-5-122(1)(j)] and 5-103 [30-5-123] are the principal limits on the scope of Article 5 [Title 30, chapter 5]. Many undertakings in commerce and contract are similar, but not identical to the letter of credit. Principal among those are "secondary," "accessory," or "suretyship" guarantees. Although the word "guarantee" is sometimes used to describe an independent obligation like that of the issuer of a letter of credit (most often in the case of European bank undertakings but occasionally in the case of undertakings of American banks), in the United States the word "guarantee" is more typically used to describe a suretyship transaction in which the "guarantor" is only secondarily liable and has the right to assert the underlying debtor's defenses. This article [chapter] does not apply to secondary or accessory guarantees and it is important to recognize the distinction between letters of credit and those guarantees. It is often a defense to a secondary or accessory guarantor's liability that the underlying debt has been discharged or that the debtor has other defenses to the underlying liability. In letter of credit law, on the other hand, the independence principle recognized throughout Article 5 [Title 30, chapter 5] states that the issuer's liability is independent of the underlying obligation. That the beneficiary may have breached the underlying contract and thus have given a good defense on that contract to the applicant against the beneficiary is no defense for the issuer's refusal to honor. Only staunch recognition of this principle by the issuers and the courts will give letters of credit the continuing vitality that arises from the certainty and speed of payment under letters of credit. To that end, it is important that the law not carry into letter of credit transactions rules that properly apply only to secondary guarantees or to other forms of engagement.

2. Like all of the provisions of the Uniform Commercial Code, Article 5 [Title 30, chapter 5] is supplemented by Section 1-103 [30-1-103] and, through it, by many rules of statutory and common law. Because this article [chapter] is quite short and has no rules on many issues that will affect liability with respect to a letter of credit transaction, law beyond Article 5 [Title 30,

chapter 5] will often determine rights and liabilities in letter of credit transactions. Even within letter of credit law, the article [chapter] is far from comprehensive; it deals only with "certain" rights of the parties. Particularly with respect to the standards of performance that are set out in Section 5-108 [30-5-128], it is appropriate for the parties and the courts to turn to customs and practice such as the Uniform Customs and Practice for Documentary Credits, currently published by the International Chamber of Commerce as I.C.C. Pub. No. 500 (hereafter UCP). Many letters of credit specifically adopt the UCP as applicable to the particular transaction. Where the UCP are adopted but conflict with Article 5 [Title 30, chapter 5] and except where variation is prohibited, the UCP terms are permissible contractual modifications under Sections 1-102(3) [30-1-102(3)] and 5-103(c) [30-5-123(3)]. See Section 5-116(c) [30-5-136(3)]. Normally Article 5 [Title 30, chapter 5] should not be considered to conflict with practice except when a rule explicitly stated in the UCP or other practice is different from a rule explicitly stated in Article 5 [Title 30, chapter 5].

Except by choosing the law of a jurisdiction that has not adopted the Uniform Commercial Code, it is not possible entirely to escape the Uniform Commercial Code. Since incorporation of the UCP avoids only "conflicting" Article 5 [Title 30, chapter 5] rules, parties who do not wish to be governed by the nonconflicting provisions of Article 5 [Title 30, chapter 5] must normally either adopt the law of a jurisdiction other than a State of the United States or state explicitly the rule that is to govern. When rules of custom and practice are incorporated by reference, they are considered to be explicit terms of the agreement or undertaking.

Neither the obligation of an issuer under Section 5-108 [30-5-128] nor that of an adviser under Section 5-107 [30-5-127] is an obligation of the kind that is invariable under Section 1-102(3) [30-1-102(3)]. Section 5-103(c) [30-5-123(3)] and Comment 1 to Section 5-108 [30-5-128] make it clear that the applicant and the issuer may agree to almost any provision establishing the obligations of the issuer to the applicant. The last sentence of subsection (c) [subsection (3)] limits the power of the issuer to achieve that result by a nonnegotiated disclaimer or limitation of remedy.

What the issuer could achieve by an explicit agreement with its applicant or by a term that explicitly defines its duty, it cannot accomplish by a general disclaimer. The restriction on disclaimers in the last sentence of subsection (c) [subsection (3)] is based more on procedural than on substantive unfairness. Where, for example, the reimbursement agreement provides explicitly that the issuer need not examine any documents, the applicant understands the risk it has undertaken. A term in a reimbursement agreement which states generally that an issuer will not be liable unless it has acted in "bad faith" or committed "gross negligence" is ineffective under Section 5-103(c) [30-5-123(3)]. On the other hand, less general terms such as terms that permit issuer reliance on an oral or electronic message believed in good faith to have been received from the applicant or terms that entitle an issuer to reimbursement when it honors a "substantially" though not "strictly" complying presentation, are effective. In each case the question is whether the disclaimer or limitation is sufficiently clear and explicit in reallocating a liability or risk that is allocated differently under a variable Article 5 [Title 30, chapter 5] provision.

Of course, no term in a letter of credit, whether incorporated by reference to practice rules or stated specifically, can free an issuer from a conflicting contractual obligation to its applicant. If, for example, an issuer promised its applicant that it would pay only against an inspection certificate of a particular company but failed to require such a certificate in its letter of credit or made the requirement only a nondocumentary condition that had to be disregarded, the issuer might be obliged to pay the beneficiary even though its payment might violate its contract with its applicant.

3. Parties should generally avoid modifying the definitions in Section 5-102 [30-5-122]. The effect of such an agreement is almost inevitably unclear. To say that something is a "guarantee" in the typical domestic transaction is to say that the parties intend that particular legal rules apply to it. By acknowledging that something is a guarantee, but asserting that it is to be treated as a "letter of credit," the parties leave a court uncertain about where the rules on guarantees stop and those concerning letters of credit begin.

4. Section 5-102(2) and (3) [former 30-5-102(2) and (3)] of Article 5 [Title 30, chapter 5] are omitted as unneeded; the omission does not change the law.

Compiler's Comments

2005 Amendment: Chapter 575 in (3) in first sentence near middle after "prohibited in" deleted "30-1-102(3) and". Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

Case Notes

Letter of Credit Not Instrument of Guaranty: The plaintiff brought suit against the defendant bank to enforce a letter of credit established on its behalf by an insurance company that subsequently went into liquidation. The bank moved for a change of venue, relying on state insurance laws. The Supreme Court held that a letter of credit, as opposed to an instrument of guaranty, created a primary obligation on the part of the bank that is independent from any obligations of the party that established the letter of credit. In light of the nature of a letter of credit, the bankrupt company and its status had nothing to do with the dispute between the parties; proper venue was the county where the defendant had its principal place of business. Gerling Global Reinsurance Corp. v. First Interstate Bank, 242 M 216, 789 P2d 1237, 47 St. Rep. 726 (1990). See also Glacier Nat'l Bank v. Challinor, 253 M 412, 833 P2d 1046, 49 St. Rep. 503 (1992), in which the Supreme Court held that it was not an abuse of discretion for the District Court to not allow the presentation of evidence regarding a "suretyship defense" when the instruments involved in the agreement were letters of credit.

Letter of Credit — What Constitutes: The Court found that an instrument entitled "letter of instruction and joint assignment of funds" was not a letter of credit because it did not meet the definition in 30-5-103 (substance now in 30-5-122) and its terms had not been met. The issuing bank had not agreed to be primarily liable. Boise Cascade Corp. v. First Sec. Bank of Anaconda, 183 M 378, 600 P2d 173 (1979).

30-5-124. Formal requirements.

Official Comment

Source: Section 5-104, U.C.C.

Official Comment:

1. Neither Section 5-104 [30-5-124] nor the definition of letter of credit in Section 5-102(a)(10) [30-5-122(1)(j)] requires inclusion of all the terms that are normally contained in a letter of credit in order for an undertaking to be recognized as a letter of credit under Article 5 [Title 30, chapter 5]. For example, a letter of credit will typically specify the amount available, the expiration date, the place where presentation should be made, and the documents that must be presented to entitle a person to honor. Undertakings that have the formalities required by Section 5-104 [30-5-124] and meet the conditions specified in Section 5-102(a)(10) [30-5-122(1)(j)] will be recognized as letters of credit even though they omit one or more of the items usually contained in a letter of credit.

2. The authentication specified in this section is authentication only of the identity of the issuer, confirmer, or adviser.

An authentication agreement may be by system rule, by standard practice, or by direct agreement between the parties. The reference to practice is intended to incorporate future developments in the UCP and other practice rules as well as those that may arise spontaneously in commercial practice.

3. Many banking transactions, including the issuance of many letters of credit, are now conducted mostly by electronic means. For example, S.W.I.F.T. is currently used to transmit letters of credit from issuing to advising banks. The letter of credit text so transmitted may be printed at the advising bank, stamped "original" and provided to the beneficiary in that form. The printed document may then be used as a way of controlling and recording payments and of recording and authorizing assignments of proceeds or transfers of rights under the letter of credit. Nothing in this section should be construed to conflict with that practice.

To be a record sufficient to serve as a letter of credit or other undertaking under this section, data must have a durability consistent with that function. Because consideration is not required for a binding letter of credit or similar undertaking (Section 5-105 [30-5-125]) yet those undertakings are to be strictly construed (Section 5-108 [30-5-128]), parties to a letter of credit transaction are especially dependent on the continued availability of the terms and conditions of the letter of credit or other undertaking. By declining to specify any particular medium in which the letter of credit must be established or communicated, Section 5-104 [30-5-124] leaves room for future developments.

30-5-125. Consideration.

Official Comment

Source: Section 5-105, U.C.C.

Official Comment:

It is not to be expected that any issuer will issue its letter of credit without some form of remuneration. But it is not expected that the beneficiary will know what the issuer's remuneration was or whether in fact there was any identifiable remuneration in a given case. And it might be difficult for the beneficiary to prove the issuer's remuneration. This section dispenses with this proof and is consistent with the position of Lord Mansfield in Pillans v. Van Mierop, 97 Eng.Rep. 1035 (K.B. 1765) in making consideration irrelevant.

30-5-126. Issuance, amendment, cancellation, and duration.

Official Comment

Source: Section 5-106, U.C.C.

Official Comment:

1. This section adopts the position taken by several courts, namely that letters of credit that are silent as to revocability are irrevocable. See, e.g., Weyerhaeuser Co. v. First Nat. Bank, 27 UCC Rep. Serv. 777 (S.D. Iowa 1979); West Va. Hous. Dev. Fund v. Sroka, 415 F. Supp. 1107 (W.D. Pa. 1976). This is the position of the current UCP (500). Given the usual commercial understanding and purpose of letters of credit, revocable letters of credit offer unhappy possibilities for misleading the parties who deal with them.

2. A person can consent to an amendment by implication. For example, a beneficiary that tenders documents for honor that conform to an amended letter of credit but not to the original letter of credit has probably consented to the amendment. By the same token an applicant that has procured the issuance of a transferable letter of credit has consented to its transfer and to performance under the letter of credit by a person to whom the beneficiary's rights are duly transferred. If some, but not all of the persons involved in a letter of credit transaction consent to performance that does not strictly conform to the original letter of credit, those persons assume the risk that other nonconsenting persons may insist on strict compliance with the original letter of credit. Under subsection (b) [subsection (2)] those not consenting are not bound. For example, an issuer might agree to amend its letter of credit or honor documents presented after the expiration date in the belief that the applicant has consented or will consent to the amendment or will waive presentation after the original expiration date. If that belief is mistaken, the issuer is bound to the beneficiary by the terms of the letter of credit as amended or waived, even though it may be unable to recover from the applicant.

In general, the rights of a recognized transferee beneficiary cannot be altered without the transferee's consent, but the same is not true of the rights of assignees of proceeds from the beneficiary. When the beneficiary makes a complete transfer of its interest that is effective under the terms for transfer established by the issuer, adviser, or other party controlling transfers, the beneficiary no longer has an interest in the letter of credit, and the transferee steps into the shoes of the beneficiary as the one with rights under the letter of credit. Section 5-102(a)(3) [30-5-122(1)(c)]. When there is a partial transfer, both the original beneficiary and the transferee beneficiary have an interest in performance of the letter of credit and each expects that its rights will not be altered by amendment unless it consents.

The assignee of proceeds under a letter of credit from the beneficiary enjoys no such expectation. Notwithstanding an assignee's notice to the issuer of the assignment of proceeds, the assignee is not a person protected by subsection (b) [subsection (2)]. An assignee of proceeds should understand that its rights can be changed or completely extinguished by amendment or cancellation of the letter of credit. An assignee's claim is precarious, for it depends entirely upon the continued existence of the letter of credit and upon the beneficiary's preparation and presentation of documents that would entitle the beneficiary to honor under Section 5-108 [30-5-128].

3. The issuer's right to cancel a revocable letter of credit does not free it from a duty to reimburse a nominated person who has honored, accepted, or undertaken a deferred obligation prior to receiving notice of the amendment or cancellation. Compare UCP Article 8.

4. Although all letters of credit should specify the date on which the issuer's engagement expires, the failure to specify an expiration date does not invalidate the letter of credit, or diminish or relieve the obligation of any party with respect to the letter of credit. A letter of credit that may be revoked or terminated at the discretion of the issuer by notice to the beneficiary is not "perpetual."

30-5-127. Confirmer, nominated person, and adviser.

Official Comment

Source: Section 5-107, U.C.C.

Official Comment:

1. A confirmer has the rights and obligations identified in Section 5-108 [30-5-128]. Accordingly, unless the context otherwise requires, the terms "confirmer" and "confirmation" should be read into this article wherever the terms "issuer" and "letter of credit" appear.

A confirmer that has paid in accordance with the terms and conditions of the letter of credit is entitled to reimbursement by the issuer even if the beneficiary committed fraud (see Section 5-109(a)(1)(ii) [30-5-129(1)(a)(ii)]) and, in that sense, has greater rights against the issuer than the beneficiary has. To be entitled to reimbursement from the issuer under the typical confirmed letter of credit, the confirmer must submit conforming documents, but the confirmer's presentation to the issuer need not be made before the expiration date of the letter of credit.

A letter of credit confirmation has been analogized to a guarantee of issuer performance, to a parallel letter of credit issued by the confirmer for the account of the issuer or the letter of credit applicant or both, and to a back-to-back letter of credit in which the confirmer is a kind of beneficiary of the original issuer's letter of credit. Like letter of credit undertakings, confirmations are both unique and flexible, so that no one of these analogies is perfect, but unless otherwise indicated in the letter of credit or confirmation, a confirmer should be viewed by the letter of credit issuer and the beneficiary as an issuer of a parallel letter of credit for the account of the original letter of credit issuer. Absent a direct agreement between the applicant and a confirmer, normally the obligations of a confirmer are to the issuer not the applicant, but the applicant might have a right to injunction against a confirmer under Section 5-109 [30-5-129] or warranty claim under Section 5-110 [30-5-130], and either might have claims against the other under Section 5-117 [30-5-137].

2. No one has a duty to advise until that person agrees to be an adviser or undertakes to act in accordance with the instructions of the issuer. Except where there is a prior agreement to serve or where the silence of the adviser would be an acceptance of an offer to contract, a person's failure to respond to a request to advise a letter of credit does not in and of itself create any liability, nor does it establish a relationship of issuer and adviser between the two. Since there is no duty to advise a letter of credit in the absence of a prior agreement, there can be no duty to advise it timely or at any particular time. When the adviser manifests its agreement to advise by actually doing so (as is normally the case), the adviser cannot have violated any duty to advise in a timely way. This analysis is consistent with the result of Sound of Market Street v. Continental Bank International, 819 F.2d 384 (3d Cir. 1987) which held that there is no such duty. This section takes no position on the reasoning of that case, but does not overrule the result. By advising or agreeing to advise a letter of credit, the adviser assumes a duty to the issuer and to the beneficiary accurately to report what it has received from the issuer, but, beyond determining the apparent authenticity of the letter, an adviser has no duty to investigate the accuracy of the message it has received from the issuer. "Checking" the apparent authenticity of the request to advise means only that the prospective adviser must attempt to authenticate the message (e.g., by "testing" the telex that comes from the purported issuer), and if it is unable to authenticate the message must report that fact to the issuer and, if it chooses to advise the message, to the beneficiary. By proper agreement, an adviser may disclaim its obligation under this section.

3. An issuer may issue a letter of credit which the adviser may advise with different terms. The issuer may then believe that it has undertaken a certain engagement, yet the text in the hands of the beneficiary will contain different terms, and the beneficiary would not be entitled to honor if the documents it submitted did not comply with the terms of the letter of credit as originally issued. On the other hand, if the adviser also confirmed the letter of credit, then as a confirmer it will be independently liable on the letter of credit as advised and confirmed. If in that situation the beneficiary's ultimate presentation entitled it to honor under the terms of the confirmation but not under those in the original letter of credit, the confirmer would have to honor but might not be entitled to reimbursement from the issuer.

4. When the issuer nominates another person to "pay," "negotiate," or otherwise to take up the documents and give value, there can be confusion about the legal status of the nominated person. In rare cases the person might actually be an agent of the issuer and its act might be the act of the issuer itself. In most cases the nominated person is not an agent of the issuer and has no authority to act on the issuer's behalf. Its "nomination" allows the beneficiary to present to it and earns it certain rights to payment under Section 5-109 [30-5-129] that others do not enjoy. For example, when an issuer issues a "freely negotiable credit," it contemplates that banks or

others might take up documents under that credit and advance value against them, and it is agreeing to pay those persons but only if the presentation to the issuer made by the nominated person complies with the credit. Usually there will be no agreement to pay, negotiate, or to serve in any other capacity by the nominated person, therefore the nominated person will have the right to decline to take the documents. It may return them or agree merely to act as a forwarding agent for the documents but without giving value against them or taking any responsibility for their conformity to the letter of credit.

30-5-128. Issuer's rights and obligations.

Official Comment

[*Corresponding U.C.C. Section:* Section 5-108, U.C.C.]

Source: Section 5-108, U.C.C.

Official Comment:

1. This section combines some of the duties previously included in Sections 5-114 and 5-109 [30-5-114 and 30-5-109]. Because a confirmer has the rights and duties of an issuer, this section applies equally to a confirmer and an issuer. See Section 5-107(a) [30-5-107(1)].

The standard of strict compliance governs the issuer's obligation to the beneficiary and to the applicant. By requiring that a "presentation" appear strictly to comply, the section requires not only that the documents themselves appear on their face strictly to comply, but also that the other terms of the letter of credit such as those dealing with the time and place of presentation are strictly complied with. Typically, a letter of credit will provide that presentation is timely if made to the issuer, confirmer, or any other nominated person prior to expiration of the letter of credit. Accordingly, a nominated person that has honored a demand or otherwise given value before expiration will have a right to reimbursement from the issuer even though presentation to the issuer is made after the expiration of the letter of credit. Conversely, where the beneficiary negotiates documents to one who is not a nominated person, the beneficiary or that person acting on behalf of the beneficiary must make presentation to a nominated person, confirmer, or issuer prior to the expiration date.

This section does not impose a bifurcated standard under which an issuer's right to reimbursement might be broader than a beneficiary's right to honor. However, the explicit deference to standard practice in Section 5-108(a) and (e) [30-5-128(1) and (5)] and elsewhere expands issuers' rights of reimbursement where that practice so provides. Also, issuers can and often do contract with their applicants for expanded rights of reimbursement. Where that is done, the beneficiary will have to meet a more stringent standard of compliance as to the issuer than the issuer will have to meet as to the applicant. Similarly, a nominated person may have reimbursement and other rights against the issuer based on this article, the UCP, bank-to-bank reimbursement rules, or other agreement or undertaking of the issuer. These rights may allow the nominated person to recover from the issuer even when the nominated person would have no right to obtain honor under the letter of credit.

The section adopts strict compliance, rather than the standard that commentators have called "substantial compliance," the standard arguably applied in Banco Espanol de Credito v. State Street Bank and Trust Company, 385 F.2d 230 (1st Cir. 1967) and Flagship Cruises Ltd. v. New England Merchants Nat. Bank, 569 F.2d 699 (1st Cir. 1978). Strict compliance does not mean slavish conformity to the terms of the letter of credit. For example, standard practice (what issuers do) may recognize certain presentations as complying that an unschooled layman would regard as discrepant. By adopting standard practice as a way of measuring strict compliance, this article indorses the conclusion of the court in New Braunfels Nat. Bank v. Odiorne, 780 S.W.2d 313 (Tex.Ct.App. 1989) (beneficiary could collect when draft requested payment on 'Letter of Credit No. 86-122-5' and letter of credit specified 'Letter of Credit No. 86-122-S' holding strict compliance does not demand oppressive perfectionism). The section also indorses the result in Tosco Corp. v. Federal Deposit Insurance Corp., 723 F.2d 1242 (6th Cir. 1983). The letter of credit in that case called for "drafts Drawn under Bank of Clarksville Letter of Credit Number 105." The draft presented stated "drawn under Bank of Clarksville, Clarksville, Tennessee letter of Credit No. 105." The court correctly found that despite the change of upper case "L" to a lower case "l" and the use of the word "No." instead of "Number," and despite the addition of the words "Clarksville, Tennessee," the presentation conformed. Similarly a document addressed by a foreign person to General Motors as "Jeneral Motors" would strictly conform in the absence of other defects.

Identifying and determining compliance with standard practice are matters of interpretation for the court, not for the jury. As with similar rules in Sections 4A-202(c) and 2-302 [30-4A-202(3) and 30-2-302], it is hoped that there will be more consistency in the outcomes and speedier resolution of disputes if the responsibility for determining the nature and scope of standard practice is granted to the court, not to a jury. Granting the court authority to make these decisions will also encourage the salutary practice of courts' granting summary judgment in circumstances where there are no significant factual disputes. The statute encourages outcomes such as American Coleman Co. v. Intrawest Bank, 887 F.2d 1382 (10th Cir. 1989), where summary judgment was granted.

In some circumstances standards may be established between the issuer and the applicant by agreement or by custom that would free the issuer from liability that it might otherwise have. For example, an applicant might agree that the issuer would have no duty whatsoever to examine documents on certain presentations (e.g., those below a certain dollar amount). Where the transaction depended upon the issuer's payment in a very short time period (e.g., on the same day or within a few hours of presentation), the issuer and the applicant might agree to reduce the issuer's responsibility for failure to discover discrepancies. By the same token, an agreement between the applicant and the issuer might permit the issuer to examine documents exclusively by electronic or electro-optical means. Neither those agreements nor others like them explicitly made by issuers and applicants violate the terms of Section 5-108(a) or (b) [30-5-128(1) or (2)] or Section 5-103(c) [30-5-123(3)].

2. Section 5-108(a) [30-5-128(1)] balances the need of the issuer for time to examine the documents against the possibility that the examiner (at the urging of the applicant or for fear that it will not be reimbursed) will take excessive time to search for defects. What is a "reasonable time" is not extended to accommodate an issuer's procuring a waiver from the applicant. See Article 14c of the UCP.

Under both the UCC and the UCP the issuer has a reasonable time to honor or give notice. The outside limit of that time is measured in business days under the UCC and in banking days under the UCP, a difference that will rarely be significant. Neither business nor banking days are defined in Article 5 [Title 30, chapter 5], but a court may find useful analogies in Regulation CC, 12 CFR 229.2, in state law outside of the Uniform Commercial Code, and in Article 4 [Title 30, chapter 4].

Examiners must note that the seven-day period is not a safe harbor. The time within which the issuer must give notice is the lesser of a reasonable time or seven business days. Where there are few documents (as, for example, with the mine run standby letter of credit), the reasonable time would be less than seven days. If more than a reasonable time is consumed in examination, no timely notice is possible. What is a "reasonable time" is to be determined by examining the behavior of those in the business of examining documents, mostly banks. Absent prior agreement of the issuer, one could not expect a bank issuer to examine documents while the beneficiary waited in the lobby if the normal practice was to give the documents to a person who had the opportunity to examine those together with many others in an orderly process. That the applicant has not yet paid the issuer or that the applicant's account with the issuer is insufficient to cover the amount of the draft is not a basis for extension of the time period.

This section does not preclude the issuer from contacting the applicant during its examination; however, the decision to honor rests with the issuer, and it has no duty to seek a waiver from the applicant or to notify the applicant of receipt of the documents. If the issuer dishonors a conforming presentation, the beneficiary will be entitled to the remedies under Section 5-111 [30-5-131], irrespective of the applicant's views.

Even though the person to whom presentation is made cannot conduct a reasonable examination of documents within the time after presentation and before the expiration date, presentation establishes the parties' rights. The beneficiary's right to honor or the issuer's right to dishonor arises upon presentation at the place provided in the letter of credit even though it might take the person to whom presentation has been made several days to determine whether honor or dishonor is the proper course. The issuer's time for honor or giving notice of dishonor may be extended or shortened by a term in the letter of credit. The time for the issuer's performance may be otherwise modified or waived in accordance with Section 5-106 [30-5-126].

The issuer's time to inspect runs from the time of its "receipt of documents." Documents are considered to be received only when they are received at the place specified for presentation by the issuer or other party to whom presentation is made. "Receipt of documents" when documents of title are presented must be read in light of the definition of "delivery" in Article 1, Section 1-201 [30-1-201] and the definition of "presentment" [sic] in Section 5-102(a)(12) [30-5-122(1)(l)].

Failure of the issuer to act within the time permitted by subsection (b) [subsection (2)] constitutes dishonor. Because of the preclusion in subsection (c) [subsection (3)] and the liability that the issuer may incur under Section 5-111 [30-5-131] for wrongful dishonor, the effect of such a silent dishonor may ultimately be the same as though the issuer had honored, i.e., it may owe damages in the amount drawn but unpaid under the letter of credit.

3. The requirement that the issuer send notice of the discrepancies or be precluded from asserting discrepancies is new to Article 5 [Title 30, chapter 5]. It is taken from the similar provision in the UCP and is intended to promote certainty and finality.

The section thus substitutes a strict preclusion principle for the doctrines of waiver and estoppel that might otherwise apply under Section 1-103 [30-1-103]. It rejects the reasoning in Flagship Cruises Ltd. v. New England Merchants' Nat. Bank, 569 F.2d 699 (1st Cir. 1978) and Wing On Bank Ltd. v. American Nat. Bank & Trust Co., 457 F.2d 328 (5th Cir. 1972) where the issuer was held to be estopped only if the beneficiary relied on the issuer's failure to give notice.

Assume, for example, that the beneficiary presented documents to the issuer shortly before the letter of credit expired, in circumstances in which the beneficiary could not have cured any discrepancy before expiration. Under the reasoning of Flagship and Wing On, the beneficiary's inability to cure, even if it had received notice, would absolve the issuer of its failure to give notice. The virtue of the preclusion obligation adopted in this section is that it forecloses litigation about reliance and detriment.

Even though issuers typically give notice of the discrepancy of tardy presentation when presentation is made after the expiration of a credit, they are not required to give that notice and the section permits them to raise late presentation as a defect despite their failure to give that notice.

4. To act within a reasonable time, the issuer must normally give notice without delay after the examining party makes its decision. If the examiner decides to dishonor on the first day, it would be obliged to notify the beneficiary shortly thereafter, perhaps on the same business day. This rule accepts the reasoning in cases such as Datapoint Corp. v. M & I Bank, 665 F. Supp. 722 (W.D. Wis. 1987) and Esso Petroleum Canada, Div. of Imperial Oil, Ltd. v. Security Pacific Bank, 710 F. Supp. 275 (D. Ore. 1989).

The section deprives the examining party of the right simply to sit on a presentation that is made within seven days of expiration. The section requires the examiner to examine the documents and make a decision and, having made a decision to dishonor, to communicate promptly with the presenter. Nevertheless, a beneficiary who presents documents shortly before the expiration of a letter of credit runs the risk that it will never have the opportunity to cure any discrepancies.

5. Confirmers, other nominated persons, and collecting banks acting for beneficiaries can be presenters and, when so, are entitled to the notice provided in subsection (b) [subsection (2)]. Even nominated persons who have honored or given value against an earlier presentation of the beneficiary and are themselves seeking reimbursement or honor need notice of discrepancies in the hope that they may be able to procure complying documents. The issuer has the obligations imposed by this section whether the issuer's performance is characterized as "reimbursement" of a nominated person or as "honor."

6. In many cases a letter of credit authorizes presentation by the beneficiary to someone other than the issuer. Sometimes that person is identified as a "payor" or "paying bank," or as an "acceptor" or "accepting bank," in other cases as a "negotiating bank," and in other cases there will be no specific designation. The section does not impose any duties on a person other than the issuer or confirmer, however a nominated person or other person may have liability under this article [chapter] or at common law if it fails to perform an express or implied agreement with the beneficiary.

7. The issuer's obligation to honor runs not only to the beneficiary but also to the applicant. It is possible that an applicant who has made a favorable contract with the beneficiary will be injured by the issuer's wrongful dishonor. Except to the extent that the contract between the issuer and the applicant limits that liability, the issuer will have liability to the applicant for wrongful dishonor under Section 5-111 [30-5-131] as a matter of contract law. A good faith extension of the time in Section 5-108(b) [30-5-128(2)] by agreement between the issuer and beneficiary binds the applicant even if the applicant is not consulted or does not consent to the extension.

The issuer's obligation to dishonor when there is no apparent compliance with the letter of credit runs only to the applicant. No other party to the transaction can complain if the applicant waives compliance with terms or conditions of the letter of credit or agrees to a less stringent standard for compliance than that supplied by this article [chapter]. Except as otherwise agreed with the applicant, an issuer may dishonor a noncomplying presentation despite an applicant's waiver.

Waiver of discrepancies by an issuer or an applicant in one or more presentations does not waive similar discrepancies in a future presentation. Neither the issuer nor the beneficiary can reasonably rely upon honor over past waivers as a basis for concluding that a future defective presentation will justify honor. The reasoning of Courtaulds of North America Inc. v. North Carolina Nat. Bank, 528 F.2d 802 (4th Cir. 1975) is accepted and that expressed in Schweibish v. Pontchartrain State Bank, 389 So.2d 731 (La.App. 1980) and Titanium Metals Corp. v. Space Metals, Inc., 529 P.2d 431 (Utah 1974) is rejected.

8. The standard practice referred to in subsection (e) [subsection (5)] includes (i) international practice set forth in or referenced by the Uniform Customs and Practice, (ii) other practice rules published by associations of financial institutions, and (iii) local and regional practice. It is possible that standard practice will vary from one place to another. Where there are conflicting practices, the parties should indicate which practice governs their rights. A practice may be overridden by agreement or course of dealing. See Section 1-205(4) [30-1-205(4)].

9. The responsibility of the issuer under a letter of credit is to examine documents and to make a prompt decision to honor or dishonor based upon that examination. Nondocumentary conditions have no place in this regime and are better accommodated under contract or suretyship law and practice. In requiring that nondocumentary conditions in letters of credit be ignored as surplusage, Article 5 [Title 30, chapter 5] remains aligned with the UCP (see UCP 500 Article 13c), approves cases like Pringle-Associated Mortgage Corp. v. Southern National Bank, 571 F.2d 871, 874 (5th Cir. 1978), and rejects the reasoning in cases such as Sherwood & Roberts, Inc. v. First Security Bank, 682 P.2d 149 (Mont. 1984).

Subsection (g) [subsection (7)] recognizes that letters of credit sometimes contain nondocumentary terms or conditions. Conditions such as a term prohibiting "shipment on vessels more than 15 years old," are to be disregarded and treated as surplusage. Similarly, a requirement that there be an award by a "duly appointed arbitrator" would not require the issuer to determine whether the arbitrator had been "duly appointed." Likewise a term in a standby letter of credit that provided for differing forms of certification depending upon the particular type of default does not oblige the issuer independently to determine which kind of default has occurred. These conditions must be disregarded by the issuer. Where the nondocumentary conditions are central and fundamental to the issuer's obligation (as for example a condition that would require the issuer to determine in fact whether the beneficiary had performed the underlying contract or whether the applicant had defaulted) their inclusion may remove the undertaking from the scope of Article 5 [Title 30, chapter 5] entirely. See Section 5-102(a)(10) [30-5-122(1)(j)] and Comment 6 to Section 5-102 [30-5-122].

Subsection (g) [subsection (7)] would not permit the beneficiary or the issuer to disregard terms in the letter of credit such as place, time, and mode of presentation. The rule in subsection (g) [subsection (7)] is intended to prevent an issuer from deciding or even investigating extrinsic facts, but not from consulting the clock, the calendar, the relevant law and practice, or its own general knowledge of documentation or transactions of the type underlying a particular letter of credit.

Even though nondocumentary conditions must be disregarded in determining compliance of a presentation (and thus in determining the issuer's duty to the beneficiary), an issuer that has promised its applicant that it will honor only on the occurrence of those nondocumentary conditions may have liability to its applicant for disregarding the conditions.

10. Subsection (f) [subsection (6)] condones an issuer's ignorance of "any usage of a particular trade"; that trade is the trade of the applicant, beneficiary, or others who may be involved in the underlying transaction. The issuer is expected to know usage that is commonly encountered in the course of document examination. For example, an issuer should know the common usage with respect to documents in the maritime shipping trade but would not be expected to understand synonyms used in a particular trade for product descriptions appearing in a letter of credit or an invoice.

11. Where the issuer's performance is the delivery of an item of value other than money, the applicant's reimbursement obligation would be to make the "item of value" available to the issuer.

12. An issuer is entitled to reimbursement from the applicant after honor of a forged or fraudulent drawing if honor was permitted under Section 5-109(a) [30-5-129(1)].

13. The last clause of Section 5-108(i)(5) [30-5-128(9)(e)] deals with a special case in which the fraud is not committed by the beneficiary, but is committed by a stranger to the transaction who forges the beneficiary's signature. If the issuer pays against documents on which a required signature of the beneficiary is forged, it remains liable to the true beneficiary. This principal is applicable to both electronic and tangible documents.

30-5-129. Fraud and forgery.

Official Comment

Source: Section 5-109, U.C.C.

Official Comment:

1. This recodification makes clear that fraud must be found either in the documents or must have been committed by the beneficiary on the issuer or applicant. See Cromwell v. Commerce & Energy Bank, 464 So.2d 721 (La. 1985).

Secondly, it makes clear that fraud must be "material." Necessarily courts must decide the breadth and width of "materiality." The use of the word requires that the fraudulent aspect of a document be material to a purchaser of that document or that the fraudulent act be significant to the participants in the underlying transaction. Assume, for example, that the beneficiary has a contract to deliver 1,000 barrels of salad oil. Knowing that it has delivered only 998, the beneficiary nevertheless submits an invoice showing 1,000 barrels. If two barrels in a 1,000 barrel shipment would be an insubstantial and immaterial breach of the underlying contract, the beneficiary's act, though possibly fraudulent, is not materially so and would not justify an injunction. Conversely, the knowing submission of those invoices upon delivery of only five barrels would be materially fraudulent. The courts must examine the underlying transaction when there is an allegation of material fraud, for only by examining that transaction can one determine whether a document is fraudulent or the beneficiary has committed fraud and, if so, whether the fraud was material.

Material fraud by the beneficiary occurs only when the beneficiary has no colorable right to expect honor and where there is no basis in fact to support such a right to honor. The section indorses articulations such as those stated in Intraworld Indus. v. Girard Trust Bank, 336 A.2d 316 (Pa. 1975), Roman Ceramics Corp. v. People's Nat. Bank, 714 F.2d 1207 (3d Cir. 1983), and similar decisions and embraces certain decisions under Section 5-114 [30-5-134] that relied upon the phrase "fraud in the transaction." Some of these decisions have been summarized as follows in Ground Air Transfer v. Westate's Airlines, 899 F.2d 1269, 1272-73 (1st Cir. 1990):

We have said throughout that courts may not "*normally*" issue an injunction because of an important exception to the general "no injunction" rule. The exception, as we also explained in Itek, 730 F.2d at 24-25, concerns "fraud" so serious as to make it obviously pointless and unjust to permit the beneficiary to obtain the money. Where the circumstances "*plainly*" show that the underlying contract forbids the beneficiary to call a letter of credit, Itek, 730 F.2d at 24; where they show that the contract deprives the beneficiary of even a "*colorable*" right to do so, id., at 25; where the contract and circumstances reveal that the beneficiary's demand for payment has "absolutely no basis in fact," id.; see Dynamics Corp. of America, 356 F. Supp. at 999; where the beneficiary's conduct has "so vitiated the entire transaction that the legitimate purposes of the independence of the issuer's obligation would no longer be served," Itek, 730 F.2d at 25 (quoting Roman Ceramics Corp. v. Peoples National Bank, 714 F.2d 1207, 1212 n.12, 1215 (3d Cir. 1983) (quoting Intraworld Indus., 336 A.2d at 324-25)); *then* a court may enjoin payment.

2. Subsection (a)(2) [subsection (1)(b)] makes clear that the issuer may honor in the face of the applicant's claim of fraud. The subsection also makes clear what was not stated in former Section 5-114 [30-5-134], that the issuer may dishonor and defend that dishonor by showing fraud or forgery of the kind stated in subsection (a) [subsection (1)]. Because issuers may be liable for wrongful dishonor if they are unable to prove forgery or material fraud, presumably most issuers will choose to honor despite applicant's claims of fraud or forgery unless the applicant procures an injunction. Merely because the issuer has a right to dishonor and to defend that dishonor by showing forgery or material fraud does not mean it has a duty to the applicant to dishonor. The applicant's normal recourse is to procure an injunction, if the applicant is unable to procure an injunction, it will have a claim against the issuer only in the rare case in which it can show that the issuer did not honor in good faith.

3. Whether a beneficiary can commit fraud by presenting a draft under a clean letter of credit (one calling only for a draft and no other documents) has been much debated. Under the current formulation it would be possible but difficult for there to be fraud in such a presentation. If the applicant were able to show that the beneficiary were committing material fraud on the applicant in the underlying transaction, then payment would facilitate a material fraud by the beneficiary on the applicant and honor could be enjoined. The courts should be skeptical of claims of fraud by one who has signed a "suicide" or clean credit and thus granted a beneficiary the right to draw by mere presentation of a draft.

4. The standard for injunctive relief is high, and the burden remains on the applicant to show, by evidence and not by mere allegation, that such relief is warranted. Some courts have enjoined payments on letters of credit on insufficient showing by the applicant. For example, in

Griffin Cos. v. First Nat. Bank, 374 N.W.2d 768 (Minn.App. 1985), the court enjoined payment under a standby letter of credit, basing its decision on plaintiff's allegation, rather than competent evidence, of fraud.

There are at least two ways to prohibit injunctions against honor under this section after acceptance of a draft by the issuer. First is to define honor (see Section 5-102(a)(8)) in the particular letter of credit to occur upon acceptance and without regard to later payment of the acceptance. Second is explicitly to agree that the applicant has no right to an injunction after acceptance — whether or not the acceptance constitutes honor.

5. Although the statute deals principally with injunctions against honor, it also cautions against granting "similar relief" and the same principles apply when the applicant or issuer attempts to achieve the same legal outcome by injunction against presentation (see Ground Air Transfer Inc. v. Westates Airlines, Inc., 899 F.2d 1269 (1st Cir. 1990)), interpleader, declaratory judgment, or attachment. These attempts should face the same obstacles that face efforts to enjoin the issuer from paying. Expanded use of any of these devices could threaten the independence principle just as much as injunctions against honor. For that reason courts should have the same hostility to them and place the same restrictions on their use as would be applied to injunctions against honor. Courts should not allow the "sacred cow of equity to trample the tender vines of letter of credit law."

6. Section 5-109(a)(1) [30-5-129(1)(a)] also protects specified third parties against the risk of fraud. By issuing a letter of credit that nominates a person to negotiate or pay, the issuer (ultimately the applicant) induces that nominated person to give value and thereby assumes the risk that a draft drawn under the letter of credit will be transferred to one with a status like that of a holder in due course who deserves to be protected against a fraud defense.

7. The "loss" to be protected against — by bond or otherwise under subsection (b)(2) [subsection (2)(b)] — includes incidental damages. Among those are legal fees that might be incurred by the beneficiary or issuer in defending against an injunction action.

30-5-130. Warranties.

Official Comment

Source: Section 5-110, U.C.C.

Official Comment:

1. Since the warranties in subsection (a) [subsection (1)] are not given unless a letter of credit has been honored, no breach of warranty under this subsection can be a defense to dishonor by the issuer. Any defense must be based on Section 5-108 or 5-109 [30-5-128 or 30-5-129] and not on this section. Also, breach of the warranties by the beneficiary in subsection (a) [subsection (1)] cannot excuse the applicant's duty to reimburse.

2. The warranty in Section 5-110(a)(2) [30-5-130(1)(b)]assumes that payment under the letter of credit is final. It does not run to the issuer, only to the applicant. In most cases the applicant will have a direct cause of action for breach of the underlying contract. This warranty has primary application in standby letters of credit or other circumstances where the applicant is not a party to an underlying contract with the beneficiary. It is not a warranty that the statements made on the presentation of the documents presented are truthful nor is it a warranty that the documents strictly comply under Section 5-108(a) [30-5-128(1)]. It is a warranty that the beneficiary has performed all the acts expressly and implicitly necessary under any underlying agreement to entitle the beneficiary to honor. If, for example, an underlying sales contract authorized the beneficiary to draw only upon "due performance" and the beneficiary drew even though it had breached the underlying contract by delivering defective goods, honor of its draw would break the warranty. By the same token, if the underlying contract authorized the beneficiary to draw only upon actual default or upon its or a third party's determination of default by the applicant and if the beneficiary drew in violation of its authorization, then upon honor of its draw the warranty would be breached. In many cases, therefore, the documents presented to the issuer will contain inaccurate statements (concerning the goods delivered or concerning default or other matters), but the breach of warranty arises not because the statements are untrue but because the beneficiary's drawing violated its express or implied obligations in the underlying transaction.

3. The damages for breach of warranty are not specified in Section 5-111 [30-5-131]. Courts may find damage analogies in Section 2-714 [30-2-714] in Article 2 [Title 30, chapter 2] and in warranty decisions under Articles 3 and 4 [Title 30, chapters 3 and 4].

Unlike wrongful dishonor cases — where the damages usually equal the amount of the draw — the damages for breach of warranty will often be much less than the amount of the draw, sometimes zero. Assume a seller entitled to draw only on proper performance of its sales contract. Assume it breaches the sales contract in a way that gives the buyer a right to damages but no right to reject. The applicant's damages for breach of the warranty in subsection (a)(2) [subsection (1)(b)] are limited to the damages it could recover for breach of the contract of sale. Alternatively assume an underlying agreement that authorizes a beneficiary to draw only the "amount in default." Assume a default of $200,000 and a draw of $500,000. The damages for breach of warranty would be no more than $300,000.

30-5-131. Remedies.

Official Comment

Source: Section 5-111, U.C.C.

Official Comment:

1. The right to specific performance is new. The express limitation on the duty of the beneficiary to mitigate damages adopts the position of certain courts and commentators. Because the letter of credit depends upon speed and certainty of payment, it is important that the issuer not be given an incentive to dishonor. The issuer might have an incentive to dishonor if it could rely on the burden of mitigation falling on the beneficiary, (to sell goods and sue only for the difference between the price of the goods sold and the amount due under the letter of credit). Under the scheme contemplated by Section 5-111(a) [30-5-131(1)], the beneficiary would present the documents to the issuer. If the issuer wrongfully dishonored, the beneficiary would have no further duty to the issuer with respect to the goods covered by documents that the issuer dishonored and returned. The issuer thus takes the risk that the beneficiary will let the goods rot or be destroyed. Of course the beneficiary may have a duty of mitigation to the applicant arising from the underlying agreement, but the issuer would not have the right to assert that duty by way of defense or setoff. See Section 5-117(d) [30-5-137(4)]. If the beneficiary sells the goods covered by dishonored documents or if the beneficiary sells a draft after acceptance but before dishonor by the issuer, the net amount so gained should be subtracted from the amount of the beneficiary's damages — at least where the damage claim against the issuer equals or exceeds the damage suffered by the beneficiary. If, on the other hand, the beneficiary suffers damages in an underlying transaction in an amount that exceeds the amount of the wrongfully dishonored demand (e.g., where the letter of credit does not cover 100 percent of the underlying obligation), the damages avoided should not necessarily be deducted from the beneficiary's claim against the issuer. In such a case, the damages would be the lesser of (i) the amount recoverable in the absence of mitigation (that is, the amount that is subject to the dishonor or repudiation plus any incidental damages) and (ii) the damages remaining after deduction for the amount of damages actually avoided.

A beneficiary need not present documents as a condition of suit for anticipatory repudiation, but if a beneficiary could never have obtained documents necessary for a presentation conforming to the letter of credit, the beneficiary cannot recover for anticipatory repudiation of the letter of credit. Doelger v. Battery Park Bank, 201 A.D. 515, 194 N.Y.S. 582 (1922) and Decor by Nikkei Int'l, Inc. v. Federal Republic of Nigeria, 497 F.Supp. 893 (S.D.N.Y. 1980), *aff'd*, 647 F.2d 300 (2d Cir. 1981), *cert. denied*, 454 U.S. 1148 (1982). The last sentence of subsection (c) [subsection (3)] does not expand the liability of a confirmer to persons to whom the confirmer would not otherwise be liable under Section 5-107 [30-5-127].

Almost all letters of credit, including those that call for an acceptance, are "obligations to pay money" as that term is used in Section 5-111(a) [30-5-131(1)].

2. What damages "result" from improper honor is for the courts to decide. Even though an issuer pays a beneficiary in violation of Section 5-108(a) [30-5-128(1)] or of its contract with the applicant, it may have no liability to an applicant. If the underlying contract has been fully performed, the applicant may not have been damaged by the issuer's breach. Such a case would occur when *A* contracts for goods at $100 per ton, but, upon delivery, the market value of conforming goods has decreased to $25 per ton. If the issuer pays over discrepancies, there should be no recovery by *A* for the price differential if the issuer's breach did not alter the applicant's obligation under the underlying contract, i.e., to pay $100 per ton for goods now worth $25 per ton. On the other hand, if the applicant intends to resell the goods and must itself satisfy the strict compliance requirements under a second letter of credit in connection with its sale, the applicant may be damaged by the issuer's payment despite discrepancies because the applicant itself may then be unable to procure honor on the letter of credit where it is the beneficiary, and may be unable to mitigate its damages by enforcing its rights against others in the underlying transaction. Note that an issuer found liable to its applicant may have recourse under Section 5-117 [30-5-137] by subrogation to the applicant's claim against the beneficiary or other persons.

One who inaccurately advises a letter of credit breaches its obligation to the beneficiary, but may cause no damage. If the beneficiary knows the terms of the letter of credit and understands the advice to be inaccurate, the beneficiary will have suffered no damage as a result of the adviser's breach.

3. Since the confirmer has the rights and duties of an issuer, in general it has an issuer's liability, see subsection (c) [subsection (3)]. The confirmer is usually a confirming bank. A confirming bank often also plays the role of an adviser. If it breaks its obligation to the beneficiary, the confirming bank may have liability as an issuer or, depending upon the obligation that was broken, as an adviser. For example, a wrongful dishonor would give it liability as an issuer under Section 5-111(a) [30-5-131(1)]. On the other hand a confirming bank that broke its obligation to advise the credit but did not commit wrongful dishonor would be treated under Section 5-111(c) [30-5-131(3)].

4. Consequential damages for breach of obligations under this article [chapter] are excluded in the belief that these damages can best be avoided by the beneficiary or the applicant and out of the fear that imposing consequential damages on issuers would raise the cost of the letter of credit to a level that might render it uneconomic. *A fortiori* punitive and exemplary damages are excluded, however, this section does not bar recovery of consequential or even punitive damages for breach of statutory or common law duties arising outside of this article [chapter].

5. The section does not specify a rate of interest. It leaves the setting of the rate to the court. It would be appropriate for a court to use the rate that would normally apply in that court in other situations where interest is imposed by law.

6. The court must award attorney's fees to the prevailing party, whether that party is an applicant, a beneficiary, an issuer, a nominated person, or adviser. Since the issuer may be entitled to recover its legal fees and costs from the applicant under the reimbursement agreement, allowing the issuer to recover those fees from a losing beneficiary may also protect the applicant against undeserved losses. The party entitled to attorneys' fees has been described as the "prevailing party." Sometimes it will be unclear which party "prevailed," for example, where there are multiple issues and one party wins on some and the other party wins on others. Determining which is the prevailing party is in the discretion of the court. Subsection (e) [subsection (5)] authorizes attorney's fees in all actions where a remedy is sought "under this article [chapter]." It applies even when the remedy might be an injunction under Section 5-109 [30-5-129] or when the claimed remedy is otherwise outside of Section 5-111 [30-5-131]. Neither an issuer nor a confirmer should be treated as a "losing" party when an injunction is granted to the applicant over the objection of the issuer or confirmer; accordingly neither should be liable for fees and expenses in that case.

"Expenses of litigation" is intended to be broader than "costs." For example, expense of litigation would include travel expenses of witnesses, fees for expert witnesses, and expenses associated with taking depositions.

7. For the purposes of Section 5-111(f) [30-5-131(6)] "harm anticipated" must be anticipated at the time when the agreement that includes the liquidated damage clause is executed or at the time when the undertaking that includes the clause is issued. See Section 2A-504 [30-2A-504].

Case Notes

Construction Contract — Letter of Credit: Haines Pipeline Construction, Inc., contracted to build a pipeline for Montana Power Company (MPC). Performance was secured by an irrevocable letter of credit. The project ran into regulatory problems, and a settlement agreement was signed between the parties. The parties entered a second contract for miscellaneous repair work on the completed portion of the pipeline, including repair of buried pipeline. Haines extended the letter of credit at the request of MPC, and MPC subsequently drew upon the letter of credit. Haines sued to recover damages against MPC for breach of the construction contract. The District Court found that MPC had accepted Haines' work, that MPC had no authority to draw upon the letter of credit, and that presentment of the letter of credit constituted a breach of the construction contract. Haines Pipeline Constr., Inc. v. Mont. Power Co., 251 M 422, 830 P2d 1230, 48 St. Rep. 1102 (1991).

30-5-132. Transfer of letter of credit.

Official Comment

Source: Section 5-112, U.C.C.

Official Comment:

1. In order to protect the applicant's reliance on the designated beneficiary, letter of credit law traditionally has forbidden the beneficiary to convey to third parties its right to draw or

demand payment under the letter of credit. Subsection (a) [subsection (1)] codifies that rule. The term "transfer" refers to the beneficiary's conveyance of that right. Absent incorporation of the UCP (which make elaborate provision for partial transfer of a commercial letter of credit) or similar trade practice and absent other express indication in the letter of credit that the term is used to mean something else, a term in the letter of credit indicating that the beneficiary has the right to transfer should be taken to mean that the beneficiary may convey to a third party its right to draw or demand payment. Even in that case, the issuer or other person controlling the transfer may make the beneficiary's right to transfer subject to conditions, such as timely notification, payment of a fee, delivery of the letter of credit to the issuer or other person controlling the transfer, or execution of appropriate forms to document the transfer. A nominated person who is not a confirmer has no obligation to recognize a transfer.

The power to establish "requirements" does not include the right absolutely to refuse to recognize transfers under a transferable letter of credit. An issuer who wishes to retain the right to deny all transfers should not issue transferable letters of credit or should incorporate the UCP. By stating its requirements in the letter of credit an issuer may impose any requirement without regard to its conformity to practice or reasonableness. Transfer requirements of issuers and nominated persons must be made known to potential transferors and transferees to enable those parties to comply with the requirements. A common method of making such requirements known is to use a form that indicates the information that must be provided and the instructions that must be given to enable the issuer or nominated person to comply with a request to transfer.

2. The issuance of a transferable letter of credit with the concurrence of the applicant is *ipso facto* an agreement by the issuer and applicant to permit a beneficiary to transfer its drawing right and permit a nominated person to recognize and carry out that transfer without further notice to them. In international commerce, transferable letters of credit are often issued under circumstances in which a nominated person or adviser is expected to facilitate the transfer from the original beneficiary to a transferee and to deal with that transferee. In those circumstances it is the responsibility of the nominated person or adviser to establish procedures satisfactory to protect itself against double presentation or dispute about the right to draw under the letter of credit. Commonly such a person will control the transfer by requiring that the original letter of credit be given to it or by causing a paper copy marked as an original to be issued where the original letter of credit was electronic. By keeping possession of the original letter of credit the nominated person or adviser can minimize or entirely exclude the possibility that the original beneficiary could properly procure payment from another bank. If the letter of credit requires presentation of the original letter of credit itself, no other payment could be procured. In addition to imposing whatever requirements it considers appropriate to protect itself against double payment the person that is facilitating the transfer has a right to charge an appropriate fee for its activity.

"Transfer" of a letter of credit should be distinguished from "assignment of proceeds." The former is analogous to a novation or a substitution of beneficiaries. It contemplates not merely payment to but also performance by the transferee. For example, under the typical terms of transfer for a commercial letter of credit, a transferee could comply with a letter of credit transferred to it by signing and presenting its own draft and invoice. An assignee of proceeds, on the other hand, is wholly dependent on the presentation of a draft and invoice signed by the beneficiary.

By agreeing to the issuance of a transferable letter of credit, which is not qualified or limited, the applicant may lose control over the identity of the person whose performance will earn payment under the letter of credit.

30-5-133. Transfer by operation of law.

Official Comment

[*Corresponding U.C.C. Section:* Section 5-113, U.C.C.]

Source: Section 5-113, U.C.C.

Official Comment:

This section affirms the result in Pastor v. Nat. Republic Bank of Chicago, 76 Ill.2d 139, 390 N.E.2d 894 (Ill. 1979) and Federal Deposit Insurance Co. v. Bank of Boulder, 911 F.2d 1466 (10th Cir. 1990). Both electronic and tangible documents may be signed.

An issuer's requirements for recognition of a successor's status might include presentation of a certificate of merger, a court order appointing a bankruptcy trustee or receiver, a certificate of appointment as bankruptcy trustee, or the like. The issuer is entitled to rely upon such documents which on their face demonstrate that presentation is made by a successor of a beneficiary. It is not obliged to make an independent investigation to determine the fact of succession.

30-5-134. Assignment of proceeds.

Official Comment

Source: Section 5-114, U.C.C.

Official Comment:

1. Subsection (b) [subsection (2)] expressly validates the beneficiary's present assignment of letter of credit proceeds if made after the credit is established but before the proceeds are realized. This section adopts the prevailing usage — "assignment of proceeds" — to an assignee. That terminology carries with it no implication, however, that an assignee acquires no interest until the proceeds are paid by the issuer. For example, an "assignment of the right to proceeds" of a letter of credit for purposes of security that meets the requirements of Section 9-203(1) [30-9-203(1), now repealed, see 30-9A-203] would constitute the present creation of a security interest in that right. This security interest can be perfected by possession (Section 9-305 [30-9-305, now repealed, see 30-9A-313]) if the letter of credit is in written form. Although subsection (a) [subsection (1)] explains the meaning of "'proceeds' of a letter of credit," it should be emphasized that those proceeds also may be Article 9 [Title 30, chapter 9A] proceeds of other collateral. For example, if a seller of inventory receives a letter of credit to support the account that arises upon the sale, payments made under the letter of credit are Article 9 [Title 30, chapter 9A] proceeds of the inventory, account, and any document of title covering the inventory. Thus, the secured party who had a perfected security interest in that inventory, account, or document has a perfected security interest in the proceeds collected under the letter of credit, so long as they are identifiable cash proceeds (Section 9-306(2), (3) [30-9-306(2) and (3), now repealed, see 30-9A-315]. This perfection is continuous, regardless of whether the secured party perfected a security interest in the right to letter of credit proceeds.

2. An assignee's rights to enforce an assignment of proceeds against an issuer and the priority of the assignee's rights against a nominated person or transferee beneficiary are governed by Article 5 [Title 30, chapter 5]. Those rights and that priority are stated in subsections (c), (d), and (e) [subsections (3), (4), and (5)]. Note also that Section 4-210 [30-4-210] gives first priority to a collecting bank that has given value for a documentary draft.

3. By requiring that an issuer or nominated person consent to the assignment of proceeds of a letter of credit, subsections (c) and (d) [subsections (3) and (4)] follow more closely recognized national and international letter of credit practices than did prior law. In most circumstances, it has always been advisable for the assignee to obtain the consent of the issuer in order better to safeguard its right to the proceeds. When notice of an assignment has been received, issuers normally have required signatures on a consent form. This practice is reflected in the revision. By unconditionally consenting to such an assignment, the issuer or nominated person becomes bound, subject to the rights of the superior parties specified in subsection (e) [subsection (5)], to pay to the assignee the assigned letter of credit proceeds that the issuer or nominated person would otherwise pay to the beneficiary or another assignee.

Where the letter of credit must be presented as a condition to honor and the assignee holds and exhibits the letter of credit to the issuer or nominated person, the risk to the issuer or nominated person of having to pay twice is minimized. In such a situation, subsection (d) [subsection (4)] provides that the issuer or nominated person may not unreasonably withhold its consent to the assignment.

Case Notes

Letter of Credit — Guaranty Distinguished: Plaintiff agreed to lend Prospect Associates, Inc. (Prospect) money to finance construction of a subdivision. As part of the security for the loan, Prospect was required to obtain a letter of credit with plaintiff as beneficiary. Prospect defaulted on the promissory note evidencing the loan. Defendant refused payment on the letter of credit, contending it was a guaranty on which it was not primarily liable. The District Court granted summary judgment to plaintiff, and defendant appealed. The Supreme Court affirmed the decision, saying the document was clearly entitled a letter of credit and its intent was to hold the bank primarily liable upon nonperformance of one of the named instruments, as opposed to secondarily liable as under a guaranty. Sherwood & Roberts, Inc. v. First Security Bank, 209 M 402, 682 P2d 149, 41 St. Rep. 787 (1984).

30-5-135. Statute of limitations.

Official Comment

Source: Section 5-115, U.C.C.

Official Comment:

1. This section is based upon Sections 4-111 and 2-725(2) [30-4-112 and 30-2-725(2)].

2. This section applies to all claims for which there are remedies under Section 5-111 [30-5-131] and to other claims made under this article [chapter], such as claims for breach of warranty under Section 5-110 [30-5-130]. Because it covers all claims under Section 5-111 [30-5-131], the statute of limitations applies not only to wrongful dishonor claims against the issuer but also to claims between the issuer and the applicant arising from the reimbursement agreement. These might be for reimbursement (issuer v. applicant) or for breach of the reimbursement contract by wrongful honor (applicant v. issuer).

3. The statute of limitations, like the rest of the statute, applies only to a letter of credit issued on or after the effective date and only to transactions, events, obligations, or duties arising out of or associated with such a letter. If a letter of credit was issued before the effective date and an obligation on that letter of credit was breached after the effective date, the complaining party could bring its suit within the time that would have been permitted prior to the adoption of Section 5-115 [30-5-135] and would not be limited by the terms of Section 5-115 [30-5-135].

30-5-136. Choice of law and forum.

Official Comment

Source: Section 5-116, U.C.C.

Official Comment:

1. Although it would be possible for the parties to agree otherwise, the law normally chosen by agreement under subsection (a) [subsection (1)] and that provided in the absence of agreement under subsection (b) [subsection (2)] is the substantive law of a particular jurisdiction not including the choice of law principles of that jurisdiction. Thus, two parties, an issuer and an applicant, both located in Oklahoma might choose the law of New York. Unless they agree otherwise, the section anticipates that they wish the substantive law of New York to apply to their transaction and they do not intend that a New York choice of law principle might direct a court to Oklahoma law. By the same token, the liability of an issuer located in New York is governed by New York substantive law — in the absence of agreement — even in circumstances in which choice of law principles found in the common law of New York might direct one to the law of another State. Subsection (b) [subsection (2)] states the relevant choice of law principles and it should not be subordinated to some other choice of law rule. Within the States of the United States *renvoi* will not be a problem once every jurisdiction has enacted Section 5-116 [30-5-136] because every jurisdiction will then have the same choice of law rule and in a particular case all choice of law rules will point to the same substantive law.

Subsection (b) [subsection (2)] does not state a choice of law rule for the "liability of an applicant." However, subsection (b) [subsection (2)] does state a choice of law rule for the liability of an issuer, nominated person, or adviser, and since some of the issues in suits by applicants against those persons involve the "liability of an issuer, nominated person, or adviser," subsection (b) [subsection (2)] states the choice of law rule for those issues. Because an issuer may have liability to a confirmer both as an issuer (Section 5-108(a) [30-5-128(1)], Comment 5 to Section 5-108 [30-5-128]) and as an applicant (Section 5-107(a) [30-5-127], Comment 1 to Section 5-107 [30-5-127], Section 5-108(i) [30-5-128(9)]), subsection (b) [subsection (2)] may state the choice of law rule for some but not all of the issuer's liability in a suit by a confirmer.

2. Because the confirmer or other nominated person may choose different law from that chosen by the issuer or may be located in a different jurisdiction and fail to choose law, it is possible that a confirmer or nominated person may be obligated to pay (under their law) but will not be entitled to payment from the issuer (under its law). Similarly, the rights of an unreimbursed issuer, confirmer, or nominated person against a beneficiary under Section 5-109, 5-110, or 5-117 [30-5-129, 30-5-130, or 30-5-137], will not necessarily be governed by the same law that applies to the issuer's or confirmer's obligation upon presentation. Because the UCP and other practice are incorporated in most international letters of credit, disputes arising from different legal obligations to honor have not been frequent. Since Section 5-108 [30-5-128] incorporates standard practice, these problems should be further minimized — at least to the extent that the same practice is and continues to be widely followed.

3. This section does not permit what is now authorized by the nonuniform Section 5-102(4) in New York. Under the current law in New York a letter of credit that incorporates the UCP

is not governed in any respect by Article 5 [Title 30, chapter 5]. Under revised Section 5-116 [30-5-136] letters of credit that incorporate the UCP or similar practice will still be subject to Article 5 [Title 30, chapter 5] in certain respects. First, incorporation of the UCP or other practice does not override the nonvariable terms of Article 5 [Title 30, chapter 5]. Second, where there is no conflict between Article 5 [Title 30, chapter 5] and the relevant provision of the UCP or other practice, both apply. Third, practice provisions incorporated in a letter of credit will not be effective if they fail to comply with Section 5-103(c) [30-5-123(3)]. Assume, for example, that a practice provision purported to free a party from any liability unless it were "grossly negligent" or that the practice generally limited the remedies that one party might have against another. Depending upon the circumstances, that disclaimer or limitation of liability might be ineffective because of Section 5-103(c) [30-5-123(3)].

Even though Article 5 [Title 30, chapter 5] is generally consistent with UCP 500, it is not necessarily consistent with other rules or with versions of the UCP that may be adopted after Article 5's [Title 30, chapter 5's] revision, or with other practices that may develop. Rules of practice incorporated in the letter of credit or other undertaking are those in effect when the letter of credit or other undertaking is issued. Except in the unusual cases discussed in the immediately preceding paragraph, practice adopted in a letter of credit will override the rules of Article 5 [Title 30, chapter 5] and the parties to letter of credit transactions must be familiar with practice (such as future versions of the UCP) that is explicitly adopted in letters of credit.

4. In several ways Article 5 [Title 30, chapter 5] conflicts with and overrides similar matters governed by Articles 3 and 4 [Title 30, chapters 3 and 4]. For example, "draft" is more broadly defined in letter of credit practice than under Section 3-104 [30-3-104]. The time allowed for honor and the required notification of reasons for dishonor are different in letter of credit practice than in the handling of documentary and other drafts under Articles 3 and 4 [Title 30, chapters 3 and 4].

5. Subsection (e) [subsection (5)] must be read in conjunction with existing law governing subject matter jurisdiction. If the local law restricts a court to certain subject matter jurisdiction not including letter of credit disputes, subsection (e) [subsection (5)] does not authorize parties to choose that forum. For example, the parties' agreement under Section 5-116(e) [30-5-136(5)] would not confer jurisdiction on a probate court to decide a letter of credit case.

If the parties choose a forum under subsection (e) [subsection (5)] and if — because of other law — that forum will not take jurisdiction, the parties' agreement or undertaking should then be construed (for the purpose of forum selection) as though it did not contain a clause choosing a particular forum. That result is necessary to avoid sentencing the parties to eternal purgatory where neither the chosen State nor the State which would have jurisdiction but for the clause will take jurisdiction — the former in disregard of the clause and the latter in honor of the clause.

30-5-137. Subrogation of issuer, applicant, and nominated person.

Official Comment

Source: Section 5-117, U.C.C.

Official Comment:

1. By itself this section does not grant any right of subrogation. It grants only the right that would exist if the person seeking subrogation "were a secondary obligor." (The term "secondary obligor" refers to a surety, guarantor, or other person against whom or whose property an obligee has recourse with respect to the obligation of a third party. See Restatement of the Law Third, Suretyship § 1 (1995).) If the secondary obligor would not have a right to subrogation in the circumstances in which one is claimed under this section, none is granted by this section. In effect, the section does no more than to remove an impediment that some courts have found to subrogation because they conclude that the issuer's or other claimant's rights are "independent" of the underlying obligation. If, for example, a secondary obligor would not have a subrogation right because its payment did not fully satisfy the underlying obligation, none would be available under this section. The section indorses the position of Judge Becker in Tudor Development Group, Inc. v. United States Fidelity and Guaranty, 968 F.2d 357 (3rd Cir. 1991).

2. To preserve the independence of the letter of credit obligation and to insure that subrogation not be used as an offensive weapon by an issuer or others, the admonition in subsection (d) [subsection (4)] must be carefully observed. Only one who has completed its performance in a letter of credit transaction can have a right to subrogation. For example, an issuer may not dishonor and then defend its dishonor or assert a setoff on the ground that it is subrogated to another person's rights. Nor may the issuer complain after honor that its subrogation rights have been impaired by any good faith dealings between the beneficiary and the applicant or

any other person. Assume, for example, that the beneficiary under a standby letter of credit is a mortgagee. If the mortgagee were obliged to issue a release of the mortgage upon payment of the underlying debt (by the issuer under the letter of credit), that release might impair the issuer's rights of subrogation, but the beneficiary would have no liability to the issuer for having granted that release.

CHAPTER 7
UNIFORM COMMERCIAL CODE — WAREHOUSE RECEIPTS, BILLS OF LADING, AND OTHER DOCUMENTS OF TITLE

Chapter Official Comments

[*Corresponding U.C.C. Section:* Article 7, U.C.C.]

Prefatory Note: Article 7 [Title 30, chapter 7] is the last of the articles of the Uniform Commercial Code [Title 30, chapters 1 through 9A] to be revised during the preceding decade. The genesis of this project is twofold: to provide a framework for the further development of electronic documents of title and to update the article for modern times in light of state, federal and international developments. Each section has been reviewed to determine its suitability given modern practice, the need for medium and gender neutrality, and modern statutory drafting.

To provide for electronic documents of title, several definitions in Article 1 [Title 30, chapter 1] were revised including "bearer," "bill of lading," "delivery," "document of title," "holder," and "warehouse receipt." The concept of an electronic document of title allows for commercial practice to determine what records issued by bailees are "in the regular course of business or financing" and are "treated as adequately evidencing that the person in possession or control of the record is entitled to receive, control, hold, and dispose of the record and the goods the record covers." Rev. Section 1-201(b)(16) [30-1-201(2)(q)]. Such records in electronic form are electronic documents of title and in tangible form are tangible documents of title. Conforming amendments to other Articles of the UCC [Title 30, chapters 1 through 5, 8, and 9A] are also necessary to fully integrate electronic documents of title into the UCC [Title 30, chapters 1 through 9A]. Conforming amendments to other Articles of the UCC [Title 30, chapters 1 through 5, 8, and 9A] are contained in Appendix I.

Key to the integration of the electronic document of title scheme is the concept of "control" defined in Section 7-106 [30-7-107]. This definition is adapted from the Uniform Electronic Transactions Act § 16 on Transferrable Records and from Uniform Commercial Code Section 9-105 [30-9A-105] concerning control of electronic chattel paper. Control of an electronic document of title is the conceptual equivalent to possession and indorsement of a tangible document of title. Of equal importance is the acknowledgment that parties may desire to substitute an electronic document of title for an already-issued paper document and vice versa. Section 7-105 [30-7-106] sets forth the minimum requirements that need to be fulfilled in order to give effect to the substitute document issued in the alternate medium. To the extent possible, the rules for electronic documents of title are the same or as similar as possible to the rules for tangible documents of title. If a rule is meant to be limited to one medium or the other, that is clearly stated. Rules that reference documents of title, warehouse receipts, or bills of lading without a designation to "electronic" or "tangible" apply to documents of title in either medium. As with tangible negotiable documents of title, electronic negotiable documents of title may be negotiated and duly negotiated. Section 7-501 [30-7-501].

Other changes that have been made are:

1. New definitions of "carrier," "good faith," "record", "sign" and "shipper" in Section 7-102 [30-7-102].
2. Deletion of references to tariffs or filed classifications given the deregulation of the affected industries. See e.g. section 7-103 [30-7-103] and 7-309 [30-7-309],
3. Clarifying the rules regarding when a document is nonnegotiable. Section 7-104 [30-7-104].
4. Making clear when rules apply just to warehouse receipts or bills of lading, thus eliminating the need for former section 7-105 [30-7-105, now repealed].
5. Clarifying that particular terms need not be included in order to have a valid warehouse receipt. Section 7-202 [30-7-202].
6. Broadening the ability of the warehouse to make an effective limitation of liability in its warehouse receipt or storage agreement in accord with commercial practice. Section 7-204 [30-7-204].

7. Allowing a warehouse to have a lien on goods covered by a storage agreement and clarifying the priority rules regarding the claim of a warehouse lien as against other interests. Section 7-209 [30-7-209].

8. Conforming language usage to modern shipping practice. Sections 7-301 [30-7-301] and 7-302 [30-7-302].

9. Clarifying the extent of the carrier's lien. Section 7-307 [30-7-307].

10. Adding references to Article 2A [Title 30, chapter 2A] when appropriate. See e.g. Sections 7-503, 7-504, 7-509 [30-7-503, 30-7-504, 30-7-509].

11. Clarifying that the warranty made by negotiation or delivery of a document of title should apply only in the case of a voluntary transfer of possession or control of the document. Section 7-507 [30-7-507].

12. Providing greater flexibility to a court regarding adequate protection against loss when ordering delivery of the goods or issuance of a substitute document. Section 7-601 [30-7-601].

13. Providing conforming amendments to the other Articles of the Uniform Commercial Code [Title 30, chapters 1 through 5, 8, and 9A] to accommodate electronic documents of title.

Chapter Compiler's Comments

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Part 1
General

30-7-101. Short title.

Official Comment

[*Corresponding U.C.C. Section:* Section 7-101, U.C.C.]

Prior Uniform Statutory Provision: Former Section 7-101.

Changes: Revised for style only.

This Article [Title 30, chapter 7] is a revision of the 1962 Official Text with Comments as amended since 1962. The 1962 Official Text was a consolidation and revision of the Uniform Warehouse Receipts Act and the Uniform Bills of Lading Act, and embraced the provisions of the Uniform Sales Act relating to negotiation of documents of title.

This Article [Title 30, chapter 7] does not contain the substantive criminal provisions found in the Uniform Warehouse Receipts and Bills of Lading Acts. These criminal provisions are inappropriate to a Commercial Code, and for the most part duplicate portions of the ordinary criminal law relating to frauds. This revision deletes the former Section 7-105 [30-7-105, now repealed] that provided that courts could apply a rule from Parts 2 and 3 [Title 30, chapter 7, parts 2 and 3] by analogy to a situation not explicitly covered in the provisions on warehouse receipts or bills of lading when it was appropriate. This is, of course, an unexceptional proposition and need not be stated explicitly in the statute. Thus former Section 7-105 [30-7-105, now repealed] has been deleted. Whether applying a rule by analogy to a situation is appropriate depends upon the facts of each case.

The Article [Title 30, chapter 7] does not attempt to define the tort liability of bailees, except to hold certain classes of bailees to a minimum standard of reasonable care. For important classes of bailees, liabilities in case of loss, damages or destruction, as well as other legal questions associated with particular documents of title, are governed by federal statutes, international treaties, and in some cases regulatory state laws, which supersede the provisions of this Article [Title 30, chapter 7] in case of inconsistency. See Section 7-103 [30-7-103].

30-7-102. Definitions and index of definitions.

Official Comment

[*Corresponding U.C.C. Section:* Section 7-102, U.C.C.]

Prior Uniform Statutory Provision: Former Section 7-102.

Changes: New definitions of "carrier," "good faith," "record," "sign," and "shipper." Other definitions revised to accommodate electronic mediums.

Purposes:

1. "Bailee" is used in this Article [Title 30, chapter 7] as a blanket term to designate carriers, warehousemen and others who normally issue documents of title on the basis of goods which they have received. The definition does not, however, require actual possession of the goods. If a bailee acknowledges possession when it does not have possession, the bailee is bound by sections of this Article [Title 30, chapter 7] which declare the "bailee's" obligations. (See definition of "Issuer" in

this section and Sections 7-203 [30-7-203] and 7-301 [30-7-301] on liability in case of non-receipt.) A "carrier" is one type of bailee and is defined as a person that issues a bill of lading. A "shipper" is a person who enters into the contract of transportation with the carrier. The definitions of "bailee," "consignee," "consignor," "goods", and "issuer", are unchanged in substance from prior law. "Document of title" is defined in Article 1 [Title 30, chapter 1].

2. The definition of warehouse receipt contained in the general definitions section of this Act (Section 1-201) [30-1-201] does not require that the issuing warehouse be "lawfully engaged" in business or for profit. The warehouse's compliance with applicable state regulations such as the filing of a bond has no bearing on the substantive issues dealt with in this Article [Title 30, chapter 7]. Certainly the issuer's violations of law should not diminish its responsibility on documents the issuer has put in commercial circulation. But it is still essential that the business be storing goods "for hire" (Section 1-201 [30-1-201] and this section). A person does not become a warehouse by storing its own goods.

3. When a delivery order has been accepted by the bailee it is for practical purposes indistinguishable from a warehouse receipt. Prior to such acceptance there is no basis for imposing obligations on the bailee other than the ordinary obligation of contract which the bailee may have assumed to the depositor of the goods. Delivery orders may be either electronic or tangible documents of title. See definition of "document of title" in Section 1-201 [30-1-201].

4. The obligation of good faith imposed by this Article [Title 30, chapter 7] and by Article 1, Section 1-304 [30-1-203] includes the observance of reasonable commercial standards of fair dealing.

5. The definitions of "record" and "sign" are included to facilitate electronic mediums. See comment 9 to Section 9-102 [30-9A-102] discussing "record" and the comment to amended Section 2-103 [30-2-103] discussing "sign."

6. "Person entitled under the document" is moved from former Section 7-403 [30-7-403, 2003 MCA].

7. These definitions apply in this Article [Title 30, chapter 7] unless the context otherwise requires. The "context" is intended to refer to the context in which the defined term is used in the Uniform Commercial Code [Title 30, chapters 1 through 9A]. The definition applies whenever the defined term is used unless the context in which the defined term is used in the statute indicates that the term was not used in its defined sense. See comment to Section 1-201 [30-1-201].

Compiler's Comments

2005 Amendment: Chapter 575 in (1) inserted definitions of carrier, good faith, person entitled under a document, record, shipper, and sign and deleted definition of document that read: ""Document" means document of title as defined in 30-1-201(15)"; in definition of consignee after "bill" inserted "of lading"; in definition of consignor after "bill" inserted "of lading"; in definition of delivery order near beginning substituted "record that contains an order" for "written order" and near middle substituted "warehouse" for "warehouseman"; in definition of issuer after "document" inserted "of title"; substituted warehouse for warehouseman as defined term; deleted former (2) that read: "(2) Other definitions applying to this chapter or to specified parts thereof, and the sections in which they appear are:

"Duly negotiate". 30-7-501.

"Person entitled under the document". 30-7-403(4)"; in (2) deleted from former list ""Overseas". 30-2-323"; inserted (2)(b) relating to lessee in ordinary course; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

Case Notes

DECISIONS UNDER UNIFORM WAREHOUSE RECEIPTS ACT

Warehouseman: One conducting a warehouse for the storage of beans, exacting a storage and handling charge from those using the warehouse facilities, and issuing negotiable warehouse receipts was a "public warehouseman" within the general meaning of the term. Fidelity & Deposit Co. of Maryland v. St., 92 F2d 693 (1937).

30-7-103. Relation of chapter to treaty or statute.

Official Comment

[*Corresponding U.C.C. Section:* Section 7-103, U.C.C.]

Prior Uniform Statutory Provision: Former Sections 7-103 and 10-104.

Changes: Deletion of references to tariffs and classifications; incorporation of former Section 10-104 [not adopted in Montana] into subsection (b) [subsection (2)].

Purposes:

1. To make clear what would of course be true without the Section, that applicable Federal law is paramount.

2. To make clear also that regulatory state statutes (such as those fixing or authorizing a commission to fix rates and prescribe services, authorizing different charges for goods of different values, and limiting liability for loss to the declared value on which the charge was based) are not affected by the Article [Title 30, chapter 7] and are controlling on the matters which they cover unless preempted by federal law. The reference in former Section 7-103 [30-7-103, 2003 MCA] to tariffs, classifications, and regulations filed or issued pursuant to regulatory state statutes has been deleted as inappropriate in the modern era of diminished regulation of carriers and warehouses. If a regulatory scheme requires a carrier or warehouse to issue a tariff or classification, that tariff or classification would be given effect via the state regulatory scheme that this Article [Title 30, chapter 7] recognizes as controlling. Permissive tariffs or classifications would not displace the provisions of this act, pursuant to this section, but may be given effect through the ability of parties to incorporate those terms by reference into their agreement.

3. The document of title provisions of this act supplement the federal law and regulatory state law governing bailees. This Article [Title 30, chapter 7] focuses on the commercial importance and usage of documents of title. State ex. rel Public Service Commission v. Gunkelman & Sons, Inc., 219 N.W.2d 853 (N.D. 1974).

4. Subsection (c) [subsection (3)] is included to make clear the interrelationship between the federal Electronic Signatures in Global and National Commerce Act and this article [Title 30, chapter 7]. Section 102 of the federal act allows a State statute to modify, limit, or supersede the provisions of Section 101 of the federal act. See the comments to Revised Article 1, Section 1-108 [not adopted].

5. Subsection (d) [subsection (4)] makes clear that once this article [Title 30, chapter 7] is in effect, its provisions regarding electronic commerce and regarding electronic documents of title control in the event there is a conflict with the provisions of the Uniform Electronic Transactions Act.

Compiler's Comments

2005 Amendment: Chapter 575 in catchline at end deleted "tariff, classification or regulation"; inserted (1) relating to federal law and treaties; inserted (2) relating to a bailee's business; inserted (3) relating to federal electronic signatures law; in (4) near beginning after "extent" deleted "that any treaty or statute of the United States, regulatory statute of this state or tariff, classification or regulation filed or issued pursuant thereto is applicable" and inserted "there is a conflict between the Uniform Electronic Transactions Act, Title 30, chapter 18, part 1, and this chapter" and at end substituted "this chapter governs" for "the provisions of this chapter are subject thereto"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-7-104. Negotiable and nonnegotiable document of title.

Official Comment

[*Corresponding U.C.C. Section:* Section 7-104, U.C.C.]

Prior Uniform Statutory Provision: Former Section 7-104.

Changes: Subsection (a) [subsection (1)] is revised to reflect modern style and trade practice. Subsection (b) [subsection (2)] is revised for style and medium neutrality. Subsection (c) [subsection (3)] is new.

Purposes:

1. This Article [Title 30, chapter 7] deals with a class of commercial paper representing commodities in storage or transportation. This "commodity paper" is to be distinguished from what might be called "money paper" dealt with in the Article of this Act on Commercial Paper (Article 3) [Title 30, chapter 3] and "investment paper" dealt with in the Article of this Act on Investment Securities (Article 8) [Title 30, chapter 8]. The class of "commodity paper" is designated "document of title" following the terminology of the Uniform Sales Act Section 76. Section 1-201 [30-1-201]. The distinctions between negotiable and nonnegotiable documents in this section makes the most important subclassification employed in the Article [Title 30, chapter 7], in that the holder of negotiable documents may acquire more rights than its transferor had (See Section 7-502) [30-7-502]. The former Section 7-104 [30-7-104, 2003 MCA], which provided that a document of title was negotiable if it runs to a named person or assigns if such designation was recognized in overseas trade, has been deleted as not necessary in light of current commercial practice.

A document of title is negotiable only if it satisfies this section. "Deliverable on proper indorsement and surrender of this receipt" will not render a document negotiable. Bailees often include such provisions as a means of insuring return of nonnegotiable receipts for record purposes. Such language may be regarded as insistence by the bailee upon a particular kind of receipt in connection with delivery of the goods. Subsection (a) [subsection (1)] makes it clear that a document is not negotiable which provides for delivery to order or bearer only if written instructions to that effect are given by a named person. Either tangible or electronic documents of title may be negotiable if the document meets the requirement of this section.

2. Prior to issuance, an issuer may stamp or otherwise provide by a notation on the document of title that it is nonnegotiable even if the document would otherwise comply with the requirement of subsection (a) [subsection (1)]. Subsection (c) [subsection (3)]. Subsection (c) [subsection (3)] is derived from Section 3-104(d) [30-3-104(4)]. Once issued as a negotiable document of title, the document cannot be changed from a negotiable document to a nonnegotiable document. However, one can fail to negotiate a negotiable document of title by due negotiation. See Section 7-501(5) [30-7-501(1)(e)]. A document of title that is nonnegotiable cannot be made negotiable by stamping or providing a notation that the document is negotiable. The only way to make a document of title negotiable is to comply with subsection (a) [subsection (1)].

Compiler's Comments

2005 Amendment: Chapter 575 in catchline after "nonnegotiable" deleted "warehouse receipt, bill of lading or other"; in (1) in introductory clause after "A" deleted "warehouse receipt, bill of lading or other"; deleted former (1)(b) that read: "(b) where recognized in overseas trade, it runs to a named person or assigns"; in (2) at beginning substituted "A document of title other than one described in subsection (1)" for "Any other document"; inserted (3) concerning nonnegotiable documents of title; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-7-106. Reissuance in alternative medium.

Official Comments

[*Corresponding U.C.C. Section:* Section 7-105, U.C.C.]

Prior Uniform Statutory Provisions: None.

Other relevant law: UNCITRAL Draft Instrument on Transport Law.

Purpose:

1. This section allows for documents of title issued in one medium to be reissued in another medium. This section applies to both negotiable and nonnegotiable documents. This section sets forth minimum requirements for giving the reissued document effect and validity. The issuer is not required to issue a document in an alternative medium and if the issuer chooses to do so, it may impose additional requirements. Because a document of title imposes obligations on the issuer of the document, it is imperative for the issuer to be the one who issues the substitute document in order for the substitute document to be effective and valid.

2. The request must be made to the issuer by the person entitled to enforce the document of title (Section 7-102(a)(9)) [30-7-102(1)(i)] and that person must surrender possession or control of the original document to the issuer. The reissued document must have a notation that it has been issued as a substitute for the original document. These minimum requirements must be met in order to give the substitute document effect and validity. If these minimum requirements are not met for issuance of a substitute document of title, the original document of title continues to be effective and valid. However, if the minimum requirements imposed by this section are met, in addition to any other requirements that the issuer may impose, the substitute document will be the document that is effective and valid.

3. To protect parties who subsequently take the substitute document of title, the person who procured issuance of the substitute document warrants that it was a person entitled under the original document at the time it surrendered possession or control of the original document to the issuer. This warranty is modeled after the warranty found in Section 4-209 [30-4-216].

Compiler's Comments

Effective Date: This section is effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-7-107. Control of electronic document of title.

Official Comments

[*Corresponding U.C.C. Section:* Section 7-106, U.C.C.]

Prior Uniform Statutory Provision: Uniform Electronic Transactions Act Section 16.

Purpose:

1. The section defines "control" for electronic documents of title and derives its rules from the Uniform Electronic Transactions Act § 16 on transferrable records. Unlike UETA § 16, however, a document of title may be reissued in an alternative medium pursuant to Section 7-105 [30-7-106]. At any point in time in which a document of title is in electronic form, the control concept of this section is relevant. As under UETA § 16, the control concept embodied in this section provides the legal framework for developing systems for electronic documents of title.

2. Control of an electronic document of title substitutes for the concept of indorsement and possession in the tangible document of title context. See Section 7-501 [30-7-501]. A person with a tangible document of title delivers the document by voluntarily transferring possession and a person with an electronic document of title delivers the document by voluntarily transferring control. (Delivery is defined in Section 1-201 [30-1-201]).

3. Subsection (a) [subsection (1)] sets forth the general rule that the "system employed for evidencing the transfer of interests in the electronic document reliably establishes that person as the person to which the electronic document was issued or transferred." The key to having a system that satisfies this test is that identity of *the* person to which the document was issued or transferred must be reliably established. Of great importance to the functioning of the control concept is to be able to demonstrate, at any point in time, *the one person* entitled under the electronic document. For example, a carrier may issue an electronic bill of lading by having the required information in a database that is encrypted and accessible by virtue of a password. If the computer system in which the required information is maintained identifies the person as *the* person to which the electronic bill of lading was issued or transferred, that person has control of the electronic document of title. That identification may be by virtue of passwords or other encryption methods. Registry systems may satisfy this test. This Article [Title 30, chapter 7] leaves to the market place the development of sufficient technologies and business practices that will meet the test.

An electronic document of title is evidenced by a record consisting of information stored in an electronic medium. Section 1-201 [30-1-201]. For example, a record in a computer database could be an electronic document of title assuming that it otherwise meets the definition of document of title. To the extent that third parties wish to deal in paper mediums, Section 7-105 [30-7-106] provides a mechanism for exiting the electronic environment by having the issuer reissue the document of title in a tangible medium. Thus if a person entitled to enforce an electronic document of title causes the information in the record to be printed onto paper without the issuer's involvement in issuing the document of title pursuant to Section 7-105 [30-7-106], that paper is not a document of title.

4. Subsection (a) [subsection (1)] sets forth the general test for control. Subsection (b) [subsection (2)] sets forth a safe harbor test that if satisfied, results in control under the general test in subsection (a) [subsection (1)]. The test in subsection (b) [subsection (2)] is also used in Section 9-105 [30-9A-105] although Section 9-105 [30-9A-105] does not include the general test of subsection (a) [subsection (1)]. Under subsection (b) [subsection (2)], at any point in time, a party should be able to identify the single authoritative copy which is unique and identifiable as the authoritative copy. This does not mean that once created that the authoritative copy need be static and never moved or copied from its original location. To the extent that backup systems exist which result in multiple copies, the key to this idea is that at any point in time, the one authoritative copy needs to be unique and identifiable.

Parties may not by contract provide that control exists. The test for control is a factual test that depends upon whether the general test in subsection (a) [subsection (1)] or the safe harbor in subsection (b) [subsection (2)] is satisfied.

5. Article 7 [Title 30, chapter 7] has historically provided for rights under documents of title and rights of transferees of documents of title as those rights relate to the goods covered by the document. Third parties may possess or have control of documents of title. While misfeasance or negligence in failure to transfer or misdelivery of the *document* by those third parties may create serious issues, this Article [Title 30, chapter 7] has never dealt with those issues as it relates to tangible documents of title, preferring to leave those issues to the law of contracts, agency and tort law. In the electronic document of title regime, third party registry systems are just beginning to develop. It is very difficult to write rules regulating those third parties without some definitive sense of how the third party registry systems will be structured. Systems that are evolving to date tend to be "closed" systems in which all participants must sign on to the master agreement which provides for rights as against the registry system as well as rights among the members. In those closed systems, the document of title never leaves the system so the parties rely upon the master agreement as to rights against the registry in its failures in dealing with the document. This article [Title 30, chapter 7] contemplates that those "closed" systems will continue to evolve and that the control mechanism in this statute provides a method for the participants in the closed system to achieve the benefits of obtaining control allowed by this article [Title 30, chapter 7].

This article [Title 30, chapter 7] also contemplates that parties will evolve open systems where parties need not be subject to a master agreement. In an open system a party that is expecting to obtain rights through an electronic document may not be a party to the master agreement. To the extent that open systems evolve by use of the control concept contained in this section, the law of contracts, agency, and torts as it applies to the registry's misfeasance or negligence concerning the transfer of control of the electronic document will allocate the risks and liabilities of the parties as that other law now does so for third parties who hold tangible documents and fail to deliver the documents.

Compiler's Comments

Effective Date: This section is effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

Part 2

Warehouse Receipts — Special Provisions

30-7-201. Person that may issue a warehouse receipt — storage under government bond.

Official Comment

[*Corresponding U.C.C. Section:* Section 7-201, U.C.C.]

Prior Uniform Statutory Provision: Former Section 7-201.

Changes: Update for style only.

Purposes:

It is not intended by re-enactment of subsection (a) [subsection (1)] to repeal any provisions of special licensing or other statutes regulating who may become a warehouse. Limitations on the transfer of the receipts and criminal sanctions for violation of such limitations are not impaired. Section 7-103 [30-7-103]. Compare Section 7-401(4) [30-7-401(4)] on the liability of the issuer in such cases. Subsection (b) [subsection (2)] covers receipts issued by the owner for whiskey or other goods stored in bonded warehouses under such statutes as 26 U.S.C. Chapter 51.

Compiler's Comments

2005 Amendment: Chapter 575 in catchline substituted "Person that" for "Who"; in (1) at end and (2) at end substituted "warehouse" for "warehouseman"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-7-202. Form of warehouse receipt.

Official Comment

[*Corresponding U.C.C. Section:* Section 7-202, U.C.C.]

Prior Uniform Statutory Provision: Former Section 7-202.

Changes: Language is updated to accommodate electronic commerce and to reflect modern style.

Purposes:

1. This section does not displace any particular legislation that requires other terms in a warehouse receipt or that may require a particular form of a warehouse receipt. This section does not require that a warehouse receipt be issued. A warehouse receipt that is issued need not contain any of the terms listed in subsection (b) [subsection (2)] in order to qualify as a warehouse receipt as long as the receipt falls within the definition of "warehouse receipt" in Article 1 [Title 30, chapter 1]. The only consequence of a warehouse receipt not containing any term listed in subsection (b) [subsection (2)] is that a person injured by a term's omission has a right as against the warehouse for harm caused by the omission.

2. The unique identification code referred to in subsection (b)(3) [subsection (2)(c)] can include any combination of letters, number, signs, and/or symbols that provide a unique identification. Whether an electronic or tangible warehouse receipt contains a signature will be resolved with the definition of sign in Section 7-102 [30-7-102].

Compiler's Comments

2005 Amendment: Chapter 575 in catchline at end deleted "essential terms — optional terms"; in (2) in introductory clause near beginning substituted "receipt provides for" for "receipt embodies within its written or printed terms" and in middle substituted "warehouse" for "warehouseman"; in (2)(a) inserted "facility"; in (2)(c) substituted "unique identification code" for "consecutive number"; in (2)(d) in two places substituted "named" for "specified"; in (2)(g) substituted "warehouse or its agent" for "warehouseman, which may be made by his authorized agent"; in (2)(h) substituted "that the warehouse owns" for "of which the warehouseman is owner"; in (2)(i) in two places substituted "warehouse" for "warehouseman" and after "security interest" deleted "(30-7-209)"; in (3) near beginning substituted "warehouse" for "warehouseman"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-7-203. Liability for nonreceipt or misdescription.

Official Comment

[*Corresponding U.C.C. Section:* Section 7-203, U.C.C.]

Prior Uniform Statutory Provision: Former Section 7-203.

Changes: Changes to this section are for style only.

Purpose:

This section is a simplified restatement of existing law as to the method by which a bailee may avoid responsibility for the accuracy of descriptions which are made by or in reliance upon information furnished by the depositor. The issuer is liable on documents issued by an agent, contrary to instructions of its principal, without receiving goods. No disclaimer of the latter liability is permitted.

Compiler's Comments

2005 Amendment: Chapter 575 in introductory clause near middle after "goods" inserted "in the document"; in (2) at end substituted "has notice of the nonreceipt or misdescription" for "otherwise has notice"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-7-204. Duty of care — contractual limitation of warehouse's liability.

Official Comment

[*Corresponding U.C.C. Section:* Section 7-204, U.C.C.]

Prior Uniform Statutory Provision: Former Section 7-204.

Changes: Updated to reflect modern, standard commercial practices.

Purposes of Changes:

1. Subsection (a) [subsection (1)] continues the rule from former Section 7-204 [30-7-204] on the warehouse's obligation to exercise reasonable care without change.

2. Former Section 7-204(2) [30-7-204(2), 2003 MCA] required that the term limiting damages do so by setting forth a specific liability per article or item or of a value per unit of weight. This requirement has been deleted as out of step with modern industry practice. Under subsection (b) [subsection (2)] a warehouse may limit its liability for damages for loss of or damage to the goods by a term in the warehouse receipt or storage agreement. The parties cannot disclaim by contract the warehouse's obligation of care. Section 1-302 [30-1-302].

3. Former Section 7-204(2) [30-7-204(2), 2003 MCA] also provided that an increased rate can not be charged if contrary to a tariff. That language has been deleted. If a tariff is required under state or federal law, pursuant to Section 7-103(a) [30-7-103(1)], the tariff would control over the rule of this section allowing an increased rate. The provisions of a non-mandatory tariff may be incorporated by reference in the parties' agreement. See Comment 2 to Section 7-103 [30-7-103]. Subsection (c) [subsection (3)] deletes the reference to tariffs for the same reason that the reference has been omitted in subsection (b) [subsection (2)].

4. As under former Section 7-204(2) [30-7-204(2), 2003 MCA], subsection (b) [subsection (2)] provides that a limitation of damages is ineffective if the warehouse has converted the goods to its own use. A mere failure to redeliver the goods is not conversion to the warehouse's own use. Conversion to its own use has a specialized meaning in the case law that is narrower than the idea of conversion generally.

5. Storage agreements commonly establish the contractual relationship between warehouses and depositors who have an on-going relationship. The storage agreement may allow for the movement into and out of a warehouse without the necessity of issuing or amending a warehouse receipt upon each entry or exit of goods from the warehouse.

Compiler's Comments

2005 Amendment: Chapter 575 in catchline substituted "warehouse's" for "warehouseman's"; in (1) near beginning substituted "warehouse" for "warehouseman"; in (2) at end of first sentence substituted "damage beyond which the warehouse is not liable" for "damage, and setting forth a specific liability per article or item, or value per unit of weight, beyond which the warehouseman shall not be liable", inserted second sentence relating to limitation upon conversion, in third sentence substituted "The warehouse's liability, on request of the bailor in a record" for "that such liability may on written request of the bailor" and at end substituted "goods covered by the storage agreement or the warehouse receipt" for "goods thereunder", in fourth sentence at end substituted "valuation of the goods" for "valuation, but that no such increase shall be permitted contrary to a lawful limitation of liability contained in the warehouseman's tariff, if any", and deleted former last sentence that read: "No such limitation is effective with respect to the warehouseman's liability for conversion to his own use"; in (3) at end substituted "storage agreement" for "tariff"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

Omitted Subsection: Montana has no subsection (4) which under the proposed version provides that states may wish to supplement this section with more rigid standards for bailees.

30-7-205. Title under warehouse receipt defeated in certain cases.

Official Comment

[*Corresponding U.C.C. Section:* Section 7-205, U.C.C.]

Prior Uniform Statutory Provision: Former Section 7-205.

Changes: Changes for style only.

Purposes:

1. The typical case covered by this section is that of the warehouse-dealer in grain, and the substantive question at issue is whether in case the warehouse becomes insolvent the receipt holders shall be able to trace and recover grain shipped to farmers and other purchasers from the elevator. This was possible under the old acts, although courts were eager to find estoppels to prevent it. The practical difficulty of tracing fungible grain means that the preservation of this theoretical right adds little to the commercial acceptability of negotiable grain receipts, which really circulate on the credit of the warehouse. Moreover, on default of the warehouse, the receipt holders at least share in what grain remains, whereas retaking the grain from a good faith cash purchaser reduces the purchaser completely to the status of general creditor in a situation where there was very little the purchaser could do to guard against the loss. Compare 15 U.S.C. Section 714p enacted in 1955.

2. This provision applies to both negotiable and nonnegotiable warehouse receipts. The concept of due negotiation is provided for in 7-501 [30-7-501]. The definition of "buyer in ordinary course" is in Article 1 [Title 30, chapter 1] and provides, among other things, that a buyer must either have possession or a right to obtain the goods under Article 2 [Title 30, chapter 2] in order to be a buyer in ordinary course. This section requires actual delivery of the fungible goods to the buyer in ordinary course. Delivery requires voluntary transfer of possession of the fungible goods to the buyer. See amended Section 2-103 [30-2-103]. This section is not satisfied by the delivery of the document of title to the buyer in ordinary course.

Compiler's Comments

2005 Amendment: Chapter 575 near middle substituted "warehouse that" for "warehouseman who" and near end substituted "if the receipt is negotiable and" for "though it". Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-7-206. Termination of storage at warehouse's option.

Official Comment

[*Corresponding U.C.C. Section:* Section 7-206, U.C.C.]

Prior Uniform Statutory Provision: Former Section 7-206.

Changes: Changes for style.

Purposes:

1. Most warehousing is for an indefinite term, the bailor being entitled to delivery on reasonable demand. It is necessary to define the warehouse's power to terminate the bailment, since it would be commercially intolerable to allow warehouses to order removal of the goods on short notice. The thirty day period provided where the document does not carry its own period of termination corresponds to commercial practice of computing rates on a monthly basis. The right to terminate under subsection (a) [subsection (1)] includes a right to require payment of "any charges", but does not depend on the existence of unpaid charges.

2. In permitting expeditious disposition of perishable and hazardous goods the pre-Code Uniform Warehouse Receipts Act, Section 34, made no distinction between cases where the warehouse knowingly undertook to store such goods and cases where the goods were discovered to be of that character subsequent to storage. The former situation presents no such emergency as justifies the summary power of removal and sale. Subsections (b) and (c) [subsections (2) and (3)] distinguish between the two situations.

3. Protection of its lien is the only interest which the warehouse has to justify summary sale of perishable goods which are not hazardous. This same interest must be recognized when the stored goods, although not perishable, decline in market value to a point which threatens the warehouse's security.

4. The right to order removal of stored goods is subject to provisions of the public warehousing laws of some states forbidding warehouses from discriminating among customers. Nor does the section relieve the warehouse of any obligation under the state laws to secure the approval of a public official before disposing of deteriorating goods. Such regulatory statutes and the regulations under them remain in force and operative. Section 7-103 [30-7-103].

Compiler's Comments

2005 Amendment: Chapter 575 in catchline substituted "warehouse's" for "warehouseman's"; in (1) in first sentence near beginning substituted "warehouse, by giving notice to" for "warehouseman may on notifying" and near middle after "document" inserted "of title" and in second sentence at end substituted "notice, the warehouse may sell them pursuant to 30-7-210" for "notification, the warehouseman may sell them in accordance with the provisions of the section on enforcement of a warehouseman's lien (30-7-210)"; in (2) near beginning substituted "warehouse" for "warehouseman" and near middle substituted "and 30-7-210, the warehouse may specify in the notice given under subsection (1)" for "for notification, advertisement and sale, the warehouseman may specify in the notification"; in (3) in first sentence near beginning substituted "warehouse did not have notice" for "warehouseman had no notice", near middle substituted "warehouse facilities, or other persons, the warehouse" for "warehouse or to persons, the warehouseman", and near end after "advertisement" inserted "or posting" and in second sentence near beginning substituted "warehouse" for "warehouseman"; in (4) at beginning substituted "A warehouse shall" for "The warehouseman must"; in (5) at beginning substituted "A warehouse" for "The warehouseman"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-7-207. Goods must be kept separate — fungible goods.

Official Comment

[*Corresponding U.C.C. Section:* Section 7-207, U.C.C.]

Prior Uniform Statutory Provision: Former Section 7-207.

Changes: Changes for style only.

Purposes:

No change of substance is made from former Section 7-207 [30-7-207]. Holders to whom overissued receipts have been duly negotiated shall share in a mass of fungible goods. Where individual ownership interests are merged into claims on a common fund, as is necessarily the case with fungible goods, there is no policy reason for discriminating between successive purchasers of similar claims.

Compiler's Comments

2005 Amendment: Chapter 575 in first sentence near middle substituted "warehouse shall" for "warehouseman must"; in (2) at beginning of first sentence substituted "If different lots of fungible goods are commingled, the goods" for "Fungible goods so commingled are" and near middle substituted "warehouse" for "warehouseman" and in second sentence substituted "warehouse" for "warehouseman"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-7-208. Altered warehouse receipts.

Official Comment

[*Corresponding U.C.C. Section:* Section 7-208, U.C.C.]

Prior Uniform Statutory Provision: Former Section 7-208.

Changes: To accommodate electronic documents of title.

Purpose:

1. The execution of tangible warehouse receipts in blank is a dangerous practice. As between the issuer and an innocent purchaser the risks should clearly fall on the former. The purchaser must have purchased the tangible negotiable warehouse receipt in good faith and for value to be protected under the rule of the first sentence which is a limited exception to the general rule in the second sentence. Electronic document of title systems should have protection against unauthorized access and unauthorized changes. Thus the protection of the first sentence is not necessary in the context of electronic documents.

2. Under the second sentence of this section, an unauthorized alteration whether made with or without fraudulent intent does not relieve the issuer of its liability on the warehouse receipt as originally executed. The unauthorized alteration itself is of course ineffective against the warehouse. This rule applies to both tangible and electronic warehouse receipts.

Compiler's Comments

2005 Amendment: Chapter 575 in first sentence near beginning inserted "tangible" and near middle inserted "good faith"; in second sentence near middle inserted "tangible or electronic warehouse"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-7-209. Lien of warehouse.

Official Comment

[*Corresponding U.C.C. Section:* Section 7-209, U.C.C.]

Prior Uniform Statutory Provision: Former Sections 7-209 and 7-503.

Changes: Expanded to recognize warehouse lien when a warehouse receipt is not issued but goods are covered by a storage agreement.

Purposes:

1. Subsection (a) [subsection (1)] defines the warehouse's statutory lien. Other than allowing a warehouse to claim a lien under this section when there is a storage agreement and not a warehouse receipt, this section remains unchanged in substance from former Section 7-209(1) [30-7-209(1)]. Under the first sentence, a specific lien attaches automatically without express notation on the receipt or storage agreement with regard to goods stored under the receipt or the storage agreement. That lien is limited to the usual charges arising out of a storage transaction.

Example 1: Bailor stored goods with a warehouse and the warehouse issued a warehouse receipt. A lien against those goods arose as set forth in subsection (a) [subsection (1)], the first sentence, for the charges for storage and the other expenses of those goods. The warehouse may enforce its lien under Section 7-210 [30-7-210] as against the bailor. Whether the warehouse receipt is negotiable or nonnegotiable is not important to the warehouse's rights as against the bailor.

Under the second sentence, by notation on the receipt or storage agreement, the lien can be made a general lien extending to like charges in relation to other goods. Both the specific lien and general lien are as to goods in the possession of the warehouse and extend to proceeds from the goods as long as the proceeds are in the possession of the warehouse. The same rules apply whether the receipt is negotiable or non-negotiable.

Example 2: Bailor stored goods (lot A) with a warehouse and the warehouse issued a warehouse receipt for those goods. In the warehouse receipt it is stated that the warehouse will also have a lien on goods covered by the warehouse receipt for storage charges and the other expenses for any other goods that are stored with the warehouse by the bailor. The statement about the lien on other goods does not specify an amount or a rate. Bailor then stored other goods (lot B) with the warehouse. Under subsection (a) [subsection (1)], first sentence, the warehouse has a lien on the specific goods (lot A) covered by the warehouse receipt. Under subsection (a) [subsection (1)], second sentence, the warehouse has a lien on the goods in lot A for the storage charges and the other expenses arising from the goods in lot B. That lien is enforceable as against the bailor regardless of whether the receipt is negotiable or nonnegotiable.

Under the third sentence, if the warehouse receipt is negotiable, the lien as against a holder of that receipt by due negotiation is limited to the amount or rate specified on the receipt for the specific lien or the general lien, or, if none is specified, to a reasonable charge for storage of the specific goods covered by the receipt for storage after the date of the receipt.

Example 3: Same facts as Example 1 except that the warehouse receipt is negotiable and has been duly negotiated (Section 7-501 [30-7-501]) to a person other than the bailor. Under the last sentence of subsection (a) [subsection (1)], the warehouse may enforce its lien against the bailor's goods stored in the warehouse as against the person to whom the negotiable warehouse receipt has been duly negotiated. Section 7-502 [30-7-502]. That lien is limited to the charges or rates specified in the receipt or a reasonable charge for storage as stated in the last sentence of subsection (a) [subsection (1)].

Example 4: Same facts as Example 2 except that the warehouse receipt is negotiable and has been duly negotiated (Section 7-501 [30-7-501]) to a person other than the bailor. Under the last sentence of subsection (a) [subsection (1)], the lien on lot A goods for the storage charges and the other expenses arising from storage of lot B goods is not enforceable as against the person to whom the receipt has been duly negotiated. Without a statement of a specified amount or rate for the general lien, the warehouse's general lien is not enforceable as against the person to whom the negotiable document has been duly negotiated. However, the warehouse lien for charges and expenses related to storage of lot A goods is still enforceable as against the person to whom the receipt was duly negotiated.

Example 5. Same facts as Examples 2 and 4 except the warehouse had stated on the negotiable warehouse receipt a specified amount or rate for the general lien on other goods (lot B). Under the last sentence of subsection (a) [subsection (1)], the general lien on lot A goods for the storage charges and the other expenses arising from storage of lot B goods is enforceable as against the person to whom the receipt has been duly negotiated.

2. Subsection (b) [subsection (2)] provides for a security interest based upon agreement. Such a security interest arises out of relations between the parties other than bailment for storage or transportation, as where the bailee assumes the role of financier or performs a manufacturing operation, extending credit in reliance upon the goods covered by the receipt. Such a security interest is not a statutory lien. Compare Sections 9-109 and 9-333 [30-9A-109 and 30-9A-333]. It is governed in all respects by Article 9 [Title 30, chapter 9A], except that subsection (b) [subsection (2)] requires that the receipt specify a maximum amount and limits the security interest to the amount specified. A warehouse could also take a security interest to secure its charges for storage and the other expenses listed in subsection (a) [subsection (1)] to protect these claims upon the loss of the statutory possessory warehouse lien if the warehouse loses possession of the goods as provided in subsection (e) [subsection (5)].

Example 6: Bailor stores goods with a warehouse and the warehouse issues a warehouse receipt that states that the warehouse is taking a security interest in the bailed goods for charges of storage, expenses, for money advanced, for manufacturing services rendered, and all other obligations that the bailor may owe the warehouse. That is a security interest covered in all respects by Article 9 [Title 30, chapter 9A]. Subsection (b) [subsection (2)]. As allowed by this section, a warehouse may rely upon its statutory possessory lien to protect its charges for storage and the other expenses related to storage. For those storage charges covered by the statutory possessory lien, the warehouse is not required to use a security interest under subsection (b) [subsection (2)].

3. Subsections (a) and (b) [subsections (1) and (2)] validate the lien and security interest "against the bailor." Under basic principles of derivative rights as provided in Section 7-504 [30-7-504], the warehouse lien is also valid as against parties who obtain their rights from the bailor except as otherwise provided in subsection (a) [subsection (1)], third sentence, or subsection (c) [subsection (3)].

Example 7: Bailor stores goods with a warehouse and the warehouse issues a nonnegotiable warehouse receipt that also claims a general lien in other goods stored with the warehouse. A lien on the bailed goods for the charges for storage and the other expenses arises under subsection (a) [subsection (1)]. Bailor notifies the warehouse that the goods have been sold to Buyer and the bailee acknowledges that fact to the Buyer. Section 2-503 [30-2-503]. The warehouse lien for storage of those goods is effective against Buyer for both the specific lien and the general lien. Section 7-504 [30-7-504].

Example 8: Bailor stores goods with a warehouse and the warehouse issues a nonnegotiable warehouse receipt. A lien on the bailed goods for the charges for storage and the other expenses arises under subsection (a) [subsection (1)]. Bailor grants a security interest in the goods while the goods are in the warehouse's possession to Secured Party (SP) who properly perfects a security interest in the goods. See Revised 9-312(d) [30-9A-312(4)]. The warehouse lien is superior in priority over SP's security interest. See Revised 9-203(b)(2) [30-9A-203(2)(b)] (debtor can grant a security interest to the extent of debtor's rights in the collateral).

Example 9: Bailor stores goods with a warehouse and the warehouse issues a negotiable warehouse receipt. A lien on the bailed goods for the charges for storage and the other expenses arises under subsection (a) [subsection (1)]. Bailor grants a security interest in the negotiable document to SP. SP properly perfects its interest in the negotiable document by taking possession through a 'due negotiation.' Revised 9-312(c) [30-9A-312(3)]. SP's security interest is subordinate to the warehouse lien. Section 7-209(a) [30-7-209(1)], third sentence. Given that bailor's rights are subject to the warehouse lien, the bailor cannot grant to the SP greater rights than the bailor has under Section 9-203(b)(2) [30-9A-203(2)(b)], perfection of the security interest in the negotiable document and the goods covered by the document through SP's filing of a financing statement should not give a different result.

As against third parties who have interests in the goods prior to the storage with the warehouse, subsection (c) [subsection (3)] continues the rule under the prior uniform statutory provision that to validate the lien or security interest of the warehouse, the owner must have entrusted the goods to the depositor, and that the circumstances must be such that a pledge by the depositor to a good faith purchaser for value would have been valid. Thus the owner's interest will not be subjected to a lien or security interest arising out of a deposit of its goods by a thief. The warehouse may be protected because of the actual, implied or apparent authority of the depositor, because of a Factor's Act, or because of other circumstances which would protect a bona fide pledgee, unless those circumstances are denied effect under the second sentence of subsection (c) [subsection (3)]. The language of Section 7-503 [30-7-503] is brought into subsection (c) [subsection (3)] for purposes of clarity. The comments to Section 7-503 [30-7-503] are helpful in interpreting delivery, entrustment or acquiescence.

Where the third party is the holder of a security interest, obtained prior to the issuance of a negotiable warehouse receipt, the rights of the warehouse depend on the priority given to a hypothetical bona fide pledgee by Article 9 [Title 30, chapter 9A], particularly Section 9-322 [30-9A-322]. Thus the special priority granted to statutory liens by Section 9-333 does not apply to liens under subsection (a) [subsection (1)] of this section, since subsection (c) [subsection (3)], second sentence, "expressly provides otherwise" within the meaning of Section 9-333 [30-9A-333].

As to household goods, however, subsection (d) [subsection (4)] makes the warehouse's lien "for charges and expenses in relation to the goods" effective against all persons if the depositor was the legal possessor. The purpose of the exception is to permit the warehouse to accept household goods for storage in sole reliance on the value of the goods themselves, especially in situations of family emergency.

Example 10: Bailor grants a perfected security interest in the goods to SP prior to storage of the goods with the warehouse. Bailor then stores goods with the warehouse and the warehouse issues a warehouse receipt for the goods. A warehouse lien on the bailed goods for the charges for storage or other expenses arises under subsection (a) [subsection (1)]. The warehouse lien is not effective as against SP unless SP entrusted the goods to the bailor with actual or apparent authority to ship store, or sell the goods or with power of disposition under subsection (c)(1) [subsection (3)(a)] or acquiesced in the bailor's procurement of a document of title under subsection (c)(2) [subsection (3)(b)]. This result obtains whether the receipt is negotiable or nonnegotiable.

Example 11: Sheriff who had lawfully repossessed household goods in an eviction action stored the goods with a warehouse. A lien on the bailed goods arises under subsection (a) [subsection (1)]. The lien is effective as against the owner of the goods. Subsection (d) [subsection (4)].

4. As under previous law, this section creates a statutory possessory lien in favor of the warehouse on the goods stored with the warehouse or on the proceeds of the goods. The warehouse loses its lien if it loses possession of the goods or the proceeds. Subsection (e) [subsection (5)].

5. Where goods have been stored under a non-negotiable warehouse receipt and are sold by the person to whom the receipt has been issued, frequently the goods are not withdrawn by the new owner. The obligations of the seller of the goods in this situation are set forth in Section 2-503(4) [30-2-503(4)] on tender of delivery and include procurement of an acknowledgment by the bailee of the buyer's right to possession of the goods. If a new receipt is requested, such an acknowledgment can be withheld until storage charges have been paid or provided for. The statutory lien for charges on the goods sold, granted by the first sentence of subsection (a) [subsection (1)], continues valid unless the bailee gives it up. See Section 7-403 [30-7-403]. But once a new receipt is issued to the buyer, the buyer becomes "the person on whose account the goods are held" under the second sentence of subsection (a) [subsection (1)]; unless the buyer undertakes liability for charges in relation to other goods stored by the seller, there is no general lien against the buyer for such charges. Of course, the bailee may preserve the general lien in such a case either by an arrangement by which the buyer "is liable for" such charges, or by reserving a security interest under subsection (b) [subsection (2)].

6. A possessory warehouse lien arises as provided under subsection (a) [subsection (1)] if the parties to the bailment have a storage agreement or a warehouse receipt is issued. In the modern warehouse, the bailor and the bailee may enter into a master contract governing the bailment with the bailee and bailor keeping track of the goods stored pursuant to the master contract by notation on their respective books and records and the parties send notification via electronic communication as to what goods are covered by the master contract. Warehouse receipts are not issued. See Comment 4 to Section 7-204 [30-7-204]. There is no particular form for a warehouse receipt and failure to contain any of the terms listed in Section 7-202 [30-7-202] does not deprive the warehouse of its lien that arises under subsection (a) [subsection (1)].

Compiler's Comments

2005 Amendment: Chapter 575 in catchline substituted "warehouse" for "warehouseman"; in (1) in first sentence near beginning substituted "warehouse" for "warehouseman" and inserted "or storage agreement", in second sentence near middle inserted "or storage agreement", substituted "warehouse" for "warehouseman", near end substituted "the goods covered by the warehouse receipt or storage agreement or on the proceeds thereof in its possession for those" for "him for such", and at end substituted "warehouse" for "warehouseman", and in third sentence near beginning substituted "warehouse's" for "warehouseman's" and near end inserted "specific"; in (2) in first sentence near beginning substituted "warehouse" for "warehouseman" and inserted "under chapter 9A" and at end of second sentence substituted "chapter 9A" for "the Chapter on Secured Transactions (Chapter 9A)"; in (3) near beginning substituted "warehouse's" for "warehouseman's" and at end of introductory clause substituted "However, the lien or security interest is not effective against a person that before issuance of a document of title had a legal interest or a perfected security interest in the goods and that did not" for "but is not effective against a person as to whom the document confers no right in the goods covered by it under 30-7-503"; inserted (3)(a) and (3)(b) concerning delivery or acquiescing relating to bailors; inserted (4) relating to household goods; in (5) near beginning substituted "warehouse" for "warehouseman"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does

not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-7-210. Enforcement of warehouse's lien.

Official Comment

[*Corresponding U.C.C. Section:* Section 7-210, U.C.C.]

Prior Uniform Statutory Provision: Former Section 7-210.

Changes: Update to accommodate electronic commerce and for style.

Purposes:

1. Subsection (a) [subsection (1)] makes "commercial reasonableness" the standard for foreclosure proceedings in all cases except non-commercial storage with a warehouse. The latter category embraces principally storage of household goods by private owners; and for such cases the detailed provisions as to notification, publication and public sale are retained in subsection (b) [subsection (2)] with one change. The requirement in former Section 7-210(2)(b) [30-7-210(2)(b), 2003 MCA] that the notification must be sent in person or by registered or certified mail has been deleted. Notification may be sent by any reasonable means as provided in Section 1-202 [30-1-210]. The swifter, more flexible procedure of subsection (a) [subsection (1)] is appropriate to commercial storage. Compare seller's power of resale on breach by buyer under the provisions of the Article on Sales (Section 2-706) [30-2-706]. Commercial reasonableness is a flexible concept that allows for a wide variety of actions to satisfy the rule of this section, including electronic means of posting and sale.

2. The provisions of subsections (d) and (e) [subsections (4) and (5)] permitting the bailee to bid at public sales and confirming the title of purchasers at foreclosure sales are designed to secure more bidding and better prices and remain unchanged from former Section 7-210 [30-7-210, 2003 MCA].

3. A warehouses may have recourse to an interpleader action in appropriate circumstances. See Section 7-603 [30-7-603].

4. If a warehouse has both a warehouse lien and a security interest, the warehouse may enforce both the lien and the security interest simultaneously by using the procedures of Article 9 [Title 30, chapter 9A]. Section 7-210 [30-7-210] adopts as its touchstone "commercial reasonableness" for the enforcement of a warehouse lien. Following the procedures of Article 9 [Title 30, chapter 9A] satisfies "commercial reasonableness."

Compiler's Comments

2005 Amendment: Chapter 575 in catchline substituted "warehouse's" for "warehouseman's"; in (1) in first sentence near beginning substituted "warehouse's" for "warehouseman's" and near middle substituted "packages" for "parcels", in third sentence near middle substituted "warehouse" for "warehouseman", in fourth sentence at beginning substituted "The warehouse has sold in a commercially reasonable manner if the warehouse" for "If the warehouseman either" and at end deleted "he has sold in a commercially reasonable manner", and in fifth sentence substituted "ensure" for "insure"; in (2) in introductory clause near beginning substituted "warehouse's" for "warehouseman's" and at end substituted "if the following requirements are satisfied" for "as follows"; deleted former (2)(b) that read: "(b) The notification must be delivered in person or sent by registered or certified letter to the last known address of any person to be notified"; in (3) in first sentence near end substituted "in complying with" for "under" and in second sentence substituted "may" for "must" and substituted "warehouse" for "warehouseman"; in (4) substituted "warehouse" for "warehouseman"; in (5) near beginning substituted "warehouse's" for "warehouseman's" and at end substituted "the warehouse's noncompliance with this section" for "noncompliance by the warehouseman with the requirements of this section"; in (6) at beginning substituted "warehouse" for "warehouseman"; in (9) near beginning substituted "warehouse" for "warehouseman"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

Part 3
Bills of Lading — Special Provisions

Part Case Notes

Limitation of Amount Where Value Not Disclosed: Shipper's failure to list antique mirrors as items of extraordinary value did not bar its recovery from carrier for their destruction in transit where, although bills of lading contained provisions limiting carrier's liability for articles of extraordinary value unless specifically listed, the shipper was not advised of such provision nor given an opportunity to list the mirrors as having extraordinary value and, in fact, did not see the bills until the carrier had completed the trip. Cordingley v. Allied Van Lines, Inc., 563 F2d 960 (C.A. Mont. 1977).

30-7-301. Liability for nonreceipt or misdescription — "said to contain" — "shipper's load and count" — improper handling.

Official Comment

[*Corresponding U.C.C. Section:* Section 7-301, U.C.C.]

Prior Uniform Statutory Provision: Former Section 7-301.

Changes: Changes for clarity, style and to recognize deregulation in the transportation industry.

Purposes:

1. This section continues the rules from former Section 7-301 [30-7-301, 2003 MCA] with one substantive change. The obligations of the issuer of the bill of lading under former subsections (2) and (3) [subsections (2) and (3), 2003 MCA] were limited to issuers who were common carriers. Subsections (b) and (c) [subsections (2) and (3), 2005 MCA] apply the same rules to all issuers not just common carriers. This section is compatible with the policies stated in the federal Bills of Lading Act, 49 U.S.C. § 80113 (2000).

2. The language of the pre-Code Uniform Bills of Lading Act suggested that a carrier is ordinarily liable for damage caused by improper loading, but may relieve itself of liability by disclosing on the bill that shipper actually loaded. A more accurate statement of the law is that the carrier is not liable for losses caused by act or default of the shipper, which would include improper loading. There was some question whether under pre-Code law a carrier was liable even to a good faith purchaser of a negotiable bill for such losses, if the shipper's faulty loading in fact caused the loss. Subsection (d) [subsection (4)] permits the carrier to bar, by disclosure of shipper's loading, liability to a good faith purchaser. There is no implication that decisions such as Modern Tool Corp. v. Pennsylvania R. Co., 100 F.Supp. 595 (D.N.J.1951), are disapproved.

3. This section is a restatement of existing law as to the method by which a bailee may avoid responsibility for the accuracy of descriptions which are made by or in reliance upon information furnished by the depositor or shipper. The wording in this section - "contents or condition of contents of packages unknown" or "shipper's weight, load and count" - to indicate that the shipper loaded the goods or that the carrier does not know the description, condition, or contents of the loaded packages continues to be appropriate as commonly understood in the transportation industry. The reasons for this wording are as important in 2002 as when the prior section initially was approved. The issuer is liable on documents issued by an agent, contrary to instructions of his principal, without receiving goods. No disclaimer of this liability is permitted since it is not a matter either of the care of the goods or their description.

4. The shipper's erroneous report to the carrier concerning the goods may cause damage to the carrier. Subsection (e) [subsection (5)] therefore provides appropriate indemnity.

5. The word "freight" in the former Section 7-301 [30-7-301] has been changed to "goods" to conform to international and domestic land transport usage in which "freight" means the price paid for carriage of the goods and not the goods themselves. Hence, changing the word "freight" to the word "goods" is a clarifying change that fits both international and domestic practice.

Compiler's Comments

2005 Amendment: Chapter 575 in (1) near middle after "document" inserted "of title"; in (2) near beginning substituted "the issuer of the bill of lading" for "an issuer who is a common carrier", near middle substituted "shipped in packages" for "package freight", substituted "if shipped in bulk" for "if bulk freight", and near end substituted "goods" for "freight"; in (3) in first sentence at beginning substituted "If bulk goods are" for "When bulk freight is", after "issuer" inserted "of the bill of lading", near middle substituted "those goods" for "such freight", after "the issuer" deleted "who is a common carrier", and at end substituted "shipper's request in a record to do so" for "written request of the shipper to do so"; in (4) near beginning substituted "including in the bill of lading" for "inserting in the bill"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-7-302. Through bills of lading and similar documents of title.

Official Comment

[*Corresponding U.C.C. Section:* Section 7-302, U.C.C.]

Prior Uniform Statutory Provision: Former Section 7-302.

Changes: To conform to current terminology and for style.

Purposes:

1. This section continues the rules from former Section 7-302 [30-7-302] without substantive change. The term "performing carrier" is substituted for the term "connecting carrier" to conform the terminology of this section with terminology used in recent UNCITRAL and OAS proposals concerning transportation and through bills of lading. This change in terminology is not substantive. This section is compatible with liability on carriers under federal law. See 49 U.S.C. § 14706.

The purpose of this section is to subject the initial carrier under a through bill to suit for breach of the contract of carriage by any performing carrier and to make it clear that any such performing carrier holds the goods on terms which are defined by the document of title even though such performing carrier did not issue the document. Since the performing carrier does hold the goods on the terms of the document, it must honor a proper demand for delivery or a diversion order just as the original bailee would have to. Similarly it has the benefits of the excuses for non-delivery and limitations of liability provided for the original bailee who issued the bill. Unlike the original bailee-issuer, the performing carrier's responsibility is limited to the period while the goods are in its possession. The section does not impose any obligation to issue through bills.

2. The reference to documents other than through bills looks to the possibility that multi-purpose documents may come into use, e.g., combination warehouse receipts and bills of lading. As electronic documents of title come into common usage, storage documents (e.g. warehouse receipts) and transportation documents (e.g. bills of lading) may merge seamlessly into one electronic document that can serve both the storage and transportation segments of the movement of goods.

3. Under subsection (a) [subsection (1)] the issuer of a through bill of lading may become liable for the fault of another person. Subsection (c) [subsection (3)] gives the issuer appropriate rights of recourse.

4. Despite the broad language of subsection (a) [subsection (1)], Section 7-302 [30-7-302] is subject to preemption by federal laws and treaties. Section 7-103 [30-7-103]. The precise scope of federal preemption in the transportation sector is a question determined under federal law.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

2005 Amendment: Chapter 575 in catchline at end inserted "of title"; in (1) in first sentence near beginning after "document" inserted "of title" and in two places substituted reference to a performing carrier for reference to connecting carrier and in second sentence near end inserted "for breach by the other person or the performing carrier"; in (3) substituted "document of title described in subsection (1) is" for "document shall be" and substituted "performing carrier" for "connecting carrier"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-7-303. Diversion — reconsignment — change of instructions.

Official Comment

[*Corresponding U.C.C. Section:* Section 7-303, U.C.C.]

Prior Uniform Statutory Provision: Former Section 7-303.

Changes: To accommodate electronic documents and for style.

Purposes:

1. Diversion is a very common commercial practice which defeats delivery to the consignee originally named in a bill of lading. This section continues former Section 7-303's [30-7-303] safe harbor rules for carriers in situations involving diversion and adapts those rules to electronic documents of title. This section works compatibly with Section 2-705 [30-2-705]. Carriers may as a business matter be willing to accept instructions from consignees in which case the carrier will be liable for misdelivery if the consignee was not the owner or otherwise empowered to dispose of the goods under subsection (a)(4) [subsection (1)(d)]. The section imposes no duty on carriers to undertake diversion. The carrier is of course subject to the provisions of mandatory filed tariffs as provided in Section 7-103 [30-7-103].

2. It should be noted that the section provides only an immunity for carriers against liability for "misdelivery." It does not, for example, defeat the title to the goods which the consignee-buyer may have acquired from the consignor-seller upon delivery of the goods to the carrier under a non-negotiable bill of lading. Thus if the carrier, upon instructions from the consignor, returns the goods to the consignor, the consignee may recover the goods from the consignor or the consignor's insolvent estate. However, under certain circumstances, the consignee's title may be defeated by diversion of the goods in transit to a different consignee. The rights that arise between the consignor-seller and the consignee-buyer out of a contract for the sale of goods are governed by Article 2 [Title 30, chapter 2].

Compiler's Comments

2005 Amendment: Chapter 575 in (1) in introductory clause near end inserted "without liability for misdelivery"; in (1)(b) substituted "even if the consignee has given contrary instructions" for "notwithstanding contrary instructions from the consignee"; in (1)(c) at end after "possession of the" inserted "tangible bill or in control of the electronic"; in (2) substituted "instructions described in subsection (1) are included in" for "such instructions are noted on"; and made minor changes in style. Amendment effective October 1, 2005.

Code Commissioner Correction: The amendments made to this section in sec. 52, Ch. 575, L. 2005, by inserting (1)(d) contained changes that should have been made by amending (1)(c). The code commissioner merged the differences in (1)(d) into (1)(c) and deleted (1)(d) as redundant.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-7-304. Tangible bills of lading in a set.

Official Comment

[*Corresponding U.C.C. Section:* Section 7-304, U.C.C.]

Prior Uniform Statutory Provision: Former Section 7-304.

Changes: To limit bills in a set to tangible bills of lading and to use terminology more consistent with modern usage.

Purposes:

1. Tangible bills of lading in a set are still used in some nations in international trade. Consequently, a tangible bill of lading part of a set could be at issue in a lawsuit that might come within Article 7 [Title 30, chapter 7]. The statement of the legal effect of a lawfully issued set is in accord with existing commercial law relating to maritime and other international tangible bills of lading. This law has been codified in the Hague and Warsaw Conventions and in the Carriage of Goods by Sea Act, the provisions of which would ordinarily govern in situations where bills

in a set are recognized by this Article [Title 30, chapter 7]. Tangible bills of lading in a set are prohibited in domestic trade.

2. Electronic bills of lading in domestic or international trade will not be issued in a set given the requirements of control necessary to deliver the bill to another person. An electronic bill of lading will be a single, authoritative copy. Section 7-106 [30-7-107]. Hence, this section differentiates between electronic bills of lading and tangible bills of lading. This section does not prohibit electronic data messages about goods in transit because these electronic data messages are not the issued bill of lading. Electronic data messages contain information for the carrier's management and handling of the cargo but this information for the carrier's use is not the issued bill of lading.

Compiler's Comments

2005 Amendment: Chapter 575 in catchline at beginning inserted "Tangible"; in (1) in first sentence substituted "international" for "overseas"; in (2) near beginning inserted "tangible", substituted "issued" for "drawn", and substituted "contains an identification code" for "is numbered"; in (3) near beginning inserted "tangible negotiable" and near middle after "document" inserted "of title"; in (4) substituted "tangible bill of lading issued" for "bill of lading drawn"; in (5) near middle inserted "tangible" and substituted "issued" for "drawn"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-7-305. Destination bills.

Official Comment

[*Corresponding U.C.C. Section:* Section 7-305, U.C.C.]

Prior Uniform Statutory Provision: Former Section 7-305.

Changes: To accommodate electronic bills of lading and for style.

Purposes:

1. Subsection (a) [subsection (1)] continues the rules of former Section 7-305(1) [30-7-305(1), 2003 MCA] without substantive change. This proposal is designed to facilitate the use of order bills in connection with fast shipments. Use of order bills on high speed shipments is impeded by the fact that the goods may arrive at destination before the documents, so that no one is ready to take delivery from the carrier. This is especially inconvenient for carriers by truck and air, who do not have terminal facilities where shipments can be held to await the consignee's appearance. Order bills would be useful to take advantage of bank collection. This may be preferable to C.O.D. shipment in which the carrier, e.g. a truck driver, is the collecting and remitting agent. Financing of shipments under this plan would be handled as follows: seller at San Francisco delivers the goods to an airline with instructions to issue a bill in New York to a named bank. Seller receives a receipt embodying this undertaking to issue a destination bill. Airline wires its New York freight agent to issue the bill as instructed by the seller. Seller wires the New York bank a draft on buyer. New York bank indorses the bill to buyer when the buyer honors the draft. Normally seller would act through its own bank in San Francisco, which would extend credit in reliance on the airline's contract to deliver a bill to the order of its New York correspondent. This section is entirely permissive; it imposes no duty to issue such bills. Whether a performing carrier will act as issuing agent is left to agreement between carriers.

2. Subsection (b) [subsection (2)] continues the rule from former Section 7-305(2) [30-7-305(2), 2003 MCA] with accommodation for electronic bills of lading. If the substitute bill changes from an electronic to a tangible medium or vice versa, the issuance of the substitute bill must comply with Section 7-105 [30-7-106] to give the substitute bill validity and effect.

Compiler's Comments

2005 Amendment: Chapter 575 in (2) near middle inserted "possession or control of" and inserted "subject to 30-7-106"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-7-306. Altered bills of lading.

Official Comment

[*Corresponding U.C.C. Section:* Section 7-306, U.C.C.]

Prior Uniform Statutory Provision: Former Section 7-306.

Changes: None

Purposes:

An unauthorized alteration or filling in of a blank, whether made with or without fraudulent intent, does not relieve the issuer of his liability on the document as originally executed. This section applies to both tangible and electronic bills of lading, applying the same rule to both types of bills of lading. The control concept of Section 7-106 [30-7-107] requires that any changes to the electronic document of title be readily identifiable as authorized or unauthorized. Section 7-306 [30-7-306] should be compared to Section 7-208 [30-7-208] where a different rule applies to the unauthorized filling in of a blank for tangible warehouse receipts.

30-7-307. Lien of carrier.

Official Comment

[*Corresponding U.C.C. Section:* Section 7-307, U.C.C.]

Prior Uniform Statutory Provision: Former Section 7-307.

Changes: Expanded to cover proceeds of the goods transported.

Purposes:

1. The section is intended to give carriers a specific statutory lien for charges and expenses similar to that given to warehouses by the first sentence of Section 7-209(a) [30-7-209(1)] and extends that lien to the proceeds of the goods as long as the carrier has possession of the proceeds. But because carriers do not commonly claim a lien for charges in relation to other goods or lend money on the security of goods in their hands, provisions for a general lien or a security interest similar to those in Section 7-209(a) and (b) [30-7-209(1) and (2)] are omitted. Carriers may utilize Article 9 [Title 30, chapter 9A] to obtain a security interest and become a secured party or a carrier may agree to limit its lien rights in a transportation agreement with the shipper. As the lien given by this section is specific, and the storage or transportation often preserves or increases the value of the goods, subsection (b) [subsection (2)] validates the lien against anyone who permitted the bailor to have possession of the goods. Where the carrier is required to receive the goods for transportation, the owner's interest may be subjected to charges and expenses arising out of deposit of his goods by a thief. The crucial mental element is the carrier's knowledge or reason to know of the bailor's lack of authority. If the carrier does not know or have reason to know of the bailor's lack of authority, the carrier has a lien under this section against any person so long as the conditions of subsection (b) [subsection (2)] are satisfied. In light of the crucial mental element, Sections 7-307 and 9-333 [30-7-307 and 30-9A-333] combine to give priority to a carrier's lien over security interests in the goods. In this regard, the judicial decision in In re Sharon Steel Corp., 25 U.C.C. Rep.2d 503, 176 B.R. 384 (W.D. Pa. 1995) is correct and is the controlling precedent.

2. The reference to charges in this section means charges relating to the bailment relationship for transportation. Charges does not mean that the bill of lading must state a specific rate or a specific amount. However, failure to state a specific rate or a specific amount has legal consequences under the second sentence of subsection (a) [subsection (1)].

3. The carrier's specific lien under this section is a possessory lien. See subsection (c) [subsection (3)]. Part 3 of Article 7 [Title 30, chapter 7, part 3] does not require any particular form for a bill of lading. The carrier's lien arises when the carrier has issued a bill of lading.

Compiler's Comments

2005 Amendment: Chapter 575 in (1) near beginning inserted "or on the proceeds thereof in its possession"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-7-308. Enforcement of carrier's lien.

Official Comment

[*Corresponding U.C.C. Section:* Section 7-308, U.C.C.]

Prior Uniform Statutory Provision: Former Section 7-308.

Changes: To conform language to modern usage and for style.

Purposes:

This section is intended to give the carrier an enforcement procedure of its lien coextensive with that given the warehouse in cases other than those covering noncommercial storage by the warehouse. See Section 7-210 [30-7-210] and comments.

Compiler's Comments

2005 Amendment: Chapter 575 in (1) in first sentence near beginning inserted "on goods" and substituted "bulk or in packages" for "bloc or in parcels" and in fourth sentence substituted "The carrier has sold goods in a commercially reasonable manner if the carrier sells the goods" for "If the carrier either sells the goods" and at end deleted "he has sold in a commercially reasonable manner"; in (2) near middle substituted "in complying with" for "under" and near end inserted "of lading"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-7-309. Duty of care — contractual limitation of carrier's liability.

Official Comment

[*Corresponding U.C.C. Section:* Section 7-309, U.C.C.]

Prior Uniform Statutory Provision: Former Section 7-309.

Changes: References to tariffs eliminated because of deregulation, adding reference to transportation agreements, and for style.

Purposes:

1. A bill of lading may also serve as the contract between the carrier and the bailor. Parties in their contract should be able to limit the amount of damages for breach of that contract including breach of the duty to take reasonable care of the goods. The parties cannot disclaim by contract the carrier's obligation of care. Section 1-302 [30-1-302].

Federal statutes and treaties for air, maritime and rail transport may alter the standard of care. These federal statutes and treaties preempt this section when applicable. Section 7-103 [30-7-103]. Subsection (a) [subsection (1)] does not impair any rule of law imposing the liability of an insurer on a common carrier in intrastate commerce. Subsection (b) [subsection (2)], however, applies to the common carrier's liability as an insurer as well as to liability based on negligence. Subsection (b) [subsection (2)] allows the term limiting damages to appear either in the bill of lading or in the parties' transportation agreement. Compare 7-204(b) [30-7-204(2)]. Subsection (c) [subsection (3)] allows the parties to agree to provisions regarding time and manner of presenting claims or commencing actions if the provisions are either in the bill of lading or the transportation agreement. Compare 7-204(c) [30-7-204(3)]. Transportation agreements are commonly used to establish agreed terms between carriers and shippers that have an on-going relationship.

2. References to public tariffs in former Section 7-309(2) and (3) [30-7-309(2) and (3), 2003 MCA] have been deleted in light of the modern era of deregulation. See Comment 2 to Section 7-103 [30-7-103]. If a tariff is required under state or federal law, pursuant to Section 7-103(a) [30-7-103(1)], the tariff would control over the rule of this section. As governed by contract law, parties may incorporate by reference the limits on the amount of damages or the reasonable

provisions as to the time and manner of presenting claims set forth in applicable tariffs, e.g. a maximum unit value beyond which goods are not taken or a disclaimer of responsibility for undeclared articles of extraordinary value.

3. As under former Section 7-309(2) [30-7-309(2), 2003 MCA], subsection (b) [subsection (2)] provides that a limitation of damages is ineffective if the carrier has converted the goods to its own use. A mere failure to redeliver the goods is not conversion to the carrier's own use. Conversion to its own use has a specialized meaning in the case law that is narrower than the idea of conversion generally.

4. As used in this section, damages may include damages arising from delay in delivery. Delivery dates and times are often specified in the parties' contract. See Section 7-403 [30-7-403].

Compiler's Comments

2005 Amendment: Chapter 575 in (1) in second sentence substituted "affect any statute, regulation, or rule" for "repeal or change any law or rule"; in (2) in first sentence near beginning substituted "term in the bill of lading or in a transportation agreement" for "provision", near middle substituted "bill or transportation agreement" for "document", after "consignor" deleted "by the carrier's tariff", and near end after "higher value" deleted "or a value as lawfully provided in the tariff, or where no tariff is filed he is otherwise"; in (3) substituted "commencing" for "instituting" and substituted "transportation agreement" for "tariff"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

Part 4
Warehouse Receipts and Bills of Lading General Obligations

30-7-401. Irregularities in issue of receipt or bill or conduct of issuer.

Official Comment

[*Corresponding U.C.C. Section:* Section 7-401, U.C.C.]

Prior Uniform Statutory Provision: Former Section 7-401.

Changes: Changes for style only.

Purposes:

The bailee's liability on its document despite non-receipt or misdescription of the goods is affirmed in Sections 7-203 and 7-301 [30-7-203 and 30-7-301]. The purpose of this section is to make it clear that regardless of irregularities a document which falls within the definition of document of title imposes on the issuer the obligations stated in this Article [Title 30, chapter 7]. For example, a bailee will not be permitted to avoid its obligation to deliver the goods (Section 7-403) [30-7-403] or its obligation of due care with respect to them (Sections 7-204 and 7-309) [30-7-204 and 30-7-309] by taking the position that no valid "document" was issued because it failed to file a statutory bond or did not pay stamp taxes or did not disclose the place of storage in the document. Sanctions against violations of statutory or administrative duties with respect to documents should be limited to revocation of license or other measures prescribed by the regulation imposing the duty. See Section 7-103 [30-7-103].

Compiler's Comments

2005 Amendment: Chapter 575 in (1) substituted "does not" for "may not" and substituted "statute, rule" for "law"; in (4) substituted "is not a warehouse but the document" for "does not come within the definition of warehouseman if it"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does

not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-7-402. Duplicate receipt or bill — overissue.

Official Comment

[*Corresponding U.C.C. Section:* Section 7-402, U.C.C.]

Prior Uniform Statutory Provision: Former Section 7-402.

Changes: Changes to accommodate electronic documents.

Purposes:

1. This section treats a duplicate which is not properly identified as a duplicate like any other overissue of documents: a purchaser of such a document acquires no title but only a cause of action for damages against the person that made the deception possible, except in the cases noted in the section. But parts of a tangible bill lawfully issued in a set of parts are not "overissue" (Section 7-304) [30-7-304]. Of course, if the issuer has clearly indicated that a document is a duplicate so that no one can be deceived by it, and in fact the duplicate is a correct copy of the original, the issuer is not liable for preparing and delivering such a duplicate copy.

Section 7-105 [30-7-106] allows documents of title to be reissued in another medium. Re-issuance of a document in an alternative medium under Section 7-105 [30-7-106] requires that the original document be surrendered to the issuer in order to make the substitute document the effective document. If the substitute document is not issued in compliance with section 7-105 [30-7-106], then the document should be treated as a duplicate under this section.

2. The section applies to nonnegotiable documents to the extent of providing an action for damages for one who acquires an unmarked duplicate from a transferor who knew the facts and would therefore have had no cause of action against the issuer of the duplicate. Ordinarily the transferee of a nonnegotiable document acquires only the rights of its transferor.

3. Overissue is defined so as to exclude the common situation where two valid documents of different issuers are outstanding for the same goods at the same time. Thus freight forwarders commonly issue bills of lading to their customers for small shipments to be combined into carload shipments for which the railroad will issue a bill of lading to the forwarder. So also a warehouse receipt may be outstanding against goods, and the holder of the receipt may issue delivery orders against the same goods. In these cases dealings with the subsequently issued documents may be effective to transfer title; e.g. negotiation of a delivery order will effectively transfer title in the ordinary case where no dishonesty has occurred and the goods are available to satisfy the orders. Section 7-503 [30-7-503] provides for cases of conflict between documents of different issuers.

Compiler's Comments

2005 Amendment: Chapter 575 in first sentence near middle substituted "tangible bills of lading in a set of parts" for "bills in a set" and at end inserted "or substitute documents issued pursuant to 30-7-106" and in last sentence at end deleted "on its face"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-7-403. Obligation of warehouse or carrier to deliver — excuse.

Official Comment

[*Corresponding U.C.C. Section:* Section 7-403, U.C.C.]

Prior Uniform Statutory Provision: Former Section 7-403.

Changes: Definition in former Section 7-403(4) [30-7-403(4), 2003 MCA] moved to Section 7-102 [30-7-102]; bracketed language in former Section 7-403(1)(b) [not adopted in Montana] deleted; added cross reference to Section 2A-526 [30-2A-526]; changes for style.

Purposes:

1. The present section, following former Section 7-403 [40-7-403, 2003 MCA], is constructed on the basis of stating what previous deliveries or other circumstances operate to excuse the bailee's normal obligation on the document. Accordingly, "justified" deliveries under the pre-Code uniform acts now find their place as "excuse" under subsection (a) [subsection (1)].

2. The principal case covered by subsection (a)(1) [subsection (1)(a)] is delivery to a person whose title is paramount to the rights represented by the document. For example, if a thief deposits stolen goods in a warehouse facility and takes a negotiable receipt, the warehouse is not liable on the receipt if it has surrendered the goods to the true owner, even though the receipt is held by a good faith purchaser. See Section 7-503(a) [30-7-503(1)]. However, if the owner entrusted the goods to a person with power of disposition, and that person deposited the goods and took a negotiable document, the owner receiving delivery would not be rightful as against a holder to whom the negotiable document was duly negotiated, and delivery to the owner would not give the bailee a defense against such a holder. See Sections 7-502(a)(2), 7-503(a)(1) [30-7-502(1)(b), 30-7-503(1)(a)].

3. Subsection (a)(2) [subsection (1)(b)] amounts to a cross reference to all the tort law that determines the varying responsibilities and standards of care applicable to commercial bailees. A restatement of this tort law would be beyond the scope of this Act. Much of the applicable law as to responsibility of bailees for the preservation of the goods and limitation of liability in case of loss has been codified for particular classes of bailees in interstate and foreign commerce by federal legislation and treaty and for intrastate carriers and other bailees by the regulatory state laws preserved by Section 7-103 [30-7-103]. In the absence of governing legislation the common law will prevail subject to the minimum standard of reasonable care prescribed by Sections 7-204 and 7-309 of this Article [30-7-204 and 30-7-309].

The bracketed language found in former Section 7-403(1)(b) [not adopted in Montana] has been deleted thereby leaving the allocations of the burden of going forward with the evidence and the burden of proof to the procedural law of the various states.

Subsection (a)(4) [subsection (1)(d)] contains a cross reference to both the seller's and the lessor's rights to stop delivery under Article 2 and Article 2A respectively [Title 30, chapters 2 and 2A].

4. As under former Section 7-403 [30-7-403, 2003 MCA], there is no requirement that a request for delivery must be accompanied by a formal tender of the amount of the charges due. Rather, the bailee must request payment of the amount of its lien when asked to deliver, and only in case this request is refused is it justified in declining to deliver because of nonpayment of charges. Where delivery without payment is forbidden by law, the request is treated as implicit. Such a prohibition reflects a policy of uniformity to prevent discrimination by failure to request payment in particular cases. Subsection (b) [subsection (2)] must be read in conjunction with the priorities given to the warehouse lien and the carrier lien under Section 7-209 and 7-307 [30-7-209 and 30-7-307], respectively. If the parties are in dispute about whether the request for payment of the lien is legally proper, the bailee may have recourse to interpleader. See Section 7-603 [30-7-603].

5. Subsection (c) [subsection (3)] states the obvious duty of a bailee to take up a negotiable document or note partial deliveries conspicuously thereon, and the result of failure in that duty. It is subject to only one exception, that stated in subsection (a)(1) of this section [subsection (1)(a)] and in Section 7-503(a) [30-7-503(1)]. Subsection (c) [subsection (3)] is limited to cases of delivery to a claimant; it has no application, for example, where goods held under a negotiable document are lawfully sold to enforce the bailee's lien.

6. When courts are considering subsection (a)(7) [subsection (1)(g)], "any other lawful excuse," among others, refers to compliance with court orders under Sections 7-601, 7-602 and 7-603 [30-7-601, 30-7-602 and 30-7-603].

Compiler's Comments

2005 Amendment: Chapter 575 in catchline substituted "warehouse" for "warehouseman"; in (1) near middle substituted "a document of title if the person" for "the document who"; in (1)(c) substituted "warehouse's" for "warehouseman's"; in (1)(d) at end inserted "or by a lessor of its right to stop delivery pursuant to 30-2A-526"; in (1)(e) at end deleted "or tariff regulating such right"; in (3) in introductory clause inserted "the goods" and substituted "of title does not confer a right" for "confers no right"; in (3)(a) inserted "possession or control of"; in (3)(b) substituted "indicate in the document" for "note"; deleted former (4) that read: "(4) "Person entitled under the document" means holder in the case of a negotiable document, or the person to whom delivery is to be made by the terms of or pursuant to written instructions under a nonnegotiable document"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

Optional Language: Montana has not adopted the bracketed language in subsection (1)(b) which deals with the burden of establishing negligence and is optional under the proposed U.C.C.

30-7-404. No liability for good faith delivery pursuant to document of title.

Official Comment

[*Corresponding U.C.C. Section:* Section 7-404, U.C.C.]

Prior Uniform Statutory Provision: Former Section 7-404.

Changes: Changes reflect the definition of good faith in Section 1-201 [7-102, U.C.C.] [30-1-201 and 30-7-102] and for style.

Purposes:

This section uses the test of good faith, as defined in Section 1-201 [7-102, U.C.C.] [30-1-201 and 30-7-102], to continue the policy of former Section 7-404 [30-7-404, 2003 MCA]. Good faith now means "honesty in fact and the observance of reasonable commercial standards of fair dealing." The section states explicitly that the common law rule of "innocent conversion" by unauthorized "intermeddling" with another's property is inapplicable to the operations of commercial carriers and warehousemen that in good faith perform obligations that they have assumed and that generally they are under a legal compulsion to assume. The section applies to delivery to a fraudulent holder of a valid document as well as to delivery to the holder of an invalid document. Of course, in appropriate circumstances, a bailee may use interpleader or other dispute resolution process. See Section 7-603 [30-7-603].

Compiler's Comments

2005 Amendment: Chapter 575 in catchline substituted "document of title" for "receipt or bill"; in introductory clause near beginning after "faith" deleted "including observance of reasonable commercial standards"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

Part 5
Warehouse Receipts and Bills of Lading Negotiation and Transfer

30-7-501. Form of negotiation and requirements of due negotiation.

Official Comment

[*Corresponding U.C.C. Section:* Section 7-501, U.C.C.]

Prior Uniform Statutory Provision: Former Section 7-501.

Changes: To accommodate negotiable electronic documents of title.

Purpose:

1. Subsection (a) [subsection (1)] has been limited to tangible negotiable documents of title but otherwise remains unchanged in substance from the rules in former Section 7-501 [30-7-501, 2003 MCA]. Subsection (b) [subsection (2)] is new and applies to negotiable electronic documents of title. Delivery of a negotiable electronic document is through voluntary transfer of control. Section 1-201 [30-1-201] definition of "delivery." The control concept as applied to negotiable electronic documents of title is the substitute for both possession and indorsement as applied to negotiable tangible documents of title. Section 7-106 [30-7-107].

As under former Section 7-501 [30-7-501], in order to effect a "due negotiation" the negotiation must be in the "regular course of business or financing" in order to transfer greater rights than those held by the person negotiating. The foundation of the mercantile doctrine of good faith purchase for value has always been, as shown by the case situations, the furtherance and protection of the regular course of trade. The reason for allowing a person, in bad faith or in error, to convey away rights which are not its own has from the beginning been to make possible the speedy handling of that great run of commercial transactions which are patently usual and normal.

There are two aspects to the usual and normal course of mercantile dealings, namely, the person making the transfer and the nature of the transaction itself. The first question which arises is: Is the transferor a person with whom it is reasonable to deal as having full powers? In regard to documents of title the only holder whose possession or control appears, commercially, to be in order is almost invariably a person in the trade. No commercial purpose is served by allowing a tramp or a professor to "duly negotiate" an order bill of lading for hides or cotton not their own, and since such a transfer is obviously not in the regular course of business, it is excluded from the scope of the protection of subsections (a)(5) or (b)(3) [subsections (1)(e) or (2)(c)].

The second question posed by the "regular course" qualification is: Is the transaction one which is normally proper to pass full rights without inquiry, even though the transferor itself may not have such rights to pass, and even though the transferor may be acting in breach of duty? In raising this question the "regular course" criterion has the further advantage of limiting, the effective wrongful disposition to transactions whose protection will really further trade. Obviously, the snapping up of goods for quick resale at a price suspiciously below the market deserves no protection as a matter of policy: it is also clearly outside the range of regular course.

Any notice on the document sufficient to put a merchant on inquiry as to the "regular course" quality of the transaction will frustrate a "due negotiation". Thus irregularity of the document or unexplained staleness of a bill of lading may appropriately be recognized as negating a negotiation in "regular" course.

A pre-existing claim constitutes value, and "due negotiation" does not require "new value." A usual and ordinary transaction in which documents are received as security for credit previously extended may be in "regular" course, even though there is a demand for additional collateral because the creditor "deems himself insecure." But the matter has moved out of the regular course of financing if the debtor is thought to be insolvent, the credit previously extended is in effect cancelled, and the creditor snatches a plank in the shipwreck under the guise of a demand for additional collateral. Where a money debt is "paid" in commodity paper, any question of "regular" course disappears, as the case is explicitly excepted from "due negotiation".

2. Negotiation under this section may be made by any holder no matter how the holder acquired possession or control of the document.

3. Subsections (a)(3) and (b)(2) [subsections (1)(c) and (2)(b)] make explicit a matter upon which the intent of the pre-Code law was clear but the language somewhat obscure: a negotiation results from a delivery to a banker or buyer to whose order the document has been taken by the person making the bailment. There is no presumption of irregularity in such a negotiation; it may very well be in "regular course."

4. This Article [Title 30, chapter 7] does not contain any provision creating a presumption of due negotiation to, and full rights in, a holder of a document of title akin to that created by Uniform Commercial Code Article 3 [Title 30, chapter 3]. But the reason of the provisions of this Act (Section 1-307) [30-1-202] on the prima facie authenticity and accuracy of third party documents, joins with the reason of the present section to work such a presumption in favor of any person who has power to make a due negotiation. It would not make sense for this Act [Title 30, chapter 7] to authorize a purchaser to indulge the presumption of regularity if the courts were not also called upon to do so.

5. Subsections (c) and (d) [subsections (3) and (4)] are unchanged from prior law and apply to both tangible and electronic documents of title.

Compiler's Comments

2005 Amendment: Chapter 575 in (1) at beginning inserted "The following rules apply to a tangible"; in (1)(a) at beginning inserted "If the document's original terms"; in (1)(b) substituted "If the document's original terms run to bearer, it is negotiated by delivery alone" for "A negotiable document of title is also negotiated by delivery alone when by its original terms it runs to bearer"; in (1)(d) substituted "the document" for "a negotiable document of title", substituted "named person" for "specified person", and substituted "named person" for "special endorsee"; in (1)(e) at beginning substituted "A document is duly negotiated if" for "A negotiable document of title is "duly negotiated" when" and near middle substituted "this subsection (1)(e)" for "this section"; inserted (2) relating to rules of negotiable electronic documents of title; in (3) after "document" inserted "of title"; in (4) inserted "of lading"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-7-502. Rights acquired by due negotiation.

Official Comment

[*Corresponding U.C.C. Section:* Section 7-502, U.C.C.]

Prior Uniform Statutory Provision: Former Section 7-502.

Changes: To accommodate electronic documents of title and for style.

Purpose:

1. This section applies to both tangible and electronic documents of title. Due negotiation is defined in Section 7-501 [30-7-501]. The several necessary qualifications of the broad principle that the holder of a document acquired in a due negotiation is the owner of the document and the goods have been brought together in the next section.

2. Subsection (a)(3) [subsection (1)(c)] covers the case of "feeding" of a duly negotiated document by subsequent delivery to the bailee of such goods as the document falsely purported to cover; the bailee in such case is estopped as against the holder of the document.

3. The explicit statement in subsection (a)(4) [subsection (1)(d)] of the bailee's direct obligation to the holder precludes the defense that the document in question was "spent" after the carrier had delivered the goods to a previous holder. But the holder is subject to such defenses as non-negligent destruction even though not apparent on the document. The sentence on delivery orders applies only to delivery orders in negotiable form which have been duly negotiated. On delivery orders, see also Section 7-503(b) [30-7-503(2)] and Comment.

4. Subsection (b) [subsection (2)] continues the law which gave full effect to the issuance or due negotiation of a negotiable document. The subsection adds nothing to the effect of the rules stated in subsection (a) [subsection (1)], but it has been included since such explicit reference was provided under former Section 7-502 [30-7-502] to preserve the right of a purchaser by due negotiation. The listing is not exhaustive. The language"any stoppage" is included lest an inference be drawn that a stoppage of the goods before or after transit might cut off or otherwise impair the purchaser's rights.

Compiler's Comments

2005 Amendment: Chapter 575 in (1) at beginning substituted "Subject to 30-7-205 and 30-7-503" for "Subject to the following section and to the provisions of 30-7-205"; in (2) substituted "30-7-503" for "the following section", inserted "by due negotiation", and after "document" inserted "of title"; in (2)(a) in two places inserted "due"; in (2)(b) substituted "a negotiable tangible document or control of a negotiable electronic document" for "the document"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-7-503. Document of title to goods defeated in certain cases.

Official Comment

[*Corresponding U.C.C. Section:* Section 7-503, U.C.C.]

Prior Uniform Statutory Provision: Former Section 7-503.

Changes: Changes to cross-reference to Article 2A [Title 30, chapter 2A] and for style.

Purposes:

1. In general it may be said that the title of a purchaser by due negotiation prevails over almost any interest in the goods which existed prior to the procurement of the document of title if the possession of the goods by the person obtaining the document derived from any action by the prior claimant which introduced the goods into the stream of commerce or carried them along

that stream. A thief of the goods cannot indeed by shipping or storing them to the thief's own order acquire power to transfer them to a good faith purchaser. Nor can a tenant or mortgagor defeat any rights of a landlord or mortgagee which have been perfected under the local law merely by wrongfully shipping or storing a portion of the crop or other goods. However, "acquiescence" by the landlord or mortgagee does not require active consent under subsection (a)(2) [subsection (1)(b)] and knowledge of the likelihood of storage or shipment with no objection or effort to control it is sufficient to defeat the landlord's or the mortgagee's rights as against one who takes by due negotiation of a negotiable document.

On the other hand, where goods are delivered to a factor for sale, even though the factor has made no advances and is limited in its duty to sell for cash, the goods are "entrusted" to the factor "with actual . . . authority . . . to sell" under subsection (a)(1) [subsection (1)(a)], and if the factor procures a negotiable document of title it can transfer the owner's interest to a purchaser by due negotiation. Further, where the factor is in the business of selling, goods entrusted to it simply for safekeeping or storage may be entrusted under circumstances which give the factor "apparent authority to ship, store or sell" under subsection (a)(1) [subsection (1)(a)], or power of disposition under Section 2-403, 2A-304(2), 2A-305(2), 7-205, or 9-320 [30-2-403, 30-2A-304(2), 30-2A-305(2), 30-7-205, or 30-9A-320], or under a statute such as the earlier Factors Acts, or under a rule of law giving effect to apparent ownership. See Section 1-103 [30-1-102(1) and 30-1-103].

Persons having an interest in goods also frequently deliver or entrust them to agents or servants other than factors for the purpose of shipping or warehousing or under circumstances reasonably contemplating such action. This Act [Title 30, chapter 7] is clear that such persons assume full risk that the agent to whom the goods are so delivered may ship or store in breach of duty, take a document to the agent's own order and then proceed to misappropriate the negotiable document of title that embodies the goods. This Act [Title 30, chapter 7] makes no distinction between possession or mere custody in such situations and finds no exception in the case of larceny by a bailee or the like. The safeguard in such situations lies in the requirement that a due negotiation can occur only "in the regular course of business or financing" and that the purchase be in good faith and without notice. See Section 7-501 [30-7-501]. Documents of title have no market among the commercially inexperienced and the commercially experienced do not take them without inquiry from persons known to be truck drivers or petty clerks even though such persons purport to be operating in their own names.

Again, where the seller allows a buyer to receive goods under a contract for sale, though as a "conditional delivery" or under "cash sale" terms and on explicit agreement for immediate payment, the buyer thereby acquires power to defeat the seller's interest by transfer of the goods to certain good faith purchasers. See Section 2-403 [30-2-403]. Both in policy and under the language of subsection (a)(1) [subsection (1)(a)] that same power must be extended to accomplish the same result if the buyer procures a negotiable document of title to the goods and duly negotiates it.

2. Under subsection (a) [subsection (1)] a delivery order issued by a person having no right in or power over the goods is ineffective unless the owner acts as provided in subsection (a)(1) or (2) [subsection (1)(a) or (1)(b)]. Thus the rights of a transferee of a non-negotiable warehouse receipt can be defeated by a delivery order subsequently issued by the transferor only if the transferee "delivers or entrusts" to the "person procuring" the delivery order or "acquiesces" in that person's procurement. Similarly, a second delivery order issued by the same issuer for the same goods will ordinarily be subject to the first, both under this section and under Section 7-402 [30-7-402]. After a delivery order is validly issued but before it is accepted, it may nevertheless be defeated under subsection (b) [subsection (2)] in much the same way that the rights of a transferee may be defeated under Section 7-504 [30-7-504]. For example, a buyer in ordinary course from the issuer may defeat the rights of the holder of a prior delivery order if the bailee receives notification of the buyer's rights before notification of the holder's rights. Section 7-504(b)(2) [30-7-504(2)(b)]. But an accepted delivery order has the same effect as a document issued by the bailee.

3. Under subsection (c) [subsection (3)] a bill of lading issued to a freight forwarder is subordinated to the freight forwarder's document of title, since the bill on its face gives notice of the fact that a freight forwarder is in the picture and the freight forwarder has in all probability issued a document of title. But the carrier is protected in following the terms of its own bill of lading.

Compiler's Comments

2005 Amendment: Chapter 575 in (1)(a) near end substituted "30-2-403, 30-2A-304(2), 30-2A-305(2), or 30-9A-320" for "this code (30-2-403 and 30-9A-320)"; in (2) substituted "30-7-504" for "the next section"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

1999 Amendment: Chapter 305 near end of (1)(a) substituted "30-9-340" (renumbered 30-9A-320) for "30-9-307"; and made minor changes in style. Amendment effective July 1, 2001.

30-7-504. Rights acquired in the absence of due negotiation — effect of diversion — stoppage of delivery.

Official Comment

[*Corresponding U.C.C. Section:* Section 7-504, U.C.C.]

Prior Uniform Statutory Provision: Former Section 7-504.

Changes: To include cross-references to Article 2A [Title 30, chapter 2A] and for style.

Purposes:

1. Under the general principles controlling negotiable documents, it is clear that in the absence of due negotiation a transferor cannot convey greater rights than the transferor has, even when the negotiation is formally perfect. This section recognizes the transferor's power to transfer rights which the transferor has or has "actual authority to convey." Thus, where a negotiable document of title is being transferred the operation of the principle of estoppel is not recognized, as contrasted with situations involving the transfer of the goods themselves. (Compare Section 2-403 [30-2-403] on good faith purchase of goods.) This section applies to both tangible and electronic documents of title.

A necessary part of the price for the protection of regular dealings with negotiable documents of title is an insistence that no dealing which is in any way irregular shall be recognized as a good faith purchase of the document or of any rights pertaining to it. So, where the transfer of a negotiable document fails as a negotiation because a requisite indorsement is forged or otherwise missing, the purchaser in good faith and for value may be in the anomalous position of having less rights, in part, than if the purchaser had purchased the goods themselves. True, the purchaser's rights are not subject to defeat by attachment of the goods or surrender of them to the purchaser's transferor (contrast subsection (b) [subsection (2)]); but on the other hand, the purchaser cannot acquire enforceable rights to control or receive the goods over the bailee's objection merely by giving notice to the bailee. Similarly, a consignee who makes payment to its consignor against a straight bill of lading can thereby acquire the position of a good faith purchaser of goods under provisions of the Article of this Act on Sales (Section 2-403) [30-2-403], whereas the same payment made in good faith against an unendorsed order bill would not have such effect. The appropriate remedy of a purchaser in such a situation is to regularize its status by compelling indorsement of the document (see Section 7-506) [30-7-506].

2. As in the case of transfer—as opposed to "due negotiation"—of negotiable documents, subsection (a) [subsection (1)] empowers the transferor of a nonnegotiable document to transfer only such rights as the transferor has or has "actual authority" to convey. In contrast to situations involving the goods themselves the operation of estoppel or agency principles is not here recognized to enable the transferor to convey greater rights than the transferor actually has. Subsection (b) [subsection (2)] makes it clear, however, that the transferee of a nonnegotiable document may acquire rights greater in some respects than those of his transferor by giving notice of the transfer to the bailee. New subsection (b)(3) [not adopted] provides for the rights of a lessee in the ordinary course.

3. Subsection (c) [subsection (3)] is in part a reiteration of the carrier's immunity from liability if it honors instructions of the consignor to divert, but there is added a provision protecting the title of the substituted consignee if the latter is a buyer in ordinary course of business. A typical situation would be where a manufacturer, having shipped a lot of standardized goods to A on nonnegotiable bill of lading, diverts the goods to customer B who pays for them. Under pre-Code passage-of-title-by-appropriation doctrine A might reclaim the goods from B. However, no consideration of commercial policy supports this involvement of an innocent third party in the default of the manufacturer on his contract to A; and the common commercial practice of diverting goods in transit suggests a trade understanding in accordance with this subsection. The same result should obtain if the substituted consignee is a lessee in ordinary course. The

extent of the lessee's interest in the goods is less than a buyer's interest in the goods. However, as against the first consignee and the lessee in ordinary course as the substituted consignee, the lessee's rights in the goods as granted under the lease are superior to the first consignee's rights.

4. Subsection (d) [subsection (4)] gives the carrier an express right to indemnity where the carrier honors a seller's request to stop delivery.

5. Section 1-202 [30-1-210] gives the bailee protection, if due diligence is exercised where the bailee's organization has not had time to act on a notification.

Compiler's Comments

2005 Amendment: Chapter 575 in catchline after "diversion —" deleted "seller's"; in (1) and (2) after "document" inserted "of title"; in (2)(a) inserted "or 30-2A-308"; in (3) near end inserted "or a lessee in ordinary course of business"; in (4) after "Delivery" inserted "of goods" and near middle inserted "or a lessor under 30-2A-526"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-7-505. Endorser not a guarantor for other parties.

Official Comment

[*Corresponding U.C.C. Section:* Section 7-505, U.C.C.]

Prior Uniform Statutory Provision: Former Section 7-505.

Changes: Limited to tangible documents of title.

Purposes:

This section is limited to tangible documents of title as the concept of indorsement is irrelevant to electronic documents of title. Electronic documents of title will be transferred by delivery of control. Section 7-106 [30-7-107]. The indorsement of a tangible document of title is generally understood to be directed towards perfecting the transferee's rights rather than towards assuming additional obligations. The language of the present section, however, does not preclude the one case in which an indorsement given for value guarantees future action, namely, that in which the bailee has not yet become liable upon the document at the time of the indorsement. Under such circumstances the indorser, of course, engages that appropriate honor of the document by the bailee will occur. See Section 7-502(a)(4) [30-7-502(1)(d)] as to negotiable delivery orders. However, even in such a case, once the bailee attorns to the transferee, the indorser's obligation has been fulfilled and the policy of this section excludes any continuing obligation on the part of the indorser for the bailee's ultimate actual performance.

30-7-506. Delivery without endorsement — right to compel endorsement.

Official Comment

[*Corresponding U.C.C. Section:* Section 7-506, U.C.C.]

Prior Uniform Statutory Provision: Former Section 7-506.

Changes: Limited to tangible documents of title.

Purposes:

1. This section is limited to tangible documents of title as the concept of indorsement is irrelevant to electronic documents of title. Electronic documents of title will be transferred by delivery of control. Section 7-106 [30-7-107]. From a commercial point of view the intention to transfer a tangible negotiable document of title which requires an indorsement for its transfer, is incompatible with an intention to withhold such indorsement and so defeat the effective use of the document. Further, the preceding section and the Comment thereto make it clear that an indorsement generally imposes no responsibility on the indorser.

2. Although this section provides that delivery of a tangible document of title without the necessary indorsement is effective as a transfer, the transferee, of course, has not regularized its position until such indorsement is supplied. Until this is done the transferee cannot claim rights under due negotiation within the requirements of this Article (Section 7-501(a)(5)) [30-7-501(1)(e)] on "due negotiation". Similarly, despite the transfer to the transferee of the transferor's title, the

transferee cannot demand the goods from the bailee until the negotiation has been completed and the document is in proper form for surrender. See Section 7-403(c) [30-7-403(3)].

Compiler's Comments

2005 Amendment: Chapter 575 near middle substituted "its" for "his". Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-7-507. Warranties on negotiation or delivery of document of title.

Official Comment

[*Corresponding U.C.C. Section:* Section 7-507, U.C.C.]

Prior Uniform Statutory Provision: Former Section 7-507.

Changes: Substitution of the word "delivery" for the word "transfer," reference leasing transactions and style.

Purposes:

1. Delivery of goods by use of a document of title does not limit or displace the ordinary obligations of a seller or lessor as to any warranties regarding the goods that arises under other law. If the transfer of documents attends or follows the making of a contract for the sale or lease of goods, the general obligations on warranties as to the goods (Sections 2-312 through 2-318 and Sections 2A-210 through 2A-316[sic]) [30-2-312 through 30-2-318 and 30-2A-210 through 30-2A-216] are brought to bear as well as the special warranties under this section.

2. The limited warranties of a delivering or collecting intermediary, including a collecting bank, are stated in Section 7-508 [30-7-508].

Compiler's Comments

2005 Amendment: Chapter 575 in catchline substituted "delivery of document of title" for "transfer of receipt or bill"; in introductory clause substituted "delivers" for "transfers", substituted "30-7-508" for "the next following section", and near end after "selling" inserted "or leasing"; in (3) substituted "delivery" for "transfer"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-7-508. Warranties of collecting bank as to documents of title.

Official Comment

[*Corresponding U.C.C. Section:* Section 7-508, U.C.C.]

Prior Uniform Statutory Provision: Former Section 7-508.

Changes: Changes for style only.

Purposes:

1. To state the limited warranties given with respect to the documents accompanying a documentary draft.

2. In warranting its authority a collecting bank or other intermediary only warrants its authority from its transferor. See Section 4-203 [30-4-203]. It does not warrant the genuineness or effectiveness of the document. Compare Section 7-507 [30-7-507].

3. Other duties and rights of banks handling documentary drafts for collection are stated in Article 4, Part 5 [Title 30, chapter 4, part 5]. On the meaning of draft, see Section 4-104 [30-4-104] and Section 5-102 [30-5-122], comment 11.

Compiler's Comments

2005 Amendment: Chapter 575 in catchline inserted "of title"; near beginning after "with documents" inserted "of title" and near end substituted "even if the collecting bank or other" for "This rule applies even though the"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-7-509. Adequate compliance with commercial contract.

Official Comment

[*Corresponding U.C.C. Section:* Section 7-509, U.C.C.]

Prior Uniform Statutory Provision: Former Section 7-509.

Changes: To reference Article 2A [Title 30, chapter 2A].

Purposes:

To cross-refer to the Articles of this Act [Title 30, chapters 2, 2A, and 5] which deal with the substantive issues of the type of document of title required under the contract entered into by the parties.

Compiler's Comments

2005 Amendment: Chapter 575 in catchline at beginning deleted "Receipt or bill — when"; near middle inserted "a contract for lease" and at end substituted "by chapter 2, 2A, or 5" for "by the Chapters on Sales (Chapter 2) and on Letters of Credit (Chapter 5)"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

Part 6

Warehouse Receipts and Bills of Lading Miscellaneous Provisions

30-7-601. Lost and missing documents.

Official Comment

[*Corresponding U.C.C. Section:* Section 7-601, U.C.C.]

Prior Uniform Statutory Provision: Former Section 7-601.

Changes: To accommodate electronic documents; to provide flexibility to courts similar to the flexibility in Section 3-309 [30-3-309]; to update to the modern era of deregulation; and for style.

Purposes:

1. Subsection (a) [subsection (1)] authorizes courts to order compulsory delivery of the goods or compulsory issuance of a substitute document. Compare Section 7-402 [30-7-402]. Using language similar to that found in Section 3-309 [30-3-309], courts are given discretion as to what is adequate protection when the lost, stolen or destroyed document was negotiable or whether security should be required when the lost, stolen or destroyed document was nonnegotiable. In determining whether a party is adequately protected against loss in the case of a negotiable document, the court should consider the likelihood that the party will suffer a loss. The court is also given discretion as to the bailee's costs and attorney fees. The rights and obligations of a bailee under this section depend upon whether the document of title is lost, stolen or destroyed and is in addition to the ability of the bailee to bring an action for interpleader. See Section 7-603 [30-7-603].

2. Courts have the authority under this section to order a substitute document for either tangible or electronic documents. If the substitute document will be in a different medium than the original document, the court should fashion its order in light of the requirements of Section 7-105 [30-7-106].

3. Subsection (b) [subsection (2)] follows prior Section 7-601 [30-7-601] in recognizing the legality of the well established commercial practice of bailees making delivery in good faith when they are satisfied that the claimant is the person entitled under a missing (i.e. lost, stolen, or destroyed) negotiable document. Acting without a court order, the bailee remains liable on the original negotiable document and, to avoid conversion liability, the bailee may insist that the claimant provide an indemnity bond. Cf. Section 7-403 [30-7-403].

4. Claimants on non-negotiable instruments are permitted to avail themselves of the subsection (a) [subsection (1)] procedure because straight (non-negotiable) bills of lading sometimes contain provisions that the goods shall not be delivered except upon production of the bill. If the carrier should choose to insist upon production of the bill, the consignee should have some means of compelling delivery on satisfactory proof of entitlement. Without a court order, a bailee may deliver, subject to Section 7-403 [30-7-403], to a person claiming goods under a non-negotiable document that the same person claims is lost, stolen, or destroyed.

5. The bailee's lien should be protected when a court orders delivery of the goods pursuant to this section.

Compiler's Comments

2005 Amendment: Chapter 575 in (1) in second sentence substituted "a court may not order delivery of the goods or issuance of a substitute document without the claimant's posting security unless it finds that" for "the claimant must post security approved by the court to indemnify", near end inserted possession or control of", and at end inserted "is adequately protected against the loss", in third sentence substituted "nonnegotiable, the court may require" for "negotiable, such" and at end deleted "may be required at the discretion of the court", and in fourth sentence after "also" deleted "in its discretion" and at end substituted "attorney's fees in any action under this subsection" for "counsel fees"; in (2) in first sentence after "document" inserted "of title", in second sentence substituted "the bailee is" for "becomes", and in third sentence after "conversion" deleted "if made in accordance with a filed classification or tariff or, where no classification or tariff is filed"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-7-602. Attachment of goods covered by negotiable document of title.

Official Comment

[*Corresponding U.C.C. Section:* Section 7-602, U.C.C.]

Prior Uniform Statutory Provisions: Former Section 7-602.

Changes: Changes to accommodate electronic documents of title and for style.

Purposes:

1. The purpose of the section is to protect the bailee from conflicting claims of the document of title holder and the judgment creditors of the person who deposited the goods. The rights of the former prevail unless, in effect, the judgment creditors immobilize the negotiable document of title through the surrender of possession of a tangible document or control of an electronic document. However, if the document of title was issued upon deposit of the goods by a person who had no power to dispose of the goods so that the document is ineffective to pass title, judgment liens are valid to the extent of the debtor's interest in the goods.

2. The last sentence covers the possibility that the holder of a document who has been enjoined from negotiating it will violate the injunction by negotiating to an innocent purchaser for value. In such case the lien will be defeated.

Compiler's Comments

2005 Amendment: Chapter 575 in catchline at end inserted "of title"; in (1) in first sentence at beginning after "document" inserted "of title" and near middle inserted "possession or control of" and in second sentence near middle inserted "possession or control of" and after "the bailee or" deleted "impounded by"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-7-603. Conflicting claims — interpleader.

Official Comment

[*Corresponding U.C.C. Section:* Section 7-603, U.C.C.]

Prior Uniform Statutory Provisions: Former Section 7-603.

Changes: Changes for style only.

Purposes:

1. The section enables a bailee faced with conflicting claims to the goods to compel the claimants to litigate their claims with each other rather than with the bailee. The bailee is protected from legal liability when the bailee complies with court orders from the interpleader. *See e.g.* Northwestern National Sales, Inc. v. Commercial Cold Storage, Inc., 162 Ga.App. 741, 293 S.E.2d. 30 (1982).

2. This section allows the bailee to bring an interpleader action but does not provide an exclusive basis for allowing interpleader. If either state or federal procedural rules allow an interpleader in other situations, the bailee may commence an interpleader under those rules. Even in an interpleader to which this section applies, the state or federal process of interpleader applies to the bailee's action for interpleader. For example, state or federal interpleader statutes or rules may permit a bailee to protect its lien or to seek attorney's fees and costs in the interpleader action.

Compiler's Comments

2005 Amendment: Chapter 575 at end of first sentence substituted "commence an action for" for "bring an action to compel all claimants to interplead and may compel such" and at beginning of second sentence inserted "The bailee may assert an interpleader"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

Case Notes

DECISIONS UNDER UNIFORM WAREHOUSE RECEIPTS ACT

Affirmative Relief on All Issues: Elevator company seeking interpleader of various parties under section 88-117, R.C.M. 1947 (now repealed), and not under general interpleader statute, to determine ownership of quantity of grain held in storage, did not defeat its right to maintain suit by way of payment of storage charges and cancellation of storage tickets erroneously issued to the grower by way of affirmative relief, as section 88-117, R.C.M. 1947 (now repealed), contemplates that all issues between the parties should be settled. Rocky Mtn. Elev. Co. v. Bammel, 106 M 407, 81 P2d 673 (1938).

Allowance of Costs to Plaintiff: Trial court in ordering that the elevator company in an action in interpleader under section 88-117, R.C.M. 1947 (now repealed), not responsible for the litigation, should be awarded its costs of suit and that each of the defendants should pay his own costs, properly exercised its discretion under 25-10-103. Rocky Mtn. Elev. Co. v. Bammel, 106 M 407, 81 P2d 673 (1938).

Marshaling of Assets: Where vendor of farm lands, in an action in interpleader by the elevator company under section 88-117, R.C.M. 1947 (now repealed), was awarded the amount claimed by him, he was in no position to urge on appeal that the District Court erred in not ordering a marshaling of the purchaser's assets because purchaser was indebted to another defendant under a mortgage when such defendant was not complaining. After vendor received all he was entitled to, he was no longer interested in what disposition the purchaser made of his share of the grain. Rocky Mtn. Elev. Co. v. Bammel, 106 M 407, 81 P2d 673 (1938).

CHAPTER 8
UNIFORM COMMERCIAL CODE INVESTMENT SECURITIES

Chapter Official Comment

Reporter's Prefatory Note to 1997 Revision:

The present version of Article 8 [Title 30, chapter 8] is the product of a major revision made necessary by the fact that the prior version of Article 8 [Title 30, chapter 8] did not adequately deal with the system of securities holding through securities intermediaries that has developed in the past few decades. Although the prior version of Article 8 [Title 30, chapter 8] did contain some provisions dealing with securities holding through securities intermediaries, these were engrafted onto a structure designed for securities practices of earlier times. The resulting legal uncertainties adversely affected all participants. The revision is intended to eliminate these uncertainties by providing a modern legal structure for current securities holding practices.

I. EVOLUTION OF SECURITIES HOLDING SYSTEMS

A. The Traditional Securities Holding System

The original version of Article 8 [Title 30, chapter 8], drafted in the 1940s and 1950s, was based on the assumption that possession and delivery of physical certificates are the key elements in the securities holding system. Ownership of securities was traditionally evidenced by possession of the certificates, and changes were accomplished by delivery of the certificates.

Transfer of securities in the traditional certificate-based system was a complicated, labor-intensive process. Each time securities were traded, the physical certificates had to be delivered from the seller to the buyer, and in the case of registered securities the certificates had to be surrendered to the issuer or its transfer agent for registration of transfer. As is well known, the mechanical problems of processing the paperwork for securities transfers reached crisis proportions in the late 1960s, leading to calls for the elimination of the physical certificate and development of modern electronic systems for recording ownership of securities and transfers of ownership. That was the focus of the revision effort that led to the promulgation of the 1978 amendments to Article 8 [Title 30, chapter 8] concerning uncertificated securities.

B. The Uncertificated Securities System Envisioned by the 1978 Amendments

In 1978, amendments to Article 8 [Title 30, chapter 8] were approved to establish the commercial law rules that were thought necessary to permit the evolution of a system in which issuers would no longer issue certificates. The Drafting Committee that produced the 1978 amendments was given a fairly limited charge. It was to draft the revisions that would be needed for uncertificated securities, but otherwise leave the Article 8 [Title 30, chapter 8] rules unchanged. Accordingly, the 1978 amendments primarily took the form of adding parallel provisions dealing with uncertificated securities to the existing rules of Article 8 [Title 30, chapter 8] on certificated securities.

The system of securities holding contemplated by the 1978 amendments differed from the traditional system only in that ownership of securities would not be evidenced by physical certificates. It was contemplated that changes in ownership would continue to be reflected by changes in the records of the issuer. The main difference would be that instead of surrendering an indorsed certificate for registration of transfer, an instruction would be sent to the issuer directing it to register the transfer. Although a system of the sort contemplated by the 1978 amendments may well develop in the coming decades, this has not yet happened for most categories of securities. Mutual funds shares have long been issued in uncertificated form, but virtually all other forms of publicly traded corporate securities are still issued in certificated form. Individual investors who wish to be recorded as registered owners on the issuers' books still obtain and hold physical certificates. The certificates representing the largest portion of the shares of publicly traded companies, however, are not held by the beneficial owners, but by clearing corporations.

Settlement of securities trading occurs not by delivery of certificates or by registration of transfer on the records of the issuers or their transfer agents, but by computer entries in the records of clearing corporations and securities intermediaries. That is quite different from the system envisioned by the 1978 amendments.

C. Evolution of the Indirect Holding System

At the time of the "paperwork crunch" in the late 1960s, the trading volume on the New York Stock Exchange that so seriously strained the capacities of the clearance and settlement system was in the range of 10 million shares per day. Today, the system can easily handle trading volume on routine days of hundreds of millions of shares. This processing capacity could have been achieved only by the application of modern electronic information processing systems. Yet the legal rules under which the system operates are *not* the uncertificated securities provisions of Article 8 [Title 30, chapter 8]. To understand why this is so, one must delve at least a bit deeper into the operations of the current system.

If one examines the shareholder records of large corporations whose shares are publicly traded on the exchanges or in the over the counter market, one would find that one entity—Cede & Co.—is listed as the shareholder of record of somewhere in the range of sixty to eighty per cent of the outstanding shares of all publicly traded companies. Cede & Co. is the nominee name used by The Depository Trust Company ("DTC"), a limited purpose trust company organized under New York law for the purpose of acting as a depository to hold securities for the benefit of its participants, some 600 or so broker-dealers and banks. Essentially all of the trading in publicly held companies is executed through the broker-dealers who are participants in DTC, and the great bulk of public securities—the sixty to eighty per cent figure noted above—are held by these broker-dealers and banks on behalf of their customers. If all of these broker-dealers and banks held physical certificates, then as trades were executed each day it would be necessary to deliver the certificates back and forth among these broker-dealers and banks. By handing all of their securities over to a common depository all of these deliveries can be eliminated. Transfers can be accomplished by adjustments to the participants' DTC accounts.

Although the use of a common depository eliminates the needs for physical deliveries, an enormous number of entries would still have to be made on DTC's books if each transaction between its participants were recorded one by one on DTC's books. Any two major broker-dealers may have executed numerous trades with each other in a given security on a single day. Significant processing efficiency has been achieved by netting all of the transactions among the participants that occur each day, so that entries need be made on the depository's books only for the net changes in the positions of each participant at the end of each day. This clearance and netting function might well be performed by the securities exchanges or by the same institution that acts as the depository, as is the case in many other securities markets around the world. In the United States, however, this clearance and netting function is carried out by a separate corporation, National Securities Clearing Corporation ("NSCC"). All that needs to be done to settle each day's trading is for NSCC to compute the net receive and deliver obligations and to instruct DTC to make the corresponding adjustments in the participants' accounts.

The broker-dealers and banks who are participants in the DTCNSCC system in turn provide analogous clearance and settlement functions to their own customers. If Customer A buys 100 shares of XYZ Co. through Broker, and Customer B sells 100 shares of XYZ Co. through the same Broker, the trade can be settled by entries on Broker's books. Neither DTC's books showing Broker's total position in XYZ Co., nor XYZ Co.'s books showing DTC's total position in XYZ Co., need be changed to reflect the settlement of this trade. One can readily appreciate the significance of the settlement function performed at this level if one considers that a single major bank may be acting as securities custodian for hundreds or thousands of mutual funds, pension funds, and other institutional investors. On any given day, the customers of that bank may have entered into an enormous number of trades, yet it is possible that relatively little of this trading activity will result in any net change in the custodian bank's positions on the books of DTC.

Settlement of market trading in most of the major U.S. securities markets is now effected primarily through some form of netted clearance and depository system. Virtually all publicly traded corporate equity securities, corporate debt securities, and municipal debt securities are now eligible for deposit in the DTC system. Recently, DTC has implemented a similar depository settlement system for the commercial paper market, and could, but for limitations in present Article 8 [Title 30, chapter 8], handle other forms of short-term money market securities such as bankers' acceptances. For trading in mortgage-backed securities, such as Ginnie Mae's, a similar depository settlement system has been developed by Participants Trust Company. For trading in

U.S. Treasury securities, a somewhat analogous book-entry system is operated under Treasury rules by the Federal Reserve System.

D. Need for Different Legal Rules for the Direct and Indirect Holding Systems

Both the traditional paper-based system, and the uncertificated system contemplated by the 1978 amendments, can be described as "direct" securities holding systems; that is, the beneficial owners of securities have a direct relationship with the issuer of the securities. For securities in bearer form, whoever has possession of the certificate thereby has a direct claim against the issuer. For registered securities, the registered owner, whether of certificated or uncertificated securities, has a direct relationship with the issuer by virtue of being recorded as the owner on the records maintained by the issuer or its transfer agent.

By contrast, the DTC depository system for corporate equity and debt securities can be described as an "indirect holding" system, that is, the issuer's records do not show the identity of all of the beneficial owners. Instead, a large portion of the outstanding securities of any given issue are recorded on the issuer's records as belonging to a depository. The depository's records in turn show the identity of the banks or brokers who are its members, and the records of those securities intermediaries show the identity of their customers.

Even after the 1978 amendments, the rules of Article 8 [Title 30, chapter 8] did not deal effectively with the indirect holding system. The rules of the 1978 version of Article 8 [Title 30, chapter 8] were based on the assumption that changes in ownership of securities would still be effected either by delivery of physical certificates or by registration of transfer on the books of the issuer. Yet in the indirect holding system, settlement of the vast majority of securities trades does not involve either of these events. For most, if not all, of the securities held through DTC, physical certificates representing DTC's total position do exist. These "jumbo certificates," however, are never delivered from person to person. Just as nothing ever happens to these certificates, virtually nothing happens to the official registry of stockholders maintained by the issuers or their transfer agents to reflect the great bulk of the changes in ownership of shares that occur each day.

The principal mechanism through which securities trades are settled today is not delivery of certificates or registration of transfers on the issuer's books, but netted settlement arrangements and accounting entries on the books of a multi-tiered pyramid of securities intermediaries. Herein is the basic problem. Virtually all of the rules of the prior version of Article 8 [Title 30, chapter 8] specifying how changes in ownership of securities are effected, and what happens if something goes awry in the process, were keyed to the concepts of a transfer of physical certificates or registration of transfers on the books of the issuers, yet that is not how changes in ownership are actually reflected in the modern securities holding system.

II. BRIEF OVERVIEW OF REVISED ARTICLE 8 [TITLE 30, CHAPTER 8]

A. Drafting Approach—Neutrality Principle

One of the objectives of the revision of Article 8 [Title 30, chapter 8] is to devise a structure of commercial law rules for investment securities that will be sufficiently flexible to respond to changes in practice over the next few decades. If it were possible to predict with confidence how the securities holding and trading system would develop, one could produce a statute designed specifically for the system envisioned. Recent experience, however, shows the danger of that approach. The 1978 amendments to Article 8 [Title 30, chapter 8] were based on the assumption that the solution to the problems that plagued the paper-based securities trading system of the 1960s would be the development of uncertificated securities. Instead, the solution thus far has been the development of the indirect holding system.

If one thought that the indirect holding system would come to dominate securities holding, one might draft Article 8 [Title 30, chapter 8] rules designed primarily for the indirect holding system, giving limited attention to the traditional direct holding system of security certificates or any uncertificated version of a direct holding system that might develop in the future. It is, however, by no means clear whether the long-term evolution will be toward decreased or increased use of direct holdings. At present, investors in most equity securities can either hold their securities through brokers or request that certificates be issued in their own name. For the immediate future it seems likely that that situation will continue. One can imagine many plausible scenarios for future evolution. Direct holding might become less and less common as investors become more familiar and comfortable with book-entry systems and/or as market or regulatory pressures develop that discourage direct holding. One might note, for example, that major brokerage firms are beginning to impose fees for having certificates issued and that some observers have suggested that acceleration of the cycle for settlement of securities trades might be facilitated by discouraging customers from obtaining certificates. On the other hand, other observers feel that it is important for investors to retain the option of holding securities in certificated form, or at least in some form that gives them a direct relationship with the issuer and does not require them to hold through brokers or other securities intermediaries. Some groups within the securities industry are beginning to work on development of uncertificated systems that would preserve this option.

Revised Article 8 [Title 30, chapter 8] takes a neutral position on the evolution of securities holding practices. The revision was based on the assumption that the path of development will be determined by market and regulatory forces and that the Article 8 [Title 30, chapter 8] rules should not seek to influence that development in any specific direction. Although various drafting approaches were considered, it became apparent early in the revision process that the differences between the direct holding system and the indirect holding system are sufficiently significant that it is best to treat them as separate systems requiring different legal concepts. Accordingly, while the rules of the prior version of Article 8 [Title 30, chapter 8] have, in large measure, been retained for the direct holding system, a new Part 5 [Title 30, chapter 8, part 5] has been added, setting out the commercial law rules for the indirect securities holding system. The principle of neutrality does carry some implications for the design of specific Article 8 [Title 30, chapter 8] rules. At the very least, the Article 8 [Title 30, chapter 8] rules for all securities holding systems should be sufficiently clear and predictable that uncertainty about the governing law does not itself operate as a constraint on market developments. In addition, an effort has been made to identify and eliminate any Article 8 [Title 30, chapter 8] rules that might act as impediments to any of the foreseeable paths of development.

B. Direct Holding System

With respect to securities held directly, Revised Article 8 [Title 30, chapter 8] retains the basic conceptual structure and rules of present law. Part 2 [Title 30, chapter 8, part 2], which is largely unchanged from former law, deals with certain aspects of the obligations of issuers. The primary purpose of the rules of Part 2 [Title 30, chapter 8, part 2] is to apply to investment securities the principles of negotiable instruments law that preclude the issuers of negotiable instruments from asserting defenses against subsequent purchasers. Part 3 [Title 30, chapter 8, part 3] deals with transfer for securities held directly. One of its principal purposes is to apply to investment securities the principles of negotiable instruments law that protect purchasers of negotiable instruments against adverse claims. Part 4 [Title 30, chapter 8, part 4] deals with the process of registration of transfer by the issuer or transfer agent.

Although the basic concepts of the direct holding system rules have been retained, there are significant changes in terminology, organization, and statement of the rules. Some of the major changes are as follows:

Simplification of Part 3 [Title 30, chapter 8, part 3]. The addition of the new Part 5 [Title 30, chapter 8, part 5] on the indirect holding system makes unnecessary the rather elaborate provisions of former law, such as those in Section 8-313 [former 30-8-313], that sought to fit the indirect holding system into the conceptual structure of the direct holding system. Thus, Part 3 of Revised Article 8 [Title 30, chapter 8, part 3] is, in many respects, more similar to the original version of Article 8 [Title 30, chapter 8] than to the 1978 version.

Protected purchaser. The prior version of Article 8 [Title 30, chapter 8] used the term "bona fide purchaser" to refer to those purchasers who took free from adverse claims, and it used the phrase "good faith" in stating the requirements for such status. In order to promote clarity, Revised Article 8 [Title 30, chapter 8] states the rules that protect purchasers against adverse claims without using the phrase "good faith" and uses the new term "protected purchaser" to refer to purchasers in the direct holding system who are protected against adverse claims. See Sections 8-105 and 8-303 [30-8-115 and 30-8-333].

Certificated versus uncertificated securities. The rules of the 1978 version of Article 8 [Title 30, chapter 8] concerning uncertificated securities have been simplified considerably. The 1978 version added provisions on uncertificated securities parallel to the provisions of the original version of Article 8 [Title 30, chapter 8] dealing with securities represented by certificates. Thus, virtually every section had one set of rules on "certificated securities" and another on "uncertificated securities." The constant juxtaposition of "certificated securities" and "uncertificated securities" has probably led readers to overemphasize the differences. Revised Article 8 [Title 30, chapter 8] has a unitary definition of "security" in Section 8-102(a)(15) [30-8-112(1)(o)] which refers to the underlying intangible interest or obligation. In Revised

Article 8 [Title 30, chapter 8], the difference between certificated and uncertificated is treated not as an inherent attribute of the security but as a difference in the means by which ownership is evidenced. The terms "certificated" and "uncertificated" security are used in those sections where it is important to distinguish between these two means of evidencing ownership. Revised Article 8 [Title 30, chapter 8] also deletes the provisions of the 1978 version concerning "transaction statements" and "registered pledges." These changes are explained in the Revision Notes 3, 4, and 5, below.

Scope of Parts 2, 3, and 4 [Title 30, chapter 8, parts 2, 3, and 4]. The rules of Parts 2, 3, and 4 [Title 30, chapter 8, parts 2, 3, and 4] deal only with the rights of persons who hold securities directly. In typical securities holding arrangements in the modern depository system, only the clearing corporation would be a direct holder of the securities. Thus, while the rules of Parts 2, 3, and 4 [Title 30, chapter 8, parts 2, 3, and 4] would apply to the relationship between the issuer and the clearing corporation, they have no application to relationships below the clearing corporation level. Under Revised Article 8 [Title 30, chapter 8], a person who holds a security through a broker or securities custodian has a security entitlement governed by the Part 5 [Title 30, chapter 8, part 5] rules but is not the direct holder of the security. Thus, the rules of Revised Section 8-303 [30-8-333] on the rights of "protected purchasers," which are the analog of the bona fide purchaser rules of former Article 8 [Title 30, chapter 8], do not apply to persons who hold securities through brokers or securities custodians. Instead, Part 5 [Title 30, chapter 8, part 5] contains its own rules to protect investors in the indirect holding system against adverse claims. See Revised Section 8-502 [30-8-502].

C. Indirect Holding System

Although the Revised Article 8 [Title 30, chapter 8] provisions for the indirect holding system are somewhat complex, the basic approach taken can be summarized rather briefly. Revised Article 8 [Title 30, chapter 8] abandons the attempt to describe all of the complex relationships in the indirect holding system using the simple concepts of the traditional direct holding system. Instead, new rules specifically designed for the indirect holding system are added as Part 5 of Article 8 [Title 30, chapter 8, part 5]. In a nutshell, the approach is to describe the core of the package of rights of a person who holds a security through a securities intermediary and then give that package of rights a name.

The starting point of Revised Article 8's [Title 30, chapter 8] treatment of the indirect holding system is the concept of "security entitlement." The term is defined in Section 8-102(a)(17) [30-8-112(1)(q)] as "the rights and property interest of an entitlement holder with respect to a financial asset specified in Part 5 [Title 30, chapter 8, part 5]." Like many legal concepts, however, the meaning of "security entitlement" is to be found less in any specific definition than in the matrix of rules that use the term. In a sense, then, the entirety of Part 5 [Title 30, chapter 8, part 5] is the definition of "security entitlement" because the Part 5 [Title 30, chapter 8, part 5] rules specify the rights and property interest that comprise a security entitlement.

Part 5 [Title 30, chapter 8, part 5] begins by specifying, in Section 8-501 [30-8-501], when an entitlement holder acquires a security entitlement. The basic rule is very simple. A person acquires a security entitlement when the securities intermediary credits the financial asset to the person's account. The remaining sections of Part 5 [Title 30, chapter 8, part 5] specify the content of the security entitlement concept. Section 8-504 [30-8-504] provides that a securities intermediary must maintain a sufficient quantity of financial assets to satisfy the claims of all of its entitlement holders. Section 8-503 [30-8-503] provides that these financial assets are held by the intermediary for the entitlement holders, are not the property of the securities intermediary, and are not subject to claims of the intermediary's general creditors. Thus, a security entitlement is itself a form of property interest not merely an *in personam* claim against the intermediary. The concept of a security entitlement does, however, include a package of *in personam* rights against the intermediary. Other Part 5 [Title 30, chapter 8, part 5] rules identify the core of this package of rights, subject to specification by agreement and regulatory law. See Sections 8-505 through 8-509 [30-8-505 through 30-8-509].

To illustrate the basic features of the new rules, consider a simple example of two investors, John and Mary, each of whom owns 1000 shares of Acme, Inc., a publicly traded company. John has a certificate representing his 1000 shares and is registered on the books maintained by Acme's transfer agent as the holder of record of those 1000 shares. Accordingly, he has a direct claim against the issuer, he receives dividends and distributions directly from the issuer, and he receives proxies directly from the issuer for purposes of voting his shares. Mary has chosen to hold her securities through her broker. She does not have a certificate and is not registered on Acme's stock books as a holder of record. She enjoys the economic and corporate benefits of ownership but does so through her broker and any other intermediaries in the chain back to the issuer. John's interest in Acme common stock would be described under Revised Article 8 [Title 30, chapter 8] as a direct interest in a "security." Thus, if John grants a security interest in his investment position, the collateral would be described as a "security." Mary's interest in Acme common stock would be described under Revised Article 8 [Title 30, chapter 8] as a "security entitlement." Thus, if Mary grants a security interest in her investment position, the collateral would be described as a "security entitlement."

For many purposes, there is no need to differentiate among the various ways that an investor might hold securities. For example, for purposes of financial accounting, John and Mary would each be described as the owner of 1000 shares of Acme common stock. For those purposes it is irrelevant that John is the registered owner and has physical possession of a certificate, while Mary holds her position through an intermediary. Revised Article 8 [Title 30, chapter 8] recognizes this point in Section 8-104 [30-8-114] which provides that acquiring a security entitlement and acquiring a security certificate are different ways of acquiring an interest in the underlying security.

D. Security Interests

Along with the revision of Article 8 [Title 30, chapter 8], significant changes have been made in the rules concerning security interests in securities. The revision returns to the pre1978 structure in which the rules on security interests in investment securities are set out in Article 9 [Title 30, chapter 9A], rather than in Article 8 [Title 30, chapter 8]. The changes in Article 9 [Title 30, chapter 9A] are, in part, conforming changes to adapt Article 9 [Title 30, chapter 9A] to the new concept of a security entitlement. The Article 9 [Title 30, chapter 9A] changes, however, go beyond that to establish a simplified structure for the creation and perfection of security interests in investment securities, whether held directly or indirectly. In order to avoid disruption of the current numbering sequence of Article 9 [Title 30, chapter 9A], the new rules on security interests in investment securities are primarily set out in a new Section 9-115 [30-9-115, now repealed, see 30-9A-106, 30-9A-203, 30-9A-308, 30-9A-309, 30-9A-313, 30-9A-314, and 30-9A-328].

The Revised Article 9 [Title 30, chapter 9A] rules continue the long-established principle that a security interest in a security represented by a certificate can be perfected by a possessory pledge. The revised rules, however, do not require that all security interests in investment securities be implemented by procedures based on the conceptual structure of the common law pledge. Under the revised Article 9 [Title 30, chapter 9A] rules, a security interest in securities can be created pursuant to Section 9-203 [30-9-203, now repealed, see 30-9A-203] in the same fashion as a security interest in any other form of property, that is, by agreement between the debtor and secured party. There is no requirement of a "transfer," "delivery," or any similar action, physical or metaphysical, for the creation of an effective security interest. A security interest in securities is, of course, a form of property interest, but the only requirements for creation of this form of property interest are those set out in Section 9-203 [30-9-203, now repealed, see 30-9A-203].

The perfection methods for security interests in investment securities are set out in Revised Section 9-115(4) [30-9-115(4), now repealed, see 30-9A-309 and 30-9A-314]. The basic rule is that a security interest may be perfected by "control." The concept of control, defined in Section 8-106 [30-8-116], plays an important role in both Article 8 and Article 9 [Title 30, chapters 8 and 9A]. In general, obtaining control means taking the steps necessary to place the lender in a position where it can have the collateral sold off without the further cooperation of the debtor. Thus, for certificated securities, a lender obtains control by taking possession of the certificate with any necessary indorsement. For securities held through a securities intermediary, the lender can obtain control in two ways. First, the lender obtains control if it becomes the entitlement holder; that is, has the securities positions transferred to an account in its own name. Second, the lender obtains control if the securities intermediary agrees to act on instructions from the secured party to dispose of the positions, even though the debtor remains the entitlement holder. Such an arrangement suffices to give the lender control even though the debtor retains the right to trade and exercise other ordinary rights of an entitlement holder.

Except where the debtor is itself a securities firm, filing of an ordinary Article 9 [Title 30, chapter 9A] financing statement is also a permissible alternative method of perfection. However, filing with respect to investment property does not assure the lender the same protections as for other forms of collateral, since the priority rules provide that a secured party who obtains control has priority over a secured party who does not obtain control.

The details of the new rules on security interests, as applied both to the retail level and to arrangements for secured financing of securities dealers, are explained in the Official Comments to Section 9-115 [30-9-115, now repealed, see 30-9A-106, 30-9A-108, 30-9A-203, 30-9A-308, 30-9A-309, 30-9A-313, 30-9A-314, and 30-9A-327 through 30-9A-329].

III. SCOPE AND APPLICATION OF ARTICLE 8 [TITLE 30, CHAPTER 8]

A. Terminology

To understand the scope and application of the rules of Revised Article 8 [Title 30, chapter 8], and the related security interest rules of Article 9 [Title 30, chapter 9A], it is necessary to understand some of the key defined terms:

Security, defined in Section 8-102(a)(15) [30-8-112(1)(o)], has essentially the same meaning as under the prior version of Article 8 [Title 30, chapter 8]. The difference in Revised Article 8 [Title 30, chapter 8] is that the definition of security does not determine the coverage of all of Article 8 [Title 30, chapter 8]. Although the direct holding system rules in Parts 2, 3, and 4 [Title 30, chapter 8, parts 2, 3, and 4] apply only to securities, the indirect holding system rules of Part 5 [Title 30, chapter 8, part 5] apply to the broader category of "financial assets."

Financial asset, defined in Section 8-103(a)(9) [30-8-113(1)(i)], is the term used to describe the forms of property to which the indirect holding system rules of Part 5 [Title 30, chapter 8, part 5] apply. The term includes not only "securities," but also other interests, obligations, or property that are held through securities accounts. The best illustration of the broader scope of the term financial asset is the treatment of money market instruments, discussed below.

Security entitlement, defined in Section 8-103(a)(17) [sic] [30-8-112(1)(q)], is the term used to describe the property interest of a person who holds a security or other financial asset through a securities intermediary.

Securities intermediary, defined in Section 8-103(a)(14) [sic] [30-8-112(1)(n)], is the term used for those who hold securities for others in the indirect holding system. It covers clearing corporations, banks acting as securities custodians, and brokers holding securities for their customers.

Entitlement holder, defined in Section 8-103(a)(7) [sic] [30-8-112(1)(g)], is the term used for those who hold securities through intermediaries.

Securities account, defined in Section 8-501(a) [30-8-501(1)], describes the form of arrangement between a securities intermediary and an entitlement holder that gives rise to a security entitlement. As explained below, the definition of securities account plays a key role in setting the scope of the indirect holding system rules of Part 5 [Title 30, chapter 8, part 5].

Investment property, defined in Section 9-115(1)(f) [30-9-115(1)(f), now repealed, see 30-9A-106, 30-9A-108, 30-9A-203, 30-9A-308, 30-9A-309, 30-9A-313, 30-9A-314, and 30-9A-327 through 30-9A-329]. determines the application of the new Article 9 [Title 30, chapter 9A] rules for secured transactions. In addition to securities and security entitlements, the Article 9 [Title 30, chapter 9A] term "investment property" is defined to include "securities account" in order to simplify the drafting of the Article 9 [Title 30, chapter 9A] rules that permit debtors to grant security interests either in specific security entitlements or in an entire securities account. The other difference between the coverage of the Article 8 and Article 9 [Title 30, chapters 8 and 9A] terms is that commodity futures contracts are excluded from Article 8 [Title 30, chapter 8], but are included within the Article 9 [Title 30, chapter 9A] definition of "investment property." Thus, the new Article 9 [Title 30, chapter 9A] rules apply to security interests in commodity futures positions as well as security interests in securities positions.

B. Notes on Scope of Article 8 [Title 30, chapter 8]

Article 8 [Title 30, chapter 8] is in no sense a comprehensive codification of the law governing securities or transactions in securities. Although Article 8 [Title 30, chapter 8] deals with some aspects of the rights of securities holders against issuers, most of that relationship is governed not by Article 8 [Title 30, chapter 8] but by corporation, securities, and contract law. Although Article 8 [Title 30, chapter 8] deals with some aspects of the rights and duties of parties who transfer securities, it is not a codification of the law of contracts for the purchase or sale of securities. (The prior version of Article 8 [Title 30, chapter 8] did include a few miscellaneous rules on contracts for the sale of securities, but these have not been included in Revised Article 8 [Title 30, chapter 8]). Although the new indirect holding system rules of Part 5 [Title 30, chapter 8, part 5] deal with some aspects of the relationship between brokers or other securities professionals and their customers, Article 8 [Title 30, chapter 8] is still not in any sense a comprehensive code of the law governing the relationship between broker-dealers or other securities intermediaries and their customers. Most of the law governing that relationship is the common law of contract and agency, supplemented or supplanted by regulatory law.

The distinction between the aspects of the broker-customer relationship that are and are not dealt with in this Article [chapter] may be illuminated by considering the differing roles of the broker in a typical securities transaction, in which the broker acts as agent for the customer. When a customer directs a broker to buy or sell securities for the customer, and the broker executes that trade on a securities exchange or in the over the counter market, the broker is entering into a contract for the purchase or sale of the securities as agent of the customer. The rules of the exchange, practices of the market, or regulatory law will specify when and how that contract is to be performed. For example, today the terms of the standard contract for trades in most corporate securities require the seller to deliver the securities, and the buyer to pay for them, five business days after the date that the contract was made, although the SEC has recently promulgated a rule that will accelerate the cycle to require settlement in three business days. In the common speech of the industry, the transaction in which the broker enters into a contract for the purchase or sale of the securities is referred to as executing the trade, and the transaction in which the securities are delivered and paid for is referred to as settlement. Thus, the current settlement cycle is known as T[plus]5, that is, settlement is required on the fifth business day after the date of the trade, and the new SEC rule will change it to T[plus]3. One must be careful in moving from the jargon of the securities industry to the jargon of the legal profession. For most practical economic purposes, the trade date is the date that counts, because that is the time at which the price is set, the risk of price changes shifts, and the parties become bound to perform. For purposes of precise legal analysis, however, the securities phrase "trade" or "execute a trade" means enter into a contract for the purchase or sale of the securities. The transfer of property interests occurs not at the time the contract is made but at the time it is performed, that is, at settlement.

The distinction between trade and settlement is important in understanding the scope of Article 8 [Title 30, chapter 8]. Article 8 [Title 30, chapter 8] deals with the settlement phase of securities transactions. It deals with the mechanisms by which interests in securities are transferred, and the rights and duties of those who are involved in the transfer process. It does not deal with the process of entering into contracts for the transfer of securities or regulate the rights and duties of those involved in the contracting process. To use securities parlance, Article 8 [Title 30, chapter 8] deals not with the trade, but with settlement of the trade. Indeed, Article 8 [Title 30, chapter 8] does not even deal with all aspects of settlement. In a netted clearance and settlement system such as the NSCCDTC system, individual trades are not settled one-by-one by corresponding entries on the books of any depository. Rather, settlement of the individual trades occurs through the clearing arrangements, in accordance with the rules and agreements that govern those arrangements.

In the rules dealing with the indirect holding system, one must be particularly careful to bear in mind the distinction between trade and settlement. Under Revised Article 8 [Title 30, chapter 8], the property interest of a person who holds securities through an intermediary is described as a "security entitlement," which is defined in Revised Section 8-102(a)(17) [30-8-112(1)(q)] as the package of rights and property interest of an entitlement holder specified in Part 5 [Title 30, chapter 8, part 5]. Saying that the security entitlement is a package of rights against the broker does not mean that all of the customer's rights against the broker are part of the security entitlement and hence part of the subject matter of Article 8 [Title 30, chapter 8]. The distinction between trade and settlement remains fundamental. The rules of this Article [chapter] on the indirect holding system deal with brokers and other intermediaries as media through which investors hold their financial assets. Brokers are also media through which investors buy and sell their financial assets, but that aspect of their role is not the subject of this Article [chapter].

The principal goal of the Article 8 [Title 30, chapter 8] revision project is to provide a satisfactory framework for analysis of the indirect holding system. The technique used in Revised Article 8 [Title 30, chapter 8] is to acknowledge explicitly that the relationship between a securities intermediary and its entitlement holders is sui generis, and to state the applicable commercial law rules directly, rather than by inference from a categorization of the relationship based on legal concepts of a different era. One of the consequences of this drafting technique is that in order to provide content to the concept of security entitlement it becomes necessary to identify the core of the package of rights that make up a security entitlement. Sections 8-504 through 8-508 [30-8-504 through 30-8-508] cover such basic matters as the duty of the securities intermediary to maintain a sufficient quantity of securities to satisfy all of its entitlement holders, the duty of the securities intermediary to pass through to entitlement holder the economic and corporate law rights of ownership of the security, and the duty of the securities intermediary to comply with authorized entitlement orders originated by the entitlement holder. These sections are best thought of as definitional; that is, a relationship which does not include these rights is not the kind of relationship that Revised Article 8 [Title 30, chapter 8] deals with. Because these sections take the form of statements of the duties of an intermediary toward its entitlement holders, one must be careful to avoid a distorted perspective on what Revised Article 8 [Title 30, chapter 8] is and is not designed to do. Revised Article 8 [Title 30, chapter 8] is not, and should not be, a comprehensive body of private law governing the relationship between brokers and their customers, nor a body of regulatory law to police against improper conduct by brokers or other intermediaries. Many, if not most, aspects of the relationship between brokers and customers are governed by the common law of contract and agency, supplemented or supplanted by federal and state regulatory law. Revised Article 8 [Title 30, chapter 8] does not take the place of this body of private and regulatory law. If there are gaps in the regulatory law, they should be dealt with as such; Article 8 [Title 30, chapter 8] is not the place to address them. Article 8 [Title 30, chapter 8] deals with how interests in securities are evidenced and how they are transferred. By way of a rough analogy, one might think of Article 8 [Title 30, chapter 8] as playing the role for the securities markets that real estate recording acts play for the real estate markets. Real estate recording acts do not regulate the conduct of parties to real estate transactions; Article 8 [Title 30, chapter 8] does not regulate the conduct of parties to securities transactions.

C. Application of Revised Articles 8 and 9 [Title 30, chapters 8 and 9A] to Common Investments and Investment Arrangements

It may aid understanding to sketch briefly the treatment under Revised Articles 8 and 9 [Title 30, chapters 8 and 9A] of a variety of relatively common products and arrangements.

1. Publicly traded stocks and bonds.

"Security" is defined in Revised Section 8-102(a)(15) [30-8-112(1)(o)] in substantially the same terms as in the prior version of Article 8 [Title 30, chapter 8]. It covers the ordinary publicly traded investment securities, such as corporate stocks and bonds. Parts 2, 3, and 4 [Title 30, chapter 8, parts 2, 3, and 4] govern the interests of persons who hold securities directly, and Part 5 [Title 30, chapter 8, part 5] governs the interest of those who hold securities indirectly.

Ordinary publicly traded securities provide a good illustration of the relationship between the direct and indirect holding system rules. The distinction between the direct and indirect holding systems is not an attribute of the securities themselves but of the way in which a particular person holds the securities. Thus, whether one looks to the direct holding system rules of Parts 2, 3, and 4 [Title 30, chapter 8, parts 2, 3, and 4] or the indirect holding system rules of Part 5 [Title 30, chapter 8, part 5] will depend on the level in the securities holding system being analyzed.

Consider, for example, corporate stock which is held through a depository, such as DTC. The clearing corporation, or its nominee, is the registered owner of all of the securities it holds on behalf of all of its participants. Thus the rules of Parts 2, 3, and 4 of Revised Article 8 [Title 30, chapter 8, parts 2, 3, and 4] apply to the relationship between the issuer and the clearing corporation. If, as is typically the case today, the securities are still represented by certificates, the clearing corporation will be the holder of the security certificate or certificates representing its total holdings. So far as Article 8 [Title 30, chapter 8] is concerned, the relationship between the issuer and the clearing corporation is no different from the relationship between the issuer and any other registered owner.

The relationship between the clearing corporation and its participants is governed by the indirect holding system rules of Part 5 [Title 30, chapter 8, part 5]. At that level, the clearing corporation is the securities intermediary and the participant is the entitlement holder. If the participant is itself a securities intermediary, such as a broker holding for its customers or a bank acting as a securities custodian, the Part 5 [Title 30, chapter 8, part 5] rules apply to its relationship to its own customers. At that level the broker or bank custodian is the securities intermediary and the customer is the entitlement holder. Note that the broker or bank custodian is both an entitlement holder and a securities intermediary—but is so with respect to different security entitlements. For purposes of Article 8 [Title 30, chapter 8] analysis, the customer's security entitlement against the broker or bank custodian is a different item of property from the security entitlement of the broker or bank custodian against the clearing corporation.

For investors who hold their securities directly, it makes no difference that some other investors hold their interests indirectly. Many investors today choose to hold their securities directly, becoming the registered owners on the books of the issuer and obtaining certificates registered in their names. For such investors, the addition of the new indirect holding system rules to Article 8 [Title 30, chapter 8] is entirely irrelevant. They will continue to deal directly with the issuers, or their transfer agents, under essentially the same rules as in the prior version of Article 8 [Title 30, chapter 8].

The securities holding options available to investors in a particular form of security may depend on the terms of the security. For example, direct holding is frequently not available for new issues of state and local government bonds. At one time, state and local government bonds were commonly issued in bearer form. Today, however, new issues of state and local government bonds must be in registered form and most are issued in what is known as "book-entry only" form; that is, the issuer specifies that the only person it will directly register as the registered owner is a clearing corporation. Thus, one of the inherent terms of the security is that investors can hold only in the indirect holding system.

2. Treasury securities.

U.S. government securities fall within the definition of security in Article 8 [Title 30, chapter 8] and therefore are governed by Article 8 [Title 30, chapter 8] in the same fashion as any other publicly held debt security, except insofar as Article 8 [Title 30, chapter 8] is preempted by applicable federal law or regulation.

New Treasury securities are no longer issued in certificated form; they can be held only through the book-entry systems established by the Treasury and Federal Reserve Banks. The Treasury offers a book-entry system, known as "Treasury Direct" which enables individual investors to have their positions recorded directly on the books of a Federal Reserve Bank, in a fashion somewhat similar to the uncertificated direct holding system contemplated by the 1978 version of Article 8 [Title 30, chapter 8]. The governing law for the Treasury Direct system, however, is set out in the applicable Treasury regulations. The Treasury Direct system is not designed for active trading.

The great bulk of Treasury securities are held not through the Treasury Direct system but through a multi-tiered indirect holding system. The Federal Reserve Banks, acting as fiscal agent for the Treasury, maintain records of the holdings of member banks of the Federal Reserve System, and those banks in turn maintain records showing the extent to which they are holding for themselves or their own customers, including government securities dealers, institutional investors, or smaller banks who in turn may act as custodians for investors. The indirect holding system for Treasury securities was established under federal regulations promulgated in the 1970s. In the 1980s, Treasury released the proposed TRADES regulations that would have established a more comprehensive body of federal commercial law for the Treasury holding system. During the Article 8 [Title 30, chapter 8] revision process, Treasury withdrew these regulations, anticipating that once Revised Article 8 is enacted, it will be possible to base the law for the Treasury system on the new Article 8 [Title 30, chapter 8] rules.

3. Broker-customer relationships.

Whether the relationship between a broker and its customer is governed by the Article 8 Part 5 [Title 30, chapter 8, part 5] rules depends on the nature of the services that the broker performs for the customer.

Some investors use brokers only to purchase and sell securities. These customers take delivery of certificates representing the securities they purchase and hold them in their own names. When they wish to sell, they deliver the certificates to the brokers. The Article 8 Part 5 [Title 30, chapter 8, part 5] rules would not affect such customers, because the Part 5 [Title 30, chapter 8, part 5] rules deal with arrangements in which investors hold securities through securities intermediaries. The transaction between the customer and broker might be the traditional agency arrangement in which the broker buys or sells on behalf of the customer as agent for an undisclosed principal, or it might be a dealer transaction in which the "broker" as principal buys from or sells to the customer. In either case, if the customer takes delivery and holds the securities directly, she will become the "purchaser" of a "security" whose interest therein is governed by the rules of Parts 2, 3, and 4 of Article 8 [Title 30, chapter 8, parts 2, 3, and 4]. If the customer meets the other requirements of Section 8-303(a) [30-8-333(1)], the customer who takes delivery can qualify as a "protected purchaser" who takes free from any adverse claims under Section 8-303(b) [30-8-333(2)]. The broker's role in such transactions is primarily governed by non-Article 8 [Title 30, chapter 8] law. There are only a few provisions of Article 8 [Title 30, chapter 8] that affect the relationship between the customer and broker in such cases. See Section 8-108 [30-8-118] (broker makes to the customer the warranties of a transferor) and 8115 [30-8-125] (broker not liable in conversion if customer was acting wrongfully against a third party in selling securities).

Many investors use brokers not only to purchase and sell securities, but also as the custodians through whom they hold their securities. The indirect holding system rules of Part 5 [Title 30, chapter 8, part 5] apply to the custodial aspect of this relationship. If a customer purchases a security through a broker and directs the broker to hold the security in an account for the customer, the customer will never become a "purchaser" of a "security" whose interest therein is governed by the rules of Parts 2, 3, and 4 of Article 8 [Title 30, chapter 8, parts 2, 3, and 4]. Accordingly, the customer does not become a "protected purchaser" under Section 8-303 [30-8-333]. Rather, the customer becomes an "entitlement holder" who has a "security entitlement" to the security against the broker as "securities intermediary." See Section 8-501 [30-8-501]. It would make no sense to say that the customer in such a case takes an interest in the security free from all other claims, since the nature of the relationship is that the customer has an interest in common with other customers who hold positions in the same security through the same broker. Section 8-502 [30-8-502], however, does protect an entitlement holder against adverse claims, in the sense that once the entitlement holder has acquired the package of rights that comprise a security entitlement no one else can take that package of rights away by arguing that the transaction that resulted in the customer's acquisition of the security entitlement was the traceable product of a transfer or transaction that was wrongful as against the claimant.

4. Bank deposit accounts; brokerage asset management accounts.

An ordinary bank deposit account would not fall within the definition of "security" in Section 8-102(a)(15) [30-8-112(1)(o)], so the rules of Parts 2, 3, and 4 of Article 8 [Title 30, chapter 8, parts 2, 3, and 4] do not apply to deposit accounts. Nor would the relationship between a bank and its depositors be governed by the rules of Part 5 of Article 8 [Title 30, chapter 8, part 5]. The Part 5 [Title 30, chapter 8, part 5] rules apply to "security entitlements." Section 8-501(b) [30-8-501(2)] provides that a person has a security entitlement when a securities intermediary credits a financial asset to the person's "securities account." "Securities account" is defined in Section 8-501(a) [30-8-501(1)] as "an account to which a financial asset is or may be credited in accordance with an agreement under which the person maintaining the account undertakes to treat the person for whom the account is maintained as entitled to exercise the rights that comprise the financial asset." The definition of securities account plays a key role in setting the scope of Part 5 of Article 8 [Title 30, chapter 8, part 5]. A person has a security entitlement governed by Part 5 [Title 30, chapter 8, part 5] only if the relationship in question falls within the definition of "securities account." The definition of securities account in Section 8-501(a) [30-8-501(1)] excludes deposit accounts from the Part 5 rules of Article 8 [Title 30, chapter 8, part 5]. One of the basic elements of the relationship between a securities intermediary and an entitlement holder is that the securities intermediary has the duty to hold exactly the quantity of securities that it carries for the account of its customers. See Section 8-504 [30-8-504]. The assets that a securities intermediary holds for its entitlement holder are not assets that the securities intermediary can use in its own proprietary business. See Section 8-503 [30-8-503]. A deposit account is an entirely different arrangement. A bank is not required to hold in its vaults or in deposit accounts with other banks a sum of money equal to the claims of all of its depositors. Banks are permitted to use depositors' funds in their ordinary lending business; indeed, that is a primary function of banks. A deposit account, unlike a securities account, is simply a debtor-creditor relationship. Thus a bank or other financial institution maintaining deposit accounts is not covered by Part 5 of Article 8 [Title 30, chapter 8, part 5].

Today, it is common for brokers to maintain securities accounts for their customers which include arrangements for the customers to hold liquid "cash" assets in the form of money market mutual fund shares. Insofar as the broker is holding money market mutual fund shares for its customer, the customer has a security entitlement to the money market mutual fund shares. It is also common for brokers to offer their customers an arrangement in which the customer has access to those liquid assets via a deposit account with a bank, whereby shares of the money market fund are redeemed to cover checks drawn on the account. Article 8 [Title 30, chapter 8] applies only to the securities account; the linked bank account remains an account covered by other law. Thus the rights and duties of the customer and the bank are governed not by Article 8 [Title 30, chapter 8], but by the relevant payment system law, such as Article 4 or Article 4A [Title 30, chapter 4 or 4A].

5. Trusts.

The indirect holding system rules of Part 5 of Article 8 [Title 30, chapter 8, part 5] are not intended to govern all relationships in which one person holds securities "on behalf of" another. Rather, the Part 5 [Title 30, chapter 8, part 5] rules come into play only if the relationship in question falls within the definition of securities account in Section 8-501(a) [30-8-501(1)]. The definition of securities account serves the important function of ensuring that ordinary trust arrangements are not inadvertently swept into Part 5 of Article 8 [Title 30, chapter 8, part 5]. Suppose that Bank serves as trustee of a trust for the benefit of Beneficiary. The corpus of the trust is invested in securities and other financial assets. Although Bank is, in some senses, holding securities for Beneficiary, the arrangement would not fall within the definition of securities account. Bank, as trustee, has not undertaken to treat Beneficiary as entitled to exercise all of the rights that comprise the portfolio securities. For instance, although Beneficiary receives the economic benefit of the portfolio securities, Beneficiary does not have the right to direct dispositions of individual trust assets or to exercise voting or other corporate law rights with respect to the individual securities. Thus Bank's obligations to Beneficiary as trustee are governed by ordinary trust law, not by Part 5 of Article 8 [Title 30, chapter 8, part 5]. Of course, if Bank, as trustee, holds the securities through an intermediary, Part 5 of Revised Article 8 [Title 30, chapter 8, part 5] would govern the relationship between Bank, as entitlement holder, and the intermediary through which Bank holds the securities. It is also possible that a different department of Bank acts as the intermediary through which Bank, as trustee, holds the securities. Bank, *qua* securities custodian, might be holding securities for a large number of customers, including Bank's own trust department. Insofar as Bank may be regarded as acting in different capacities, Part 5 of Article 8 [Title 30, chapter 8, part 5] may be relevant to the relationship between the two sides of Bank's business. However, the relationship between Bank as trustee and the beneficiaries of the trust would remain governed by trust law, not Article 8 [Title 30, chapter 8].

6. Mutual fund shares.

Shares of mutual funds are Article 8 [Title 30, chapter 8] securities, whether the fund is organized as a corporation, business trust, or other form of entity. See Sections 8-102(a)(15) and 8-103(b) [30-8-112(1)(o) and 30-8-113(2)]. Mutual funds commonly do not issue certificates. Thus, mutual fund shares are typically uncertificated securities under Article 8 [Title 30, chapter 8].

Although a mutual fund is, in a colloquial sense, holding the portfolio securities on behalf of the fund's shareholders, the indirect holding system rules of Part 5 [Title 30, chapter 8, part 5] do not apply to the relationship between the fund and its shareholders. The Part 5 [Title 30, chapter 8, part 5] rules apply to "security entitlements." Section 8-501(e) [30-8-501(5)] provides that issuance of a security is not establishment of a security entitlement. Thus, because mutual funds shares do fit within the Article 8 [Title 30, chapter 8] definition of security, the relationship between the fund and its shareholders is automatically excluded from the Part 5 [Title 30, chapter 8, part 5] rules.

Of course, a person might hold shares in a mutual fund through a brokerage account. Because mutual fund shares are securities, they automatically fall within the broader term "financial asset," so the Part 5 [Title 30, chapter 8, part 5] indirect holding system rules apply to mutual fund shares that are held through securities accounts. That is, a person who holds mutual fund shares through a brokerage account could have a security entitlement to the mutual fund shares, just as the person would have a security entitlement to any other security carried in the brokerage account.

7. Stock of closely held corporations.

Ordinary corporate stock falls within the Article 8 [Title 30, chapter 8] definition of security, whether or not it is publicly traded. See Sections 8-102(a)(15) and 8-103(a) [30-8-112(1)(o) and 30-8-113(1)]. There is nothing in the new indirect holding system rules of Article 8 [Title 30, chapter 8] that would preclude their application to shares of companies that are not publicly traded. The indirect holding system rules, however, would come into play only if the shares were in fact held through a securities account with a securities intermediary. Since that is typically not the case with respect to shares of closely held corporations, transactions involving those shares will continue to be governed by the traditional rules, as amended, that are set out in Parts 2, 3, and 4 of Article 8 [Title 30, chapter 8, parts 2, 3, and 4], and the corresponding provisions of Article 9 [Title 30, chapter 9A]. The simplification of the Article 8 [Title 30, chapter 8] rules on uncertificated securities may, however, make the alternative of dispensing with certificates more attractive for closely held corporations.

8. Partnership interests and limited liability company shares.

Interests in partnerships or shares of limited liability companies are not Article 8 [Title 30, chapter 8] securities unless they are in fact dealt in or traded on securities exchanges or in securities markets. See Section 8-103(c) [30-8-113(3)]. The issuers, however, may if they wish explicitly "opt-in" by specifying that the interests or shares are securities governed by Article 8 [Title 30, chapter 8]. Even though interests in partnerships or shares of limited liability companies do not generally fall within the category of "security" in Article 8 [Title 30, chapter 8], they would fall within the broader term "financial asset." Accordingly, if such interests are held through a securities account with a securities intermediary, the indirect holding system rules of Part 5 [Title 30, chapter 8, part 5] apply, and the interest of a person who holds them through such an account is a security entitlement.

9. Bankers' acceptances, commercial paper, and other money market instruments.

Money market instruments, such as commercial paper, bankers' acceptances, and certificates of deposit, are good examples of a form of property that may fall within the definition of "financial asset," even though they may not fall within the definition of "security." Section 8-103(d) [30-8-113(4)] provides that a writing that meets the definition of security certificate under Section 8-102(a)(15) [30-8-112(1)(o)] is governed by Article 8 [Title 30, chapter 8], even though it also fits within the definition of "negotiable instrument" in Article 3 [Title 30, chapter 3].

Some forms of short term money market instruments may meet the requirements of an Article 8 [Title 30, chapter 8] security, while others may not. For example, the Article 8 [Title 30, chapter 8] definition of security requires that the obligation be in registered or bearer form. Bankers' acceptances are typically payable "to order," and thus do not qualify as Article 8 [Title 30, chapter 8] securities. Thus, the obligations of the immediate parties to a bankers' acceptance are governed by Article 3 [Title 30, chapter 3], rather than Article 8 [Title 30, chapter 8]. That is an entirely appropriate classification, even for those bankers' acceptance that are handled as investment media in the securities markets, because Article 8 [Title 30, chapter 8], unlike Article 3 [Title 30, chapter 3], does not contain rules specifying the standardized obligations of parties to instruments. For example, the Article 3 [Title 30, chapter 3] rules on the obligations of acceptors and drawers of drafts are necessary to specify the obligations represented by bankers' acceptances, but Article 8 [Title 30, chapter 8] contains no provisions dealing with these issues.

Immobilization through a depository system is, however, just as important for money market instruments as for traditional securities. Under the prior version of Article 8 [Title 30, chapter 8], the rules on the depository system, set out in Section 8-320 [former 30-8-320], applied only to Article 8 [Title 30, chapter 8] securities. Although some forms of money market instruments could be fitted within the language of the Article 8 [Title 30, chapter 8] definition of "security," this is not true for bankers' acceptances. Accordingly, it was not thought feasible to make bankers' acceptances eligible for deposit in clearing corporations under the prior version of Article 8 [Title 30, chapter 8]. Revised Article 8 [Title 30, chapter 8] solves this problem by separating the coverage of the Part 5 [Title 30, chapter 8, part 5] rules from the definition of security. Even though a bankers' acceptance or other money market instrument is an Article 3 [Title 30, chapter 3] negotiable instrument rather than an Article 8 [Title 30, chapter 8] security, it would still fall within the definition of financial asset in Section 8-102(a)(9) [30-8-112(1)(i)]. Accordingly, if the instrument is held through a clearing corporation or other securities intermediary, the rules of Part 5 of Article 8 [Title 30, chapter 8, part 5] apply.

10. Repurchase agreement transactions.

Repurchase agreements are an important form of transaction in the securities business, particularly in connection with government securities. Repos and reverse repos can be used for a variety of purposes. The one that is of particular concern for purposes of commercial law rules is the use of repurchase agreements as a form of financing transaction for government securities dealers. Government securities dealers typically obtain intra-day financing from their clearing banks, and then at the end of the trading day seek overnight financing from other sources to repay that day's advances from the clearing bank. Repos are the principal source of this financing. The dealer ("repo seller") sells securities to the financing source ("repo buyer") for cash, and at the same time agrees to repurchase the same or like securities the following day, or at some other brief interval. The sources of the financing include a variety of entities seeking short term investments for surplus cash, such as pension funds, business corporations, money market funds, and banks. The pricing may be computed in various ways, but in essence the price at which the dealer agrees to repurchase the securities exceeds the price paid to the dealer by an amount equivalent to interest on the funds.

The transfer of the securities from a securities dealer as repo seller to a provider of funds as repo buyer can be effected in a variety of ways. The repo buyer might be willing to allow the repo seller to keep the securities "in its hands," relying on the dealer's representation that it will hold them on behalf of the repo buyer. In the jargon of the trade, these are known as "hold-in-custody repos" or "HIC repos." At the other extreme, the repo buyer might insist that the dealer "hand over" the securities so that in the event that the dealer fails and is unable to perform its obligation to repurchase them, the repo buyer will have the securities "in its hands." The jargon for these is "delivered-out repos." A wide variety of arrangements between these two extremes might be devised, in which the securities are "handed over" to a third party with powers concerning their disposition allocated between the repo seller and repo buyer in a variety of ways.

Specification of the rights of repo buyers is complicated by the fact that the transfer of the interest in securities from the repo seller to the repo buyer might be characterized as an outright sale or as the creation of a security interest. Article 8 [Title 30, chapter 8] does not attempt to specify any categorical rules on that issue.

Article 8 [Title 30, chapter 8] sets out rules on the rights of parties who have implemented securities transactions in certain ways. It does not, however, deal with the legal characterization of the transactions that are implemented through the Article 8 [Title 30, chapter 8] mechanisms. Rather, the Article 8 [Title 30, chapter 8] rules apply without regard to the characterization of transactions for other purposes. For example, the Article 8 [Title 30, chapter 8] rules for the direct holding system provide that a person who takes delivery of a duly indorsed security certificate for value and without notice of adverse claims takes free from any adverse claims. That rule applies without regard to the character of the transaction in which the security certificate was delivered. It applies both to delivery upon original issue and to delivery upon transfer. It applies to transfers in settlement of sales and to transfers in pledge. Similarly, the Article 8 [Title 30, chapter 8] indirect holding system rules, such as the adverse claim cut-off rules in Sections 8-502 and 8-510 [30-8-502 and 30-8-510], apply to the transactions that fall within their terms, whether those transactions were sales, secured transactions, or something else.

Repos involve transfers of interests in securities. The Article 8 [Title 30, chapter 8] rules apply to transfers of securities in repos, just as they apply to transfers of securities in any other form of transaction. The transfer of the interest in securities from the repo seller to the repo buyer might be characterized as an outright sale or as the creation of a security interest. Article 8 [Title 30, chapter 8] does not determine that question. The rules of Revised Article 8 [Title 30, chapter 8] have, however, been drafted to minimize the possibility that disputes over the characterization of the transfer in a repo would affect substantive questions that are governed by Article 8 [Title 30, chapter 8]. See, e.g., Section 8-510 [30-8-510] and Comment 4 thereto.

11. Securities lending transactions.

In a typical securities lending transaction, the owner of securities lends them to another person who needs the securities to satisfy a delivery obligation. For example, when a customer of a broker sells a security short, the broker executes an ordinary trade as seller and so must deliver the securities at settlement. The customer is "short" against the broker because the customer has an open obligation to deliver the securities to the broker, which the customer hopes to be able to satisfy by buying in the securities at a lower price. If the short seller's broker does not have the securities in its own inventory, the broker will borrow them from someone else. The securities lender delivers the securities to the borrowing broker, and the borrowing broker becomes contractually obligated to redeliver a like quantity of the same security. Securities borrowers are required to provide collateral, usually government securities, to assure performance of their redelivery obligation.

The securities lender does not retain any property interest in the securities that are delivered to the borrower. The transaction is an outright transfer in which the borrower obtains full title. The whole point of securities lending is that the borrower needs the securities to transfer them to someone else. It would make no sense to say that the lender retains any property interest in the securities it has lent. Accordingly, even if the securities borrower defaults on its redelivery obligation, the securities lender has no property interest in the original securities that could be asserted against any person to whom the securities borrower may have transferred them. One need not look to adverse claim cut-off rules to reach that result; the securities lender never had an adverse claim. The securities borrower's default is no different from any other breach of contract. The securities lender's protection is its right to foreclose on the collateral given to secure the borrower's redelivery obligation. Perhaps the best way to understand securities lending is to note that the word "loan" in securities lending transactions is used in the sense it carries in loans of money, as distinguished from loans of specific identifiable chattels. Someone who lends money does not retain any property interest in the money that is handed over to the borrower. To use civil law terminology, securities lending is *mutuum*, rather than *commodatum*. See Story on Bailments, §§ 6 and 47.

12. Traded stock options.

Stock options issued and cleared through the Options Clearing Corporation ("OCC") are a good example of a form of investment vehicle that is treated as a financial asset to which the Part 5 [Title 30, chapter 8, part 5] rules apply, but not as an Article 8 [Title 30, chapter 8] security to which Parts 2, 3, and 4 [Title 30, chapter 8, parts 2, 3, and 4] apply. OCC carries on its books the options positions of the brokerage firms which are clearing members of OCC. The clearing members in turn carry on their books the options positions of their customers. The arrangements are structurally similar to the securities depository system. In the options structure, however, there is no issuer separate from the clearing corporation. The financial assets held through the system are standardized contracts entitling the holder to purchase or sell a certain security at a set price. Rather than being an interest in or obligation of a separate issuer, an option is a contractual right against the counter-party. In order to assure performance of the options, OCC interposes itself as counter-party to each options trade. The rules of Parts 2, 3, and 4 of this Article [Title 30, chapter 8, parts 2, 3, and 4], however, do not well describe the obligations and rights of OCC. On the other hand, the rules of Part 5 [Title 30, chapter 8, part 5], and the related Article 9 [Title 30, chapter 9A] rules on security interests and priorities, do provide a workable legal framework for the commercial law analysis of the rights of the participants in the options market. Accordingly, publicly traded securities options are included within the definition of "financial asset," but not "security." See Section 8-103(e) [30-8-113(5)]. Thus, although OCC would not be an issuer of a security for purposes of this Article [chapter], it would be a clearing corporation, against whom its clearing members have security entitlements to the options positions. Similarly, the clearing members' customers have security entitlements against the clearing members. Traded stock options are also a good illustration of the point that the classification issues under Article 8 [Title 30, chapter 8] are very different from classification under other law, such as the federal securities laws. See Section 8-102(d) [30-8-112(4)]. Stock options are treated as securities for purposes of federal securities laws, but not for purposes of Article 8 [Title 30, chapter 8].

13. Commodity futures.

Section 8-103(f) [30-8-113(6)] provides that a "commodity contract" is not a security or a financial asset. Section 9-115 [30-9-115, now repealed, see 30-9A-102] defines commodity contract to include commodity futures contracts, commodity options, and options on commodity futures contracts that are traded on or subject to the rules of a board of trade that has been designated as a contract market for that contract pursuant to the federal commodities laws. Thus, commodity contracts themselves are not Article 8 [Title 30, chapter 8] securities to which the rules of Parts 2, 3, and 4 [Title 30, chapter 8, parts 2, 3, and 4] apply, nor is the relationship between a customer and a commodity futures commission merchant governed by the Part 5 rules of Article 8 [Title 30, chapter 8, part 5]. Commodity contracts, however, are included within the Article 9 [Title 30, chapter 9A] definition of "investment property." Thus security interests in commodity positions are governed by essentially the same set of rules as security interests in security entitlements.

14. "Whatever else they have or may devise."

The classification question posed by the above-captioned category of investment products and arrangements is among the most difficult—and important—issue raised by the Article 8 [Title 30, chapter 8] revision process. Rapid innovation is perhaps the only constant characteristic of the securities and financial markets. The rules of Revised Article 8 [Title 30, chapter 8] are intended to be sufficiently flexible to accommodate new developments.

A common mechanism by which new financial instruments are devised is that a financial institution that holds some security, financial instrument, or pool thereof, creates interests in that asset or pool which are sold to others. It is not possible to answer in the abstract the question of how such interests are treated under Article 8 [Title 30, chapter 8], because the variety of such products is limited only by human imagination and current regulatory structures. At this general level, however, one can note that there are at least three possible treatments under Article 8 [Title 30, chapter 8] of the relationship between the institution which creates the interests and the persons who hold them. (Again, it must be borne in mind that the Article 8 [Title 30, chapter 8] classification issue may be different from the classification question posed by federal securities law or other regulation.) First, creation of the new interests in the underlying assets may constitute issuance of a new Article 8 [Title 30, chapter 8] security. In that case the relationship between the institution that created the interest and the persons who hold them is not governed by the Part 5 rules [Title 30, chapter 8, part 5], but by the rules of Parts 2, 3, and 4 [Title 30, chapter 8, parts 2, 3, and 4]. See Section 8-501(e) [30-8-501(5)]. That, for example, is the structure of issuance of mutual fund shares. Second, the relationship between the entity creating the interests and those holding them may fit within the Part 5 [Title 30, chapter 8, part 5] rules, so that the persons are treating as having security entitlements against the institution with respect to the underlying assets. That, for example, is the structure used for stock options. Third, it may be that the creation of the new interests in the underlying assets does not constitute issuance of a new Article 8 [Title 30, chapter 8] security, nor does the relationship between the entity creating the interests and those holding them fit within the Part 5 [Title 30, chapter 8, part 5] rules. In that case, the relationship is governed by other law, as in the case of ordinary trusts.

The first of these three possibilities—that the creation of the new interest is issuance of a new security for Article 8 [Title 30, chapter 8] purposes—is a fairly common pattern. For example, an American depositary receipt facility does not maintain securities accounts but issues securities called ADRs in respect of foreign securities deposited in such facility. Similarly, custodians of government securities which issue receipts, certificates, or the like representing direct interests in those securities (sometimes interests split between principal and income) do not maintain securities accounts but issue securities representing those interests. Trusts holding assets, in a variety of structured and securitized transactions, which issue certificates or the like representing "pass-through" or undivided beneficial interests in the trust assets, do not maintain securities accounts but issue securities representing those interests.

In analyzing these classification questions, courts should take care to avoid mechanical jurisprudence based solely upon exegesis of the wording of definitions in Article 8 [Title 30, chapter 8]. The result of classification questions is that different sets of rules come into play. In order to decide the classification question it is necessary to understand fully the commercial setting and consider which set of rules best fits the transaction. Rather than letting the choice of rules turn on interpretation of the words of the definitions, the interpretation of the words of the definitions should turn on the suitability of the application of the substantive rules.

IV. CHANGES FROM PRIOR (1978) VERSION OF ARTICLE 8 [TITLE 30, CHAPTER 8]

Revision Notes

1. Provisions of former Article 8 [Title 30, chapter 8] on clearing corporations.

The keystone of the treatment of the indirect holding system in the prior version of Article 8 [Title 30, chapter 8] was the special provision on clearing corporations in Section 8-320 [former 30-8-320]. Section 8-320 [former 30-8-320] was added to Article 8 [Title 30, chapter 8] in 1962, at the very end of the process that culminated in promulgation and enactment of the original version of the Code. The key concepts of the original version of Article 8 [Title 30, chapter 8] were "bona fide purchaser" and "delivery." Under Section 8-302 (1962) [former 30-8-302] one could qualify as a "bona fide purchaser" only if one had taken delivery of a security, and Section 8-313 (1962) [former 30-8-313] specified what counted as a delivery.

Section 8-320 [former 30-8-320] was added to take account of the development of the system in which trades can be settled by netted book-entry movements at a depository without physical deliveries of certificates. Rather than reworking the basic concepts, however, Section 8-320 [former 30-8-320] brought the depository system within Article 8 [Title 30, chapter 8] by definitional fiat. Subsection (a) of Section 8-320 (1962) [former 30-8-320(1)] stated that a transfer or pledge could be effected by entries on the books of a central depository, and subsection (b) [subsection (2)] stated that such an entry "has the effect of a delivery of a security in bearer form or duly indorsed in blank." In 1978, Section 8-320 [former 30-8-320] was revised to conform it to the general substitution of the concept of "transfer" for "delivery," but the basic structure remained the same. Under the 1978 version of Article 8 [Title 30, chapter 8], the only book-entry transfers that qualified the transferee for bona fide purchaser rights were those made on the books of a clearing corporation. See Sections 8-302(1)(c), 8-313(1)(g), and 8-320 [former 30-8-302(1)(c), 30-8-313(1)(g), and 30-8-320]. Thus, for practical purposes, the indirect holding system rules of the prior version of Article 8 [Title 30, chapter 8] required that the securities be held by a clearing corporation in accordance with the central depository rules of Section 8-320 [former 30-8-320].

Some of the definitional provisions concerning clearing corporation in the prior version of Article 8 [Title 30, chapter 8] seem to have conflated the commercial law rules on the effect of book-entry transactions with issues about the regulation of entities that are acting as clearing corporations. For example, the Section 8-320 [former 30-8-320] rules that gave effect to book-entry transfers applied only if the security was "in the custody of the clearing corporation, another clearing corporation, [or] a custodian bank." "Custodian bank" was defined in Section 8-102(4) [former 30-8-102(4)] as "a bank or trust company that is supervised and examined by state or federal authority having supervision over banks and is acting as custodian for a clearing corporation." Although this was probably inadvertent, these definitional provisions have operated as an obstacle to the development of clearing arrangements for global trading, since they effectively precluded clearing corporations from using foreign banks as custodians.

Revised Article 8 [Title 30, chapter 8] is based on the view that Article 8 [Title 30, chapter 8] is not the proper place for regulatory decisions about whether certain sorts of financial institutions should or should not be permitted to engage in a particular aspect of the securities business, such as acting as a clearing corporation, or how they should be permitted to conduct that business. Rather, Article 8 [Title 30, chapter 8] should deal only with the commercial law questions of what duties and rights flow from doing business as a clearing corporation, leaving it to other regulatory law to decide which entities should be permitted to act as clearing corporations, and to regulate their activities. Federal securities laws now establish a detailed regulatory structure for clearing corporations; there is no need for Article 8 [Title 30, chapter 8] to duplicate parts of that structure. Revised Article 8 [Title 30, chapter 8] deletes all provision of the prior version which had the effect of specifying how clearing corporations should conduct their operations. For example, Revised Article 8 [Title 30, chapter 8] deletes the definition of "custodian bank," which operated in the prior version only as a regulatory restriction on how clearing corporations could hold securities.

In general, the structure of Revised Article 8 [Title 30, chapter 8] is such that there is relatively little need for special provisions on clearing corporations. Book-entry transactions effected through clearing corporations are treated under the same rules in Part 5 [Title 30, chapter 8, part 5] as book-entry transactions effected through any other securities intermediary. Accordingly, Revised Article 8 [Title 30, chapter 8] has no direct analog of the special provisions in Section 8-320 [former 30-8-320] on transfers on the books of clearing corporations.

2. Former Section 8-313 [former 30-8-313]—"Transfer."

Section 8-313 [former 30-8-313] of the 1978 version of Article 8 [Title 30, chapter 8] was extremely complicated, because it attempted to cover many different issues. The following account of the evolution of Section 8-313 [former 30-8-313] may assist in understanding why a different approach is taken in Revised Article 8 [Title 30, chapter 8]. This explanation is, however, intended not as an actual account of historical events, but as a conceptual reconstruction, devised from the perspective of, and with the benefit of, hindsight.

The original objective of Article 8 [Title 30, chapter 8] was to ensure that certificates representing investment securities would be "negotiable" in the sense that purchasers would be protected by the bona fide purchaser rules. The requirements for bona fide purchaser status were that the purchaser had to (i) take delivery of the security and (ii) give value in good faith and without notice of adverse claims. Section 8-313 [former 30-8-313] specified what counted as a "delivery," and Section 8-302 [former 30-8-302] specified the other requirements.

The 1978 amendments added provisions on uncertificated securities, but the basic organizational pattern was retained. Section 8-302 [former 30-8-302] continued to state the requirements of value, good faith, and lack of notice for good faith purchase, and Section 8-313 [former 30-8-313] stated the mechanism by which the purchase had to be implemented. Delivery as defined in the original version of Section 8-313 [former 30-8-313] had a meaning similar to the concept known in colloquial securities jargon as "good delivery"; that is, physical delivery with any necessary indorsement. Although the word "delivery" has now come to be used in securities parlance in a broader sense than physical delivery, when the provisions for uncertificated securities were added it was thought preferable to use another word. Thus, the word "transfer" was substituted for "delivery" in Section 8-313 [former 30-8-313].

The 1978 amendments also moved the rules governing security interests in securities from Article 9 [Title 30, chapter 9A] to Article 8 [Title 30, chapter 8], though the basic conceptual structure of the common law of pledge was retained. Since a pledge required a delivery, and since the term transfer had been substituted for delivery, the 1978 amendments provided that in order to create a security interest there must be a "transfer," in the defined Article 8 [Title 30, chapter 8] sense, from the debtor to the secured party. Accordingly, provisions had to be added to Section 8-313 [former 30-8-313] so that any of the steps that should suffice to create a perfected security interest would be deemed to constitute a "transfer" within the meaning of Section 8-313 [former 30-8-313]. Thus, the Section 8-313 [former 30-8-313] rules on "transfer," which had in the previous version dealt only with what counted as a delivery that qualified one for bona fide purchaser status, became the statutory locus for all of the rules on creation and perfection of security interests in securities. Accordingly the rather elaborate rules of subsections (1)(h), (1)(i), and (1)(j) [former subsections (1)(h), (1)(i), and (1)(j)] were added.

Having expanded Section 8-313 [former 30-8-313] to the point that it served as the rule specifying the formal requirements for transfer of all significant forms of interests in securities, it must have seemed only logical to take the next step and make the Section 8-313 [former 30-8-313] rules the exclusive means of transferring interests in securities. Thus, while the prior version had stated that "Delivery to a purchaser occurs when ...", the 1978 version stated that "Transfer of a security or a limited interest (including a security interest) therein to a purchaser occurs *only* ....” Having taken that step, however, it then became necessary to ensure that anyone who should be regarded as having an interest in a security would be covered by some provision of Section 8-313 [former 30-8-313]. Thus, the provisions of subsection (1)(d)(ii) and (iii) [former subsections (1)(d)(ii) and (1)(d)(iii)] were added to make it possible to say that the customers of a securities intermediary who hold interests in securities held by the intermediary in fungible bulk received “transfers.”

Section 8-313(1)(d) [former 30-8-313(1)(d)] was the key provision in the 1978 version dealing with the indirect holding system at the level below securities depositories. It operated in essentially the same fashion as Section 8-320 [former 30-8-320]; that is, it stated that when a broker or bank holding securities in fungible bulk makes entries on its books identifying a quantity of the fungible bulk as belonging to the customer, that action is treated as a “transfer”—in the special Section 8-313 [former 30-8-313] sense—of an interest in the security from the intermediary to the customer.

Revised Article 8 [Title 30, chapter 8] has no direct analog of the 1978 version of Section 8-313 [former 30-8-313]. The rules on secured transactions have been returned to Article 9 [Title 30, chapter 9A], so subsections of Section 8-313 (1978) [former 30-8-313] dealing with security interests are deleted from Article 8 [Title 30, chapter 8]. Insofar as portions of Section 8-313 (1978) [former 30-8-313] were designed to specify the formal requirements for transferees to qualify for protection against adverse claims, their place is taken by Revised Section 8-301 [30-8-331], which defines “delivery,” in a fashion somewhat akin to the pre1978 version of Section 8-313 [former 30-8-313]. The descendant of the provisions of Section 8-313 (1978) [former 30-8-313] dealing with the indirect holding system is Revised Section 8-501 [30-8-501] which specifies when a person acquires a security entitlement. Section 8-501 [30-8-501], however, is based on a different analysis of the transaction in which a customer acquires a position in the indirect holding system. The transaction is not described as a “transfer” of an interest in some portion of a fungible bulk of securities held by the securities intermediary but as the creation of a security entitlement. Accordingly, just as Revised Article 8 [Title 30, chapter 8] has no direct analog of the Section 8-320 [former 30-8-320] rules on clearing corporation transfers, it has no direct analog of the Section 8-313(1) [former 30-8-313(1)] rules on “transfers” of interests in securities held in fungible bulk.

3. Uncertificated securities provisions.

Given the way that securities holding practices have evolved, the sharp distinction that the 1978 version of Article 8 [Title 30, chapter 8] drew between certificated securities and uncertificated securities has become somewhat misleading. Since many provisions of the 1978 version had separate subsections dealing first with certificated securities and then with uncertificated securities, and since people intuitively realize that the volume of trading in the modern securities markets could not possibly be handled by pushing around certificates, it was only natural for a reader of the statute to conclude that the uncertificated securities provisions of Article 8 [Title 30, chapter 8] were the basis of the book-entry system. That, however, is not the case. Although physical delivery of certificates plays little role in the settlement system, most publicly traded securities are still, in legal theory, certificated securities. To use clearance and settlement jargon, the book-entry securities holding system has used “immobilization” rather than “dematerialization.”

The important legal and practical difference is between the direct holding system, in which the beneficial owners have a direct relationship with the issuer, and the indirect holding system, in which securities are held through tiers of securities intermediaries. Accordingly, in Revised Article 8 [Title 30, chapter 8] the contrast between certificated securities and uncertificated securities has been minimized or eliminated as much as possible in stating the substantive provisions.

4. Transaction statements.

Although the 1978 provisions on uncertificated securities contemplated a system in which there would be no definitive certificates as reifications of the underlying interests or obligations, the 1978 amendments did not really dispense with all requirements of paper evidence of securities holding. The 1978 amendments required issuers of uncertificated securities to send paper “transaction statements” upon registration of transfer. Section 8-408 [former 30-8-408] regulated the content and format of these transaction statements in considerable detail. The statements had to be in writing, include specific information, and contain a conspicuous legend stating that “This statement is merely a record of the rights of the addressee as of the time of its issuance. Delivery of this statement, of itself, confers no rights on the recipient. This statement is neither a negotiable instrument nor a security.” Issuers were required to send statements when any transfer was registered (known as "initial transaction statements") and also were required to send periodic statements at least annually and also upon any security holder's reasonable request. Fees were regulated to some extent, in that Section 8-408(8) [former 30-8-408(8)] specified that if periodic statements were sent at least quarterly, the issuer could charge for statements requested by security holders at other times.

The detailed specification of reporting requirements for issuers of uncertificated securities was quite different from the treatment of securities intermediaries. Though the prior version of Article 8 [Title 30, chapter 8] did require non-clearing corporation securities intermediaries to send confirmations of transfers—a requirement deleted in Revised Article 8 [Title 30, chapter 8]—it did not regulate their content or format. Article 8 [Title 30, chapter 8] has never imposed periodic reporting requirements on securities intermediaries. Thus, reporting requirements for the indirect holding system were left to agreements and regulatory authorities, while reporting requirements for a book-entry direct holding system were imposed by statute.

Securities holding systems based on transaction statements of the sort contemplated by the 1978 amendments have not yet evolved to any major extent—indeed, the statutory specification of the details of the information system may itself have acted as an impediment to the evolution of a book-entry direct system. Accordingly, Revised Article 8 [Title 30, chapter 8] drops the statutory requirements concerning transaction statements. The record keeping and reporting obligations of issuers of uncertificated securities would be left to agreement and other law, as is the case today for securities intermediaries.

In the 1978 version, the Part 2 [Title 30, chapter 8, part 2] rules concerning transfer restrictions, issuers' defenses, and the like were based on the assumption that transaction statements would be used in a fashion analogous to traditional security certificates. For example, Sections 8-202 and 8-204 [former 30-8-202 and 30-8-204] specified that the terms of a security, or any restrictions on transfer imposed by the issuer, had to be noted on the transaction statement. Revised Article 8 [Title 30, chapter 8] deletes all such references to transaction statements. The terms of securities, or of restrictions of transfer, would be governed by whatever law or agreement specifies these matters, just as is the case for various other forms of business entities, such as partnerships, that have never issued certificates representing interests. Other Part 2 [Title 30, chapter 8, part 2] rules, such as Sections 8-205, 8-206, and 8-208 [former 30-8-205, 30-8-206, and 30-8-208], attempted to state rules on forgery and related matters for transactions statements. Since Revised Article 8 [Title 30, chapter 8] does not specify the format for information systems for uncertificated securities, there is no point in attempting to state rules on the consequences of wrongful information transmission in the particular format of written statements authenticated by signatures.

5. Deletion of provisions on registered pledges.

The 1978 version of Article 8 [Title 30, chapter 8] also added detailed provisions concerning "registered pledges" of uncertificated securities. Revised Article 8 [Title 30, chapter 8] adopts a new system of rules for security interests in securities, for both the direct and indirect holding systems that make it unnecessary to have special statutory provisions for registered pledges of uncertificated securities.

The reason that the 1978 version of Article 8 [Title 30, chapter 8] created this concept was that if the only means of creating security interests was the pledge, it seemed necessary to provide some substitute for the pledge in the absence of a certificate. The point of the registered pledge was, presumably, that it permitted a debtor to grant a perfected security interest in securities, yet still keep the securities in the debtor's own name for purposes of dividends, voting, and the like. The concept of registered pledge has, however, been thought troublesome by many legal commentators and securities industry participants. For example, in Massachusetts where many mutual funds have their headquarters, a non-uniform amendment was enacted to permit the issuer of an uncertificated security to refuse to register a pledge and instead issue a certificate to the owner that the owner could then pledge by ordinary means.

Under the 1978 version of Article 8 [Title 30, chapter 8], if an issuer chose to issue securities in uncertificated form, it was also required by statute to offer a registered pledge program. Revised Articles 8 and 9 [Title 30, chapters 8 and 9A] take a different approach. All of the provisions dealing with registered pledges have been deleted. This does not mean, however, that issuers cannot offer such a service. The control rules of Revised Section 8-106 [30-8-116] and the related priority provisions in Article 9 [Title 30, chapter 9A] establish a structure that permits issuers to develop systems akin to the registered pledge device, without mandating that they do so, or legislating the details of the system. In essence, the registered pledge or control device amounts to a record keeping service. A debtor can always transfer securities to its lender. In a registered pledge or control agreement arrangement, the issuer keeps track of which securities the secured party holds for its own account outright, and which securities it holds in pledge from its debtors.

Under the rules of Revised Articles 8 and 9 [Title 30, chapters 8 and 9A], the registered pledge issue can easily be left to resolution by the market. The concept of control is defined in such fashion that if an issuer or securities intermediary wishes to offer a service akin to the registered pledge device it can do so. The issuer or securities intermediary would offer to enter into agreements with the debtor and secured party under which it would hold the securities for the account of the debtor, but subject to instructions from the secured party. The secured party would thereby obtain control assuring perfection and priority of its lien.

Even if such arrangements are not offered by issuers, persons who hold uncertificated securities will have several options for using them as collateral for secured loans. Under the new rules, filing is a permissible method of perfection, for debtors other than securities firms. A secured party who relies on filing is, of course, exposed to the risk that the debtor will double finance and grant a later secured lender a security interest under circumstances that give that lender control and hence priority. If the lender is unwilling to run that risk, the debtor can transfer the securities outright to the lender on the books of the issuer, though between the parties the debtor would be the owner and the lender only a secured party. That, of course, requires that the debtor trust the secured party not to dispose of the collateral wrongfully, and the debtor may also need to make arrangements with the secured party to exercise benefits of ownership such as voting and receiving distributions.

It may well be that both lenders and borrowers would prefer to have some arrangement, such as the registered pledge device of current law, that permits the debtor to remain as the registered owner entitled to vote and receive dividends but gives the lender exclusive power to order their disposition. The approach taken in this revision is that if there is a genuine demand for such arrangements, it can be met by the market. The difficulty with the approach of present Article 8 [Title 30, chapter 8] is that it mandates that any issuer that wishes to issue securities in uncertificated form must also offer this record keeping service. That obligation may well have acted as a disincentive to the development of uncertificated securities. Thus, the deletion of the mandated registered pledge provisions is consistent with the principle of neutrality toward the evolution of securities holding practices.

6. Former Section 8-403 [former 30-8-403] Issuer's Duty as to Adverse Claims.

Section 8-403 [former 30-8-403] of the prior version of Article 8 [Title 30, chapter 8] dealt with the obligations of issuers to adverse claimants. The starting point of American law on issuers' liability in such circumstances is the old case of Lowry v. Commercial & Farmers' Bank, 15 F.Cas. 1040 (C.C.D.Md.1848) (No. 8551), under which issuers could be held liable for registering a transfer at the direction of a registered owner who was acting wrongfully as against a third person in making the transfer. The *Lowry* principle imposed onerous liability on issuers, particularly in the case of transfers by fiduciaries, such as executors and trustees. To protect against risk of such liability, issuers developed the practice of requiring extensive documentation for fiduciary stock transfers to assure themselves that the fiduciaries were acting rightfully. As a result, fiduciary stock transfers were cumbersome and time consuming.

In the present century, American law has gradually moved away from the *Lowry* principle. Statutes such as the Uniform Fiduciaries Act, the Model Fiduciary Stock Transfer Act, and the Uniform Act for the Simplification of Fiduciary Security Transfers sought to avoid the delays in stock transfers that could result from issuers' demands for documentation by limiting the issuer's responsibility for transfers in breach of the registered owner's duty to others. Although these statutes provided that issuers had no duty of inquiry to determine whether a fiduciary was acting rightfully, they all provided that an issuer could be liable if the issuer acted with notice of third party claims.

The prior version of Article 8 [Title 30, chapter 8] followed the same approach as the various fiduciary transfer statutes. Issuers were not required to seek out information from which they could determine whether a fiduciary was acting properly, but they were liable if they registered a transfer with notice that the fiduciary was acting improperly. Former Section 8-308(11) [former 30-8-308(11)] said that the failure of a fiduciary to comply with a controlling instrument or failure to obtain a court approval required under local law did not render the indorsement or instruction unauthorized. However, if a fiduciary was in fact acting improperly, then the beneficiary would be treated as an adverse claimant. See Section 8-302(2) (1978) [former 30-8-302(2)] and Comment 4. Former Section 8-403 [former 30-8-403] specified that if written notice of an adverse claim had been sent to the issuer, the issuer "shall inquire into the adverse claim" before registering a transfer on the indorsement or instruction of the registered owner. The issuer could "discharge any duty of inquiry by any reasonable means," including by notifying the adverse claimant that the transfer would be registered unless the adverse claimant obtained a court order or gave an indemnity bond.

Revised Article 8 rejects the *Lowry* principle altogether. It provides that an issuer is not liable for wrongful registration if it acts on an effective indorsement or instruction, even though the issuer may have notice of adverse claims, so long as the issuer has not been served with legal process and is not acting in collusion with the wrongdoer in registering the transfer. See Revised Section 8-404 [30-8-414] and Comments thereto. The provisions of prior Section 8-403 [former 30-8-403] specifying that issuers had a duty to investigate adverse claims of which they had notice are deleted.

Revised Article 8 [Title 30, chapter 8] also deletes the provisions set out in Section 8-403(3) [former 30-8-403(3)] of prior law specifying that issuers did not have a duty to inquire into the rightfulness of transfers by fiduciaries. The omission of the rules formerly in Section 8-403(3) [former 30-8-403(3)] does not, of course, mean that issuers would be liable for acting on the instruction of fiduciaries in the circumstances covered by former Section 8-403(3) [former 30-8-403(3)]. Former Section 8-403(3) [former 30-8-403(3)] assumed that issuers would be liable if they registered a transfer with notice of an adverse claim. Former Section 8-403(3) [former 30-8-403(3)] was necessary only to negate any inference that knowledge that a transfer was initiated by a fiduciary might give constructive notice of adverse claims. Under Section 8-404 [30-8-414] of Revised Article 8 [Title 30, chapter 8], mere notice of adverse claims does not impose duties on the issuer. Accordingly the provisions included in former Section 8-403(3) [former 30-8-403(3)] are unnecessary.

Although the prior version of Article 8 [Title 30, chapter 8] included provisions similar or identical to those set out in the Uniform Act for the Simplification of Fiduciary Security Transfers and similar statutes, most states retained these statutes at the time the Uniform Commercial Code was adopted. These statutes are based on a premise different from Revised Article 8 [Title 30, chapter 8]. The fiduciary simplification acts are predicated on the assumption that an issuer would be liable to an adverse claimant if the issuer had notice. These statutes seek only to preclude any inference that issuers have such notice when they register transfers on the instructions of a fiduciary. Revised Article 8 [Title 30, chapter 8] is based on the view that a third party should not be able to interfere with the relationship between an issuer and its registered shareholders unless the claimant obtains legal process. Since notice of an adverse claim does not impose duties on an issuer under Revised Article 8 [Title 30, chapter 8], the Uniform Act for the Simplification of Fiduciary Security Transfers, or similar statutes, should be repealed upon enactment of Revised Article 8 [Title 30, chapter 8].

7. Former Section 8-319 [former 30-8-319] Statute of Frauds.

Revised Article 8 [Title 30, chapter 8] deletes the special statute of frauds provision for securities contracts that was set out in former Section 8-319 [former 30-8-319]. See Revised Section 8-113 [30-8-123]. Most of the litigation involving the statute of frauds rule of the prior version of Article 8 [Title 30, chapter 8] involved informal transactions, rather than transactions on the organized securities markets. Typical cases were those in which an employee or former employee of a small enterprise sued to enforce an alleged promise that he or she would receive an equity interest in the business. The usual commercial policies relating to writings in contracts for the sale of personal property are at most tangentially implicated in such cases. There was a rather large and complex body of case law dealing with the applicability of Section 8-319 [former 30-8-319] to cases of this sort. It seems doubtful that the cost of litigating these issues was warranted by whatever protections the statute of frauds offered against fraudulent claims.

Subsection (c) of former Section 8-319 [former 30-8-319(3)] provided that the statute of frauds bar did not apply if a written confirmation was sent and the recipient did not seasonably send an objection. That provision, however, presumably would not have had the effect of binding a broker's customer to the terms of a trade for which confirmation had been sent though the customer had not objected within 10 days. In the first place, the relationship between a broker and customer is ordinarily that of agent and principal; thus the broker is not seeking to enforce a contract for sale of a security, but to bind its principal for action taken by the broker as agent. Former Section 8-319 [former 30-8-319] did not by its terms apply to the agency relationship. Moreover, even if former Section 8-319(c) [former 30-8-319(3)] applied, it is doubtful that it, of its own force, had the effect of precluding the customer from disputing whether there was a contract or what the terms of the contract were. Former Section 8-319(c) [former 30-8-319(3)] only removed the statute of frauds as a bar to enforcement; it did not say that there was a contract or that the confirmation had the effect of excluding other evidence of its terms. Thus, deletion of former Section 8-319 [former 30-8-319] does not change the law one way or the other on whether a customer who fails to object to a written confirmation is precluded from denying the trade described in the confirmation, because that issue was never governed by former Section 8-319(c) [former 30-8-319(3)].

8. Miscellaneous.

Prior Section 8-105 [former 30-8-105]. Revised Article 8 [Title 30, chapter 8] deletes the statement found in Section 8-105(1) [former 30-8-105(1)] of the prior version that certificated securities "are negotiable instruments." This provision was added very late in the drafting process of the original Uniform Commercial Code. Apparently the thought was that it might be useful in dealing with potential transition problems arising out of the fact that bonds were then treated as negotiable instruments under the Uniform Negotiable Instruments Law. During that era, many other statutes, such as those specifying permissible categories of investments for regulated entities, might have used such phrases as "negotiable securities" or "negotiable instruments." Section 8-105 [former 30-8-105] seems to have been included in the original version of Article 8 [Title 30, chapter 8] to avoid unfortunate interpretations of those other statutes once securities were moved from the Uniform Negotiable Instruments Law to UCC Article 8 [Title 30, chapter 8]. Whether or not Section 8-105 [former 30-8-105] was necessary at that time, it has surely outlived its purpose. The statement that securities "are negotiable instruments" is very confusing. As used in the Uniform Commercial Code, the term "negotiable instrument" means an instrument that is governed by Article 3 [Title 30, chapter 3]; yet Article 8 [Title 30, chapter 8] securities are not governed by Article 3 [Title 30, chapter 3]. Courts have occasionally cited Section 8-105(1) [former 30-8-105(1)] of prior law for the proposition that the rules that are generally thought of as characteristic of negotiability, such as the rule that bona fide purchasers take free from adverse claims, apply to certificated securities. Section 8-105(1) [former 30-8-105(1)], however, is unnecessary for that purpose, since the relevant rules are set out in specific provisions of Article 8 [Title 30, chapter 8].

Prior Sections 8-107 and 8-314 [former 30-8-107 and 30-8-314]. Article 8 [Title 30, chapter 8] has never been, and should not be, a comprehensive codification of the law of contracts for the purchase and sale of securities. The prior version of Article 8 [Title 30, chapter 8] did contain, however, a number of provisions dealing with miscellaneous aspects of the law of contracts as applied to contracts for the sale of securities. Section 8-107 [former 30-8-107] dealt with one remedy for breach, and Section 8-314 [former 30-8-314] dealt with certain aspects of performance. Revised Article 8 [Title 30, chapter 8] deletes these on the theory that inclusion of a few sections on issues of contract law is likely to cause more harm than good since inferences might be drawn from the failure to cover related issues. The deletion of these sections is not, however, intended as a rejection of the rules of contract law and interpretation that they expressed.

Prior Section 8-315 [former 30-8-315]. It is not entirely clear what the function of Section 8-315 [former 30-8-315] of prior law was. The section specified that the owner of a security could recover it from a person to whom it had been transferred, if the transferee did not qualify as a bona fide purchaser. It seems to have been intended only to recognize that securities, like any other form of personal property, are governed by the general principle of property law that an owner can recover property from a person to whom it has been transferred under circumstances that did not cut off the owner's claim. Although many other Articles of the UCC deal with cut-off rules, Article 8 [Title 30, chapter 8] was the only one that included an affirmative statement of the rights of an owner to recover her property. It seems wiser to adopt the same approach as in Articles 2, 3, 7, and 9 [Title 30, chapters 2, 3, 7, and 9A], and leave this point to other law. Accordingly, Section 8-315 [former 30-8-315] is deleted in Revised Article 8 [Title 30, chapter 8], without, of course, implying rejection of the nearly self-evident rule that it sought to express.

Prior Section 8-407 [former 30-8-407]. This section, entitled "Exchangeability of Securities," seemed to say that holders of securities had the right to cause issuers to convert them back and forth from certificated to uncertificated form. The provision, however, applied only if the issuer "regularly maintains a system for issuing the class of securities involved under which both certificated and uncertificated securities are regularly issued to the category of owners, which includes the person in whose name the new security is to be registered." The provision seems unnecessary, since it applied only if the issuer decided that it should. The matter can be covered by agreement or corporate charter or by-laws.

Chapter Compiler's Comments

Retroactivity of 1985 Amendments: The title of Ch. 80, L. 1985, amending sections 30-8-202, 30-8-205, 30-8-207, 30-8-309, 30-8-313, 30-8-319, and 30-8-405, read in part: "An act to generally revise Title 30, chapters 8 and 9 [now 9A], of Montana's codification of the Uniform Commercial

Code to conform with the intent of Chapter 402, Laws of 1983, which substantially adopted the 1972 and 1977 changes recommended by the Uniform Law Commissioners; . . . and providing an immediate effective date and retroactive application to the effective date of Chapter 402, Laws of 1983."

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Montana Compiler's Changes: Compiler has changed the Official Comments by changing "Article" to "Chapter" wherever it appears, and by prefacing section numbers with Title 30 so as to reflect Montana's codification of the U.C.C.

Part 1
Short Title and General Matters

30-8-101. Short title.

Official Comment

Purposes: This chapter sets forth certain rights and duties of the issuers of and the parties that deal with investment securities, both certificated and uncertificated. Unlike a corporation code, it does not set forth general rules defining property rights that accrue to holders of securities. And unlike a Blue Sky statute it does not set forth specific requirements for disclosing to the public the nature of the property interest that is the security. Rather it sets forth rules relative to the transfer of the rights that constitute securities and to the establishment of those rights against the issuer and other parties.

As is true with respect to all other Chapters of the Code, parties may by agreement create rights and duties between themselves that vary from those set forth in this Chapter. Section 30-1-102(3). But prejudice to the rights of those not party to the agreement is limited by Code provisions (e.g., Sections 30-8-313 and 30-8-321, both repealed) as well as by general legal principles that supplement the Code. See Section 30-1-103 and Comment 2 to Section 30-1-102.

This Chapter does not purport to determine whether a particular issue of securities should be represented by certificates, in whole or in part. That determination is left to the parties involved, subject to federal and state law.

Reasons for 1977 Change: Although the title of the Chapter has not been changed, its coverage has been broadened, by amendment to Section 30-8-102 [substance now in 30-8-112], to include both securities which are reified, i.e., represented by certificates or other instruments, and those which are not. The former are defined as "certificated securities" and constitute the entire subject matter of present Chapter 8. The latter are defined as "uncertificated securities" and are not now expressly covered by the Uniform Commercial Code. The revised Chapter is intended to govern the relationships, rights and duties of the issuers of and the parties that deal with both certificated and uncertificated securities to the same extent that present Chapter 8 governs such relationships, rights and duties with respect to certificated securities alone.

This Chapter does not purport to determine whether a particular issue of securities should be represented by certificates, in whole or in part. It is contemplated that such determination will be made by the issuer under appropriate state or federal law. It is further contemplated that a particular issue of securities may be partly certificated and partly uncertificated, in which event the determination will be at the option of the owner to the extent that the issuer permits.

The form of the Chapter has been disturbed as little as possible and each numbered section deals with the subject matter of the similarly numbered section of the present Chapter. Only four new sections, 30-8-108, 30-8-321, 30-8-407 and 30-8-408 [all repealed], have been added.

30-8-112. Definitions.

Official Comment

Source: Section 8-102, U.C.C.

Official Comment:

1. "Adverse claim." The definition of the term "adverse claim" has two components. First, the term refers only to property interests. Second, the term means not merely that a person has a property interest in a financial asset but that it is a violation of the claimant's property interest for the other person to hold or transfer the security or other financial asset.

The term adverse claim is not, of course, limited to ownership rights, but extends to other property interests established by other law. A security interest, for example, would be an adverse claim with respect to a transferee from the debtor since any effort by the secured party to enforce the security interest against the property would be an interference with the transferee's interest.

The definition of adverse claim in the prior version of Article 8 [Title 30, chapter 8] might have been read to suggest that any wrongful action concerning a security, even a simple breach of contract, gave rise to an adverse claim. Insofar as such cases as Fallon v. Wall Street Clearing Corp., 586 N.Y.S.2d 953, 182 A.D.2d 245, (1992) and Pentech Intl. v. Wall St. Clearing Co., 983 F.2d 441 (2d Cir.1993), were based on that view, they are rejected by the new definition which explicitly limits the term adverse claim to property interests. Suppose, for example, that A contracts to sell or deliver securities to B, but fails to do so and instead sells or pledges the securities to C. B, the promisee, has an action against A for breach of contract, but absent unusual circumstances the action for breach would not give rise to a property interest in the securities. Accordingly, B does not have an adverse claim. An adverse claim might, however, be based upon principles of equitable remedies that give rise to property claims. It would, for example, cover a right established by other law to rescind a transaction in which securities were transferred. Suppose, for example, that A holds securities and is induced by B's fraud to transfer them to B. Under the law of contract or restitution, A may have a right to rescind the transfer, which gives A a property claim to the securities. If so, A has an adverse claim to the securities in B's hands. By contrast, if B had committed no fraud, but had merely committed a breach of contract in connection with the transfer from A to B, A may have only a right to damages for breach, not a right to rescind. In that case, A would not have an adverse claim to the securities in B's hands.

2. "Bearer form." The definition of "bearer form" has remained substantially unchanged since the early drafts of the original version of Article 8 [Title 30, chapter 8]. The requirement that the certificate be payable to bearer by its terms rather than by an indorsement has the effect of preventing instruments governed by other law, such as chattel paper or Article 3 [Title 30, chapter 3] negotiable instruments, from being inadvertently swept into the Article 8 [Title 30, chapter 8] definition of security merely by virtue of blank indorsements. Although the other elements of the definition of security in Section 8-102(a)(14) [30-8-112(1)(o)] probably suffice for that purpose in any event, the language used in the prior version of Article 8 [Title 30, chapter 8] has been retained.

3. "Broker." Broker is defined by reference to the definitions of broker and dealer in the federal securities laws. The only difference is that banks, which are excluded from the federal securities law definition, are included in the Article 8 [Title 30, chapter 8] definition when they perform functions that would bring them within the federal securities law definition if it did not have the clause excluding banks. The definition covers both those who act as agents ("brokers" in securities parlance) and those who act as principals ("dealers" in securities parlance). Since the definition refers to persons "defined" as brokers or dealers under the federal securities law, rather than to persons required to "register" as brokers or dealers under the federal securities law, it covers not only registered brokers and dealers but also those exempt from the registration requirement, such as purely intrastate brokers. The only substantive rules that turn on the defined term broker are one provision of the section on warranties, Section 8-108(i) [30-8-118(9)], and the special perfection rule in Article 9 [Title 30, chapter 9A] for security interests granted by brokers, Section 9-115(4)(c) [30-9-115(4)(c), now repealed, see 30-9A-309].

4. "Certificated security." The term "certificated security" means a security that is represented by a security certificate.

5. "Clearing corporation." The definition of clearing corporation limits its application to entities that are subject to a rigorous regulatory framework. Accordingly, the definition includes only federal reserve banks, persons who are registered as "clearing agencies" under the federal securities laws (which impose a comprehensive system of regulation of the activities and rules of clearing agencies), and other entities subject to a comparable system of regulatory oversight.

6. "Communicate." The term "communicate" assures that the Article 8 [Title 30, chapter 8] rules will be sufficiently flexible to adapt to changes in information technology. Sending a signed writing always suffices as a communication, but the parties can agree that a different means of transmitting information is to be used. Agreement is defined in Section 1-201(3) [30-1-201(3)] as "the bargain of the parties in fact as found in their language or by implication from other circumstances including course of dealing or usage of trade or course of performance." Thus, use of an information transmission method might be found to be authorized by agreement, even though the parties have not explicitly so specified in a formal agreement. The term communicate is used in Sections 8-102(a)(7) [30-8-112(1)(h)] (definition of entitlement order), 8-102(a)(11) [30-8-112(1)(l)] (definition of instruction), and 8-403 [30-8-413] (demand that issuer not register transfer).

7. "Entitlement holder." This term designates those who hold financial assets through intermediaries in the indirect holding system. Because many of the rules of Part 5 [Title 30,

chapter 8, part 5] impose duties on securities intermediaries in favor of entitlement holders, the definition of entitlement holder is, in most cases, limited to the person specifically designated as such on the records of the intermediary. The last sentence of the definition covers the relatively unusual cases where a person may acquire a security entitlement under Section 8-501 [30-8-501] even though the person may not be specifically designated as an entitlement holder on the records of the securities intermediary.

A person may have an interest in a security entitlement, and may even have the right to give entitlement orders to the securities intermediary with respect to it, even though the person is not the entitlement holder. For example, a person who holds securities through a securities account in its own name may have given discretionary trading authority to another person, such as an investment adviser. Similarly, the control provisions in Section 8-106 [30-8-116] and the related provisions in Article 9 [Title 30, chapter 9A] are designed to facilitate transactions in which a person who holds securities through a securities account uses them as collateral in an arrangement where the securities intermediary has agreed that if the secured party so directs the intermediary will dispose of the positions. In such arrangements, the debtor remains the entitlement holder but has agreed that the secured party can initiate entitlement orders. Moreover, an entitlement holder may be acting for another person as a nominee, agent, trustee, or in another capacity. Unless the entitlement holder is itself acting as a securities intermediary for the other person, in which case the other person would be an entitlement holder with respect to the securities entitlement, the relationship between an entitlement holder and another person for whose benefit the entitlement holder holds a securities entitlement is governed by other law.

8. "Entitlement order." This term is defined as a notification communicated to a securities intermediary directing transfer or redemption of the financial asset to which an entitlement holder has a security entitlement. The term is used in the rules for the indirect holding system in a fashion analogous to the use of the terms "indorsement" and "instruction" in the rules for the direct holding system. If a person directly holds a certificated security in registered form and wishes to transfer it, the means of transfer is an indorsement. If a person directly holds an uncertificated security and wishes to transfer it, the means of transfer is an instruction. If a person holds a security entitlement, the means of disposition is an entitlement order. An entitlement order includes a direction under Section 8-508 [30-8-508] to the securities intermediary to transfer a financial asset to the account of the entitlement holder at another financial intermediary or to cause the financial asset to be transferred to the entitlement holder in the direct holding system (e.g., the delivery of a securities certificate registered in the name of the former entitlement holder). As noted in Comment 7, an entitlement order need not be initiated by the entitlement holder in order to be effective, so long as the entitlement holder has authorized the other party to initiate entitlement orders. See Section 8-107(b) [30-8-117(2)].

9. "Financial asset." The definition of "financial asset," in conjunction with the definition of "securities account" in Section 8-501 [30-8-501], sets the scope of the indirect holding system rules of Part 5 of Revised Article 8 [Title 30, chapter 8, part 5]. The Part 5 [Title 30, chapter 8, part 5] rules apply not only to securities held through intermediaries, but also to other financial assets held through intermediaries. The term financial asset is defined to include not only securities but also a broader category of obligations, shares, participations, and interests.

Having separate definitions of security and financial asset makes it possible to separate the question of the proper scope of the traditional Article 8 [Title 30, chapter 8] rules from the question of the proper scope of the new indirect holding system rules. Some forms of financial assets should be covered by the indirect holding system rules of Part 5 [Title 30, chapter 8, part 5], but not by the rules of Parts 2, 3, and 4 [Title 30, chapter 8, parts 2, 3, and 4]. The term financial asset is used to cover such property. Because the term security entitlement is defined in terms of financial assets rather than securities, the rules concerning security entitlements set out in Part 5 of Article 8 [Title 30, chapter 8, part 5] and in Revised Article 9 [Title 30, chapter 9A] apply to the broader class of financial assets.

The fact that something does or could fall within the definition of financial asset does not, without more, trigger Article 8 [Title 30, chapter 8] coverage. The indirect holding system rules of Revised Article 8 [Title 30, chapter 8] apply only if the financial asset is in fact held in a securities account, so that the interest of the person who holds the financial asset through the securities account is a security entitlement. Thus, questions of the scope of the indirect holding system rules cannot be framed as "Is such-and-such a 'financial asset' under Article 8 [Title 30, chapter 8]?" Rather, one must analyze whether the relationship between an institution and a person on whose behalf the institution holds an asset falls within the scope of the term securities account as defined in Section 8-501 [30-8-501]. That question turns in large measure on whether it makes sense to apply the Part 5 [Title 30, chapter 8, part 5] rules to the relationship.

The term financial asset is used to refer both to the underlying asset and the particular means by which ownership of that asset is evidenced. Thus, with respect to a certificated security, the term financial asset may, as context requires, refer either to the interest or obligation of the issuer or to the security certificate representing that interest or obligation. Similarly, if a person holds a security or other financial asset through a securities account, the term financial asset may, as context requires, refer either to the underlying asset or to the person's security entitlement.

10. "Good faith." Good faith is defined in Article 8 [Title 30, chapter 8] for purposes of the application to Article 8 [Title 30, chapter 8] of Section 1-203 [30-1-203], which provides that "Every contract or duty within this Act imposes an obligation of good faith in its performance or enforcement." The sole function of the good faith definition in Revised Article 8 [Title 30, chapter 8] is to give content to the Section 1-203 [30-1-203] obligation as it applies to contracts and duties that are governed by Article 8 [Title 30, chapter 8]. The standard is one of "reasonable commercial standards of fair dealing." The reference to commercial standards makes clear that assessments of conduct are to be made in light of the commercial setting. The substantive rules of Article 8 [Title 30, chapter 8] have been drafted to take account of the commercial circumstances of the securities holding and processing system. For example, Section 8-115 [30-8-125] provides that a securities intermediary acting on an effective entitlement order, or a broker or other agent acting as a conduit in a securities transaction, is not liable to an adverse claimant, unless the claimant obtained legal process or the intermediary acted in collusion with the wrongdoer. This, and other similar provisions, see Sections 8-404 and 8-503(e) [30-8-414 and 30-8-503(5)], do not depend on notice of adverse claims, because it would impair rather than advance the interest of investors in having a sound and efficient securities clearance and settlement system to require intermediaries to investigate the propriety of the transactions they are processing. The good faith obligation does not supplant the standards of conduct established in provisions of this kind.

In Revised Article 8 [Title 30, chapter 8], the definition of good faith is not germane to the question whether a purchaser takes free from adverse claims. The rules on such questions as whether a purchaser who takes in suspicious circumstances is disqualified from protected purchaser status are treated not as an aspect of good faith but directly in the rules of Section 8-105 [30-8-115] on notice of adverse claims.

11. "Indorsement" is defined as a signature made on a security certificate or separate document for purposes of transferring or redeeming the security. The definition is adapted from the language of Section 8-308(1) [former 30-8-308(1)] of the prior version and from the definition of indorsement in the Negotiable Instruments Article, see Section 3-204(a) [30-3-203(1)]. The definition of indorsement does not include the requirement that the signature be made by an appropriate person or be authorized. Those questions are treated in the separate substantive provision on whether the indorsement is effective, rather than in the definition of indorsement. See Section 8-107 [30-8-117].

12. "Instruction" is defined as a notification communicated to the issuer of an uncertificated security directing that transfer be registered or that the security be redeemed. Instructions are the analog for uncertificated securities of indorsements of certificated securities.

13. "Registered form." The definition of "registered form" is substantially the same as in the prior version of Article 8 [Title 30, chapter 8]. Like the definition of bearer form, it serves primarily to distinguish Article 8 [Title 30, chapter 8] securities from instruments governed by other law, such as Article 3 [Title 30, chapter 3].

Contrary to the holding in Highland Capital Management LP v. Schneider, 8 N.Y.3d 406 (2007), the registrability requirement in the definition of "registered form," and its parallel in the definition of "security," are satisfied only if books are maintained by or on behalf of the issuer for the purpose of registration of transfer, including the determination of rights under Section 8-207(a) [30-8-217(1)] (or if, in the case of a certificated security, the security certificate so states). It is not sufficient that the issuer records ownership, or records transfers thereof, for other purposes. Nor is it sufficient that the issuer, while not in fact maintaining books for the purpose of registration of transfer, could do so, for such is always the case.

14. "Securities intermediary." A "securities intermediary" is a person that in the ordinary course of its business maintains securities accounts for others and is acting in that capacity. The most common examples of securities intermediaries would be clearing corporations holding securities for their participants, banks acting as securities custodians, and brokers holding securities on behalf of their customers. Clearing corporations are listed separately as a category of securities intermediary in subparagraph (i) [subsection (1)(n)(i)] even though in

most circumstances they would fall within the general definition in subparagraph (ii) [subsection (1)(n)(ii)]. The reason is to simplify the analysis of arrangements such as the NSCCDTC system in which NSCC performs the comparison, clearance, and netting function, while DTC acts as the depository. Because NSCC is a registered clearing agency under the federal securities laws, it is a clearing corporation and hence a securities intermediary under Article 8 [Title 30, chapter 8], regardless of whether it is at any particular time or in any particular aspect of its operations holding securities on behalf of its participants.

The terms securities intermediary and broker have different meanings. Broker means a person engaged in the business of buying and selling securities, as agent for others or as principal. Securities intermediary means a person maintaining securities accounts for others. A stockbroker, in the colloquial sense, may or may not be acting as a securities intermediary.

The definition of securities intermediary includes the requirement that the person in question is "acting in the capacity" of maintaining securities accounts for others. This is to take account of the fact that a particular entity, such as a bank, may act in many different capacities in securities transactions. A bank may act as a transfer agent for issuers, as a securities custodian for institutional investors and private investors, as a dealer in government securities, as a lender taking securities as collateral, and as a provider of general payment and collection services that might be used in connection with securities transactions. A bank that maintains securities accounts for its customers would be a securities intermediary with respect to those accounts; but if it takes a pledge of securities from a borrower to secure a loan, it is not thereby acting as a securities intermediary with respect to the pledged securities, since it holds them for its own account rather than for a customer. In other circumstances, those two functions might be combined. For example, if the bank is a government securities dealer it may maintain securities accounts for customers and also provide the customers with margin credit to purchase or carry the securities, in much the same way that brokers provide margin loans to their customers.

15. "Security." The definition of "security" has three components. First, there is the subparagraph (i) [subsection (1)(o)(i)] test that the interest or obligation be fully transferable, in the sense that the issuer either maintains transfer books or the obligation or interest is represented by a certificate in bearer or registered form. Second, there is the subparagraph (ii) [subsection (1)(o)(ii)] test that the interest or obligation be divisible, that is, one of a class or series, as distinguished from individual obligations of the sort governed by ordinary contract law or by Article 3 [Title 30, chapter 3]. Third, there is the subparagraph (iii) [subsection (1)(o)(iii)] functional test, which generally turns on whether the interest or obligation is, or is of a type, dealt in or traded on securities markets or securities exchanges. There is, however, an "opt-in" provision in subparagraph (iii) [subsection (1)(o)(iii)] which permits the issuer of any interest or obligation that is "a medium of investment" to specify that it is a security governed by Article 8 [Title 30, chapter 8].

The divisibility test of subparagraph (ii) [subsection (1)(o)(ii)] applies to the security—that is, the underlying intangible interest—not the means by which that interest is evidenced. Thus, securities issued in book-entry only form meet the divisibility test because the underlying intangible interest is divisible via the mechanism of the indirect holding system. This is so even though the clearing corporation is the only eligible direct holder of the security.

The third component, the functional test in subparagraph (iii) [subsection (1)(o)(iii)], provides flexibility while ensuring that the Article 8 [Title 30, chapter 8] rules do not apply to interests or obligations in circumstances so unconnected with the securities markets that parties are unlikely to have thought of the possibility that Article 8 [Title 30, chapter 8] might apply. Subparagraph (iii)(A) [subsection (1)(o)(iii)(A)] covers interests or obligations that either are dealt in or traded on securities exchanges or securities markets, or are of a type dealt in or traded on securities exchanges or securities markets. The "is dealt in or traded on" phrase eliminates problems in the characterization of new forms of securities which are to be traded in the markets, even though no similar type has previously been dealt in or traded in the markets. Subparagraph (iii)(B) [subsection (1)(o)(ii)(B)] covers the broader category of media for investment, but it applies only if the terms of the interest or obligation specify that it is an Article 8 [Title 30, chapter 8] security. This opt-in provision allows for deliberate expansion of the scope of Article 8 [Title 30, chapter 8].

Section 8-103 [30-8-113] contains additional rules on the treatment of particular interests as securities or financial assets.

16. "Security certificate." The term "security" refers to the underlying asset, e.g., 1000 shares of common stock of Acme, Inc. The term "security certificate" refers to the paper certificates that have traditionally been used to embody the underlying intangible interest.

17. "Security entitlement" means the rights and property interest of a person who holds securities or other financial assets through a securities intermediary. A security entitlement is both a package of personal rights against the securities intermediary and an interest in the property held by the securities intermediary. A security entitlement is not, however, a specific property interest in any financial asset held by the securities intermediary or by the clearing corporation through which the securities intermediary holds the financial asset. See Sections 8-104(c) and 8-503 [30-8-114(3) and 30-8-503]. The formal definition of security entitlement set out in subsection (a)(16)[(1)(q)] of this section is a cross-reference to the rules of Part 5 [Title 30, chapter 8, part 5]. In a sense, then, the entirety of Part 5 [Title 30, chapter 8, part 5] is the definition of security entitlement. The Part 5 [Title 30, chapter 8, part 5] rules specify the rights and property interest that comprise a security entitlement.

18. "Uncertificated security." The term "uncertificated security" means a security that is not represented by a security certificate. For uncertificated securities, there is no need to draw any distinction between the underlying asset and the means by which a direct holder's interest in that asset is evidenced. Compare "certificated security" and "security certificate."

30-8-113. Rules for determining whether certain obligations and interests are securities or financial assets.

Official Comment

[*Corresponding U.C.C. Section:* Section 8-103, U.C.C.]

Source: Section 8-103, U.C.C.

Official Comment:

1. This section contains rules that supplement the definitions of "financial asset" and "security" in Section 8-102 [30-8-112]. The Section 8-102 [30-8-112] definitions are worded in general terms, because they must be sufficiently comprehensive and flexible to cover the wide variety of investment products that now exist or may develop. The rules in this section are intended to foreclose interpretive issues concerning the application of the general definitions to several specific investment products. No implication is made about the application of the Section 8-102 [30-8-112] definitions to investment products not covered by this section.

2. Subsection (a) [subsection (1)] establishes an unconditional rule that ordinary corporate stock is a security. That is so whether or not the particular issue is dealt in or traded on securities exchanges or in securities markets. Thus, shares of closely held corporations are Article 8 [Title 30, chapter 8] securities.

3. Subsection (b) [subsection (2)] establishes that the Article 8 [Title 30, chapter 8] term "security" includes the various forms of the investment vehicles offered to the public by investment companies registered as such under the federal Investment Company Act of 1940, as amended. This clarification is prompted principally by the fact that the typical transaction in shares of open-end investment companies is an issuance or redemption, rather than a transfer of shares from one person to another as is the case with ordinary corporate stock. For similar reasons, the definitions of indorsement, instruction, and entitlement order in Section 8-102 [30-8-112] refer to "redemptions" as well as "transfers," to ensure that the Article 8 [Title 30, chapter 8] rules on such matters as signature guaranties, Section 8-306 [30-8-336], assurances, Sections 8-402 and 8-507 [30-8-412 and 30-8-507], and effectiveness, Section 8-107 [30-8-117], apply to directions to redeem mutual fund shares. The exclusion of insurance products is needed because some insurance company separate accounts are registered under the Investment Company Act of 1940, but these are not traded under the usual Article 8 [Title 30, chapter 8] mechanics.

4. Subsection (c) [subsection (3)] is designed to foreclose interpretive questions that might otherwise be raised by the application of the "of a type" language of Section 8-102(a)(15)(iii) [30-8-112(1)(o)(iii)] to partnership interests. Subsection (c) [subsection (3)] establishes the general rule that partnership interests or shares of limited liability companies are not Article 8 [Title 30, chapter 8] securities unless they are in fact dealt in or traded on securities exchanges or in securities markets. The issuer, however, may explicitly "opt-in" by specifying that the interests or shares are securities governed by Article 8 [Title 30, chapter 8]. Partnership interests or shares of limited liability companies are included in the broader term "financial asset." Thus, if they are held through a securities account, the indirect holding system rules of Part 5 [Title 30, chapter 8, part 5] apply, and the interest of a person who holds them through such an account is a security entitlement.

5. Subsection (d) [subsection (4)] deals with the line between Article 3 [Title 30, chapter 3] negotiable instruments and Article 8 [Title 30, chapter 8] investment securities. It continues the rule of the prior version of Article 8 [Title 30, chapter 8] that a writing that meets the

Article 8 [Title 30, chapter 8] definition is covered by Article 8 [Title 30, chapter 8] rather than Article 3 [Title 30, chapter 3], even though it also meets the definition of negotiable instrument. However, subsection (d) [subsection (4)] provides that an Article 3 [Title 30, chapter 3] negotiable instrument is a "financial asset" so that the indirect holding system rules apply if the instrument is held through a securities intermediary. This facilitates making items such as money market instruments eligible for deposit in clearing corporations.

6. Subsection (e) [subsection (5)] is included to clarify the treatment of investment products such as traded stock options, which are treated as financial assets but not securities. Thus, the indirect holding system rules of Part 5 [Title 30, chapter 8, part 5] apply, but the direct holding system rules of Parts 2, 3, and 4 [Title 30, chapter 8, parts 2, 3, and 4] do not.

7. Subsection (f) [subsection (6)] excludes commodity contracts from all of Article 8 [Title 30, chapter 8]. However, the Article 9 [Title 30, chapter 9A] rules on security interests in investment property do apply to security interests in commodity positions. See Section 9-115 [30-9-115, now repealed, see 30-9A-102] and Comment 8 thereto. "Commodity contract" is defined in Section 9-115 [30-9-115, now repealed, see 30-9A-102].

8. Subsection (g) [subsection (7)] allows a document of title to be a financial asset and thus subject to the indirect holding system rules of Part 5 [Title 30, chapter 8, part 5] only to the extent that the intermediary and the person entitled under the document agree to do so. This is to prevent the inadvertent application of the Part 5 [Title 30, chapter 8, part 5] rules to intermediaries who may hold either electronic or tangible documents of title.

Compiler's Comments

2005 Amendment: Chapter 575 inserted (7) relating to a document of title. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

1999 Amendment: Chapter 305 in (6) substituted "30-9-122" (renumbered 30-9A-102) for "30-9-115". Amendment effective July 1, 2001.

Case Notes

Annuity Contract Considered Investment, Not Life Insurance: Miles invested $30,000 in a tax-deferred variable annuity contract. After Mile's death, the plaintiffs demanded one-half of the annuity investment on grounds that the annuity was life insurance that they were entitled to under Miles' will. The District Court denied their demand, holding that the annuity contract did not constitute insurance under Montana law. On appeal, the heirs cited In re Fligman's Estate, 113 M 505, 129 P2d 627 (1942), for the proposition that because annuity contracts were considered insurance for inheritance tax purposes in that case, it followed that annuity contracts have to be considered insurance for all purposes. The Supreme Court held that because the annuity contract in Miles' case did not involve indemnification, loss, damage, liability, or contingent events, it was an investment, not insurance, and the District Court did not err in so holding. In re Estate of Miles v. Miles, 2000 MT 41, 298 M 312, 994 P2d 1139, 57 St. Rep. 191 (2000).

30-8-114. Acquisition of security or financial asset or interest therein.

Official Comment

Source: Section 8-104, U.C.C.

Official Comment:

1. This section lists the ways in which interests in securities and other financial assets are acquired under Article 8 [Title 30, chapter 8]. In that sense, it describes the scope of Article 8 [Title 30, chapter 8]. Subsection (a) [subsection (1)] describes the two ways that a person may acquire a security or interest therein under this Article [chapter]: (1) by delivery (Section 8-301 [30-8-331]), and (2) by acquiring a security entitlement. Each of these methods is described in detail in the relevant substantive provisions of this Article [chapter]. Part 3 [Title 30, chapter 8, part 3], beginning with the definition of "delivery" in Section 8-301 [30-8-331], describes how interests in securities are acquired in the direct holding system. Part 5 [Title 30, chapter 8, part 5], beginning with the rules of Section 8-501 [30-8-501] on how security entitlements are acquired, describes how interests in securities are acquired in the indirect holding system.

Subsection (b) [subsection (2)] specifies how a person may acquire an interest under Article 8 [Title 30, chapter 8] in a financial asset other than a security. This Article [chapter] deals with financial assets other than securities only insofar as they are held in the indirect holding system. For example, a bankers' acceptance falls within the definition of "financial asset," so if it is held through a securities account the entitlement holder's right to it is a security entitlement governed by Part 5 [Title 30, chapter 8, part 5]. The bankers' acceptance itself, however, is a negotiable instrument governed by Article 3 [Title 30, chapter 3], not by Article 8 [Title 30, chapter 8]. Thus, the provisions of Parts 2, 3, and 4 of this Article [Title 30, chapter 8, parts 2, 3, and 4] that deal with the rights of direct holders of securities are not applicable. Article 3 [Title 30, chapter 3], not Article 8 [Title 30, chapter 8], specifies how one acquires a direct interest in a bankers' acceptance. If a bankers' acceptance is delivered to a clearing corporation to be held for the account of the clearing corporation's participants, the clearing corporation becomes the holder of the bankers' acceptance under the Article 3 [Title 30, chapter 3] rules specifying how negotiable instruments are transferred. The rights of the clearing corporation's participants, however, are governed by Part 5 of this Article [Title 30, chapter 8, part 5].

2. The distinction in usage in Article 8 [Title 30, chapter 8] between the term "security" (and its correlatives "security certificate" and "uncertificated security") on the one hand, and "security entitlement" on the other, corresponds to the distinction between the direct and indirect holding systems. For example, with respect to certificated securities that can be held either directly or through intermediaries, obtaining possession of a security certificate and acquiring a security entitlement are both means of holding the underlying security. For many other purposes, there is no need to draw a distinction between the means of holding. For purposes of commercial law analysis, however, the form of holding may make a difference. Where an item of property can be held in different ways, the rules on how one deals with it, including how one transfers it or how one grants a security interest in it, differ depending on the form of holding.

Although a security entitlement is means of holding the underlying security or other financial asset, a person who has a security entitlement does not have any direct claim to a specific asset in the possession of the securities intermediary. Subsection (c) [subsection (3)] provides explicitly that a person who acquires a security entitlement is a "purchaser" of any security, security entitlement, or other financial asset held by the securities intermediary only in the sense that under Section 8-503 [30-8-503] a security entitlement is treated as a *sui generis* form of property interest.

3. Subsection (d) [subsection (4)] is designed to ensure that parties will retain their expected legal rights and duties under Revised Article 8 [Title 30, chapter 8]. One of the major changes made by the revision is that the rules for the indirect holding system are stated in terms of the "security entitlements" held by investors, rather than speaking of them as holding direct interests in securities. Subsection (d) [subsection (4)] is designed as a translation rule to eliminate problems of co-ordination of terminology, and facilitate the continued use of systems for the efficient handling of securities and financial assets through securities intermediaries and clearing corporations. The efficiencies of a securities intermediary or clearing corporation are, in part, dependent on the ability to transfer securities credited to securities accounts in the intermediary or clearing corporation to the account of an issuer, its agent, or other person by book entry in a manner that permits exchanges, redemptions, conversions, and other transactions (which may be governed by pre-existing or new agreements, constitutional documents, or other instruments) to occur and to avoid the need to withdraw from immobilization in an intermediary or clearing corporation physical securities in order to deliver them for such purposes. Existing corporate charters, indentures and like documents may require the "presentation," "surrender," "delivery," or "transfer" of securities or security certificates for purposes of exchange, redemption, conversion or other reason. Likewise, documents may use a wide variety of terminology to describe, in the context for example of a tender or exchange offer, the means of putting the offeror or the issuer or its agent in possession of the security. Subsection (d) [subsection (4)] takes the place of provisions of prior law which could be used to reach the legal conclusion that book-entry transfers are equivalent to physical delivery to the person to whose account the book entry is credited.

30-8-115. Notice of adverse claim.

Official Comment

Source: Section 8-105, U.C.C.

Official Comment:

1. The rules specifying whether adverse claims can be asserted against persons who acquire securities or security entitlements, Sections 8-303, 8-502, and 8-510 [30-8-333, 30-8-502, and

30-8-510], provide that one is protected against an adverse claim only if one takes without notice of the claim. This section defines notice of an adverse claim.

The general Article 1 [Title 30, chapter 1] definition of "notice" in Section 1-201(25) [30-1-201(25)] which provides that a person has notice of a fact if "from all the facts and circumstances known to him at the time in question he has reason to know that it exists"does not apply to the interpretation of "notice of adverse claims." The Section 1-201(25) [30-1-201(25)] definition of "notice" does, however, apply to usages of that term and its cognates in Article 8 [Title 30, chapter 8] in contexts other than notice of adverse claims.

2. This section must be interpreted in light of the definition of "adverse claim" in Section 8-102(a)(1) [30-8-112(1)(a)]. "Adverse claim" does not include all circumstances in which a third party has a property interest in securities, but only those situations where a security is transferred in violation of the claimant's property interest. Therefore, awareness that someone other than the transferor has a property interest is not notice of an adverse claim. The transferee must be aware that the transfer violates the other party's property interest. If A holds securities in which B has some form of property interest, and A transfers the securities to C, C may know that B has an interest, but infer that A is acting in accordance with A's obligations to B. The mere fact that C knew that B had a property interest does not mean that C had notice of an adverse claim. Whether C had notice of an adverse claim depends on whether C had sufficient awareness that A was acting in violation of B's property rights. The rule in subsection (b) [subsection (2)] is a particularization of this general principle.

3. Paragraph (a)(1) [subsection (1)(a)] provides that a person has notice of an adverse claim if the person has knowledge of the adverse claim. Knowledge is defined in Section 1-201(25) [30-1-201(25)] as actual knowledge.

4. Paragraph (a)(2) [subsection (1)(b)] provides that a person has notice of an adverse claim if the person is aware of a significant probability that an adverse claim exists and deliberately avoids information that might establish the existence of the adverse claim. This is intended to codify the "willful blindness" test that has been applied in such cases. See May v. Chapman, 16 M. & W. 355, 153 Eng.Rep. 1225 (1847); Goodman v. Simonds, 61 U.S. 343 (1857).

The first prong of the willful blindness test of paragraph (a)(2) [subsection (1)(b)] turns on whether the person is aware facts sufficient to indicate that there is a significant probability that an adverse claim exists. The "awareness" aspect necessarily turns on the actor's state of mind. Whether facts known to a person make the person aware of a "significant probability" that an adverse claim exists turns on facts about the world and the conclusions that would be drawn from those facts, taking account of the experience and position of the person in question. A particular set of facts might indicate a significant probability of an adverse claim to a professional with considerable experience in the usual methods and procedures by which securities transactions are conducted, even though the same facts would not indicate a significant probability of an adverse claim to a non-professional.

The second prong of the willful blindness test of paragraph (a)(2) [subsection (1)(b)] turns on whether the person "deliberately avoids information" that would establish the existence of the adverse claim. The test is the character of the person's response to the information the person has. The question is whether the person deliberately failed to seek further information because of concern that suspicions would be confirmed.

Application of the "deliberate avoidance" test to a transaction by an organization focuses on the knowledge and the actions of the individual or individuals conducting the transaction on behalf of the organization. Thus, an organization that purchases a security is not willfully blind to an adverse claim unless the officers or agents who conducted that purchase transaction are willfully blind to the adverse claim. Under the two prongs of the willful blindness test, the individual or individuals conducting a transaction must know of facts indicating a substantial probability that the adverse claim exists and deliberately fail to seek further information that might confirm or refute the indication. For this purpose, information known to individuals within an organization who are not conducting or aware of a transaction, but not forwarded to the individuals conducting the transaction, is not pertinent in determining whether the individuals conducting the transaction had knowledge of a substantial probability of the existence of the adverse claim. Cf. Section 1-201(27) [30-1-201(27)]. An organization may also "deliberately avoid information" if it acts to preclude or inhibit transmission of pertinent information to those individuals responsible for the conduct of purchase transactions.

5. Paragraph (a)(3) [subsection (1)(c)] provides that a person has notice of an adverse claim if the person would have learned of the adverse claim by conducting an investigation that is required by other statute or regulation. This rule applies only if there is some other statute or

regulation that explicitly requires persons dealing with securities to conduct some investigation. The federal securities laws require that brokers and banks, in certain specified circumstances, check with a stolen securities registry to determine whether securities offered for sale or pledge have been reported as stolen. If securities that were listed as stolen in the registry are taken by an institution that failed to comply with requirement to check the registry, the institution would be held to have notice of the fact that they were stolen under paragraph (a)(3) [subsection (1)(c)]. Accordingly, the institution could not qualify as a protected purchaser under Section 8-303 [30-8-333]. The same result has been reached under the prior version of Article 8 [Title 30, chapter 8]. See First Nat'l Bank of Cicero v. Lewco Securities, 860 F.2d 1407 (7th Cir.1988).

6. Subsection (b) [subsection (2)] provides explicitly for some situations involving purchase from one described or identifiable as a representative. Knowledge of the existence of the representative relation is not enough in itself to constitute "notice of an adverse claim" that would disqualify the purchaser from protected purchaser status. A purchaser may take a security on the inference that the representative is acting properly. Knowledge that a security is being transferred to an individual account of the representative or that the proceeds of the transaction will be paid into that account is not sufficient to constitute "notice of an adverse claim," but knowledge that the proceeds will be applied to the personal indebtedness of the representative is. See State Bank of Binghamton v. Bache, 162 Misc. 128, 293 N.Y.S. 667 (1937).

7. Subsection (c) [subsection (3)] specifies whether a purchaser of a "stale" security is charged with notice of adverse claims, and therefore disqualified from protected purchaser status under Section 8-303 [30-8-333]. The fact of "staleness" is viewed as notice of certain defects after the lapse of stated periods, but the maturity of the security does not operate automatically to affect holders' rights. The periods of time here stated are shorter than those appearing in the provisions of this Article [chapter] on staleness as notice of defects or defenses of an issuer (Section 8-203 [30-8-213]) since a purchaser who takes a security after funds or other securities are available for its redemption has more reason to suspect claims of ownership than issuer's defenses. An owner will normally turn in a security rather than transfer it at such a time. Of itself, a default never constitutes notice of a possible adverse claim. To provide otherwise would not tend to drive defaulted securities home and would serve only to disrupt current financial markets where many defaulted securities are actively traded. Unpaid or overdue coupons attached to a bond do not bring it within the operation of this subsection, though they may be relevant under the general test of notice of adverse claims in subsection (a) [subsection (1)].

8. Subsection (d) [subsection (4)] provides the owner of a certificated security with a means of protection while a security certificate is being sent in for redemption or exchange. The owner may endorse it "for collection" or "for surrender," and this constitutes notice of the owner's claims, under subsection (d) [subsection (4)].

30-8-116. Control.

Official Comment

Source: Section 8-106, U.C.C.

Official Comment:

1. The concept of "control" plays a key role in various provisions dealing with the rights of purchasers, including secured parties. See Sections 8-303 [30-8-333] (protected purchasers); 8-503(e) [30-8-503(5)] (purchasers from securities intermediaries); 8-510 [30-8-510] (purchasers of security entitlements from entitlement holders); 9-314 [30-9A-314] (perfection of security interests); 9-328 [30-9A-328] (priorities among conflicting security interests).

Obtaining "control" means that the purchaser has taken whatever steps are necessary, given the manner in which the securities are held, to place itself in a position where it can have the securities sold, without further action by the owner.

2. Subsection (a) [subsection (1)] provides that a purchaser obtains "control" with respect to a certificated security in bearer form by taking "delivery," as defined in Section 8-301 [30-8-331]. Subsection (b) [subsection (2)] provides that a purchaser obtains "control" with respect to a certificated security in registered form by taking "delivery," as defined in Section 8-301 [30-8-331], provided that the security certificate has been indorsed to the purchaser or in blank. Section 8-301 [30-8-331] provides that delivery of a certificated security occurs when the purchaser obtains possession of the security certificate, or when an agent for the purchaser (other than a securities intermediary) either acquires possession or acknowledges that the agent holds for the purchaser.

3. Subsection (c) [subsection (3)] specifies the means by which a purchaser can obtain control over uncertificated securities which the transferor holds directly. Two mechanisms are possible.

Under subsection (c)(1) [subsection (3)(a)], securities can be "delivered" to a purchaser. Section 8-301(b) [30-8-331(2)] provides that "delivery" of an uncertificated security occurs when the purchaser becomes the registered holder. So far as the issuer is concerned, the purchaser would then be entitled to exercise all rights of ownership. See Section 8-207 [30-8-217]. As between the parties to a purchase transaction, however, the rights of the purchaser are determined by their contract. Cf. Section 9-202 [30-9-202, now repealed, see 30-9A-202]. Arrangements covered by this paragraph are analogous to arrangements in which bearer certificates are delivered to a secured party—so far as the issuer or any other parties are concerned, the secured party appears to be the outright owner, although it is in fact holding as collateral property that belongs to the debtor.

Under subsection (c)(2) [subsection (3)(b)], a purchaser has control if the issuer has agreed to act on the instructions of the purchaser, even though the owner remains listed as the registered owner. The issuer, of course, would be acting wrongfully against the registered owner if it entered into such an agreement without the consent of the registered owner. Subsection (g) [subsection (7)] makes this point explicit. The subsection (c)(2) [subsection (3)(b)] provision makes it possible for issuers to offer a service akin to the registered pledge device of the 1978 version of Article 8 [Title 30, chapter 8], without mandating that all issuers offer that service.

4. Subsection (d) [subsection (4)] specifies the means by which a purchaser can obtain control of a security entitlement. Three mechanisms are possible, analogous to those provided in subsection (c) [subsection (3)] for uncertificated securities. Under subsection (d)(1) [subsection (4)(a)], a purchaser has control if it is the entitlement holder. This subsection would apply whether the purchaser holds through the same intermediary that the debtor used, or has the securities position transferred to its own intermediary.

Subsection (d)(2) [subsection (4)(b)] provides that a purchaser has control if the securities intermediary has agreed to act on entitlement orders originated by the purchaser if no further consent by the entitlement holder is required. Under subsection (d)(2) [subsection (4)(b)], control may be achieved even though the original entitlement holder remains as the entitlement holder. Finally, a purchaser may obtain control under subsection (d)(3) [subsection (4)(c]) if another person has control and the person acknowledges that it has control on the purchaser's behalf. Control under subsection (d)(3) [subsection (4)(c)] parallels the delivery of certificated securities and uncertificated securities under Section 8-301 [30-8-331]. Of course, the acknowledging person cannot be the debtor.

This section specifies only the minimum requirements that such an arrangement must meet to confer "control"; the details of the arrangement can be specified by agreement. The arrangement might cover all of the positions in a particular account or subaccount, or only specified positions. There is no requirement that the control party's right to give entitlement orders be exclusive. The arrangement might provide that only the control party can give entitlement orders, or that either the entitlement holder or the control party can give entitlement orders. See subsection (f) [subsection (6)].

The following examples illustrate the application of subsection (d) [subsection (4)]:

Example 1. Debtor grants Alpha Bank a security interest in a security entitlement that includes 1000 shares of XYZ Co. stock that Debtor holds through an account with Able & Co. Alpha also has an account with Able. Debtor instructs Able to transfer the shares to Alpha, and Able does so by crediting the shares to Alpha's account. Alpha has control of the 1000 shares under subsection (d)(1) [subsection (4)(a)]. Although Debtor may have become the beneficial owner of the new securities entitlement, as between Debtor and Alpha, Able has agreed to act on Alpha's entitlement orders because, as between Able and Alpha Alpha has become the entitlement holder. See Section 8-506 [30-8-506].

Example 2. Debtor grants Alpha Bank a security interest in a security entitlement that includes 1000 shares of XYZ Co. stock that Debtor holds through an account with Able & Co. Alpha does not have an account with Able. Alpha uses Beta Bank as its securities custodian. Debtor instructs Able to transfer the shares to Beta Bank, for the account of Alpha, and Able does so. Alpha has control of the 1000 shares under subsection (d)(1) [subsection (4)(a)]. As in Example 1, although Debtor may have become the beneficial owner of the new securities entitlement, as between Debtor and Alpha, Beta has agree to act on Alpha's entitlement orders because, as between Beta and Alpha, Alpha has become the entitlement holder.

Example 3. Debtor grants Alpha Bank a security interest in a security entitlement that includes 1000 shares of XYZ Co. stock that Debtor holds through an account with Able & Co. Debtor, Able, and Alpha enter into an agreement under which Debtor will continue to receive dividends and distributions, and will continue to have the right to direct dispositions, but Alpha also has the right to direct dispositions. Alpha has control of the 1000 shares under subsection (d)(2) [subsection (4)(b)].

Example 4. Able & Co., a securities dealer, grants Alpha Bank a security interest in a security entitlement that includes 1000 shares of XYZ Co. stock that Able holds through an account with Clearing Corporation. Able causes Clearing Corporation to transfer the shares into Alpha's account at Clearing Corporation. As in Example 1, Alpha has control of the 1000 shares under subsection (d)(1) [subsection (4)(a)].

Example 5. Able & Co., a securities dealer, grants Alpha Bank a security interest in a security entitlement that includes 1000 shares of XYZ Co. stock that Able holds through an account with Clearing Corporation. Alpha does not have an account with Clearing Corporation. It holds its securities through Beta Bank, which does have an account with Clearing Corporation. Able causes Clearing Corporation to transfer the shares into Beta's account at Clearing Corporation. Beta credits the position to Alpha account with Beta. As in Example 2, Alpha has control of the 1000 shares under subsection (d)(1) [subsection (4)(a)].

Example 6. Able & Co. a securities dealer, grants Alpha Bank a security interest in a security entitlement that includes 1000 shares of XYZ Co. stock that Able holds through an account with Clearing Corporation. Able causes Clearing Corporation to transfer the shares into a pledge account, pursuant to an agreement under which Able will continue to receive dividends, distributions, and the like, but Alpha has the right to direct dispositions. As in Example 3, Alpha has control of the 1000 shares under subsection (d)(2) [subsection (4)(b)].

Example 7. Able & Co. a securities dealer, grants Alpha Bank a security interest in a security entitlement that includes 1000 shares of XYZ Co. stock that Able holds through an account with Clearing Corporation. Able, Alpha, and Clearing Corporation enter into an agreement under which Clearing Corporation will act on instructions from Alpha with respect to the XYZ Co. stock carried in Able's account, but Able will continue to receive dividends, distributions, and the like, and will also have the right to direct dispositions. As in Example 3, Alpha has control of the 1000 shares under subsection (d)(2) [subsection (4)(b)].

Example 8. Able & Co. a securities dealer, holds a wide range of securities through its account at Clearing Corporation. Able enters into an arrangement with Alpha Bank pursuant to which Alpha provides financing to Able secured by securities identified as the collateral on lists provided by Able to Alpha on a daily or other periodic basis. Able, Alpha, and Clearing Corporation enter into an agreement under which Clearing Corporation agrees that if at any time Alpha directs Clearing Corporation to do so, Clearing Corporation will transfer any securities from Able's account at Alpha's instructions. Because Clearing Corporation has agreed to act on Alpha's instructions with respect to any securities carried in Able's account, at the moment that Alpha's security interest attaches to securities listed by Able, Alpha obtains control of those securities under subsection (d)(2) [subsection (4)(b)]. There is no requirement that Clearing Corporation be informed of which securities Able has pledged to Alpha.

Example 9. Debtor grants Alpha Bank a security interest in a security entitlement that includes 1000 shares of XYZ Co. stock that Debtor holds through an account with Able & Co. Beta Bank agrees with Alpha to act as Alpha's collateral agent with respect to the security entitlement. Debtor, Able, and Beta enter into an agreement under which Debtor will continue to receive dividends and distributions, and will continue to have the right to direct dispositions, but Beta also has the right to direct dispositions. Because Able has agreed that it will comply with entitlement orders originated by Beta without further consent by Debtor, Beta has control of the security entitlement (see Example 3). Because Beta has control on behalf of Alpha, Alpha also has control under subsection (d)(3) [subsection (4)(c)]. It is not necessary for Able to enter into an agreement directly with Alpha or for Able to be aware of Beta's agency relationship with Alpha.

5. For a purchaser to have "control" under subsection (c)(2) or (d)(2) [subsection (3)(b) or (4)(b)] it is essential that the issuer or securities intermediary, as the case may be, actually be a party to the agreement. If a debtor gives a secured party a power of attorney authorizing the secured party to act in the name of the debtor, but the issuer or securities intermediary does not specifically agree to this arrangement, the secured party does not have "control" within the meaning of subsection (c)(2) or (d)(2) [subsection (3)(b) or (4)(b)] because the issuer or securities intermediary is not a party to the agreement. The secured party does not have control under subsection (c)(1) or (d)(1) [subsection (3)(a) or (4)(a)] because, although the power of attorney might give the secured party authority to act on the debtor's behalf as an agent, the secured party has not actually become the registered owner or entitlement holder.

6. Subsection (e) [subsection (5)] provides that if an interest in a security entitlement is granted by an entitlement holder to the securities intermediary through which the security entitlement is maintained, the securities intermediary has control. A common transaction covered by this provision is a margin loan from a broker to its customer.

7. The term "control" is used in a particular defined sense. The requirements for obtaining control are set out in this section. The concept is not to be interpreted by reference to similar concepts in other bodies of law. In particular, the requirements for "possession" derived from the common law of pledge are not to be used as a basis for interpreting subsection (c)(2) or (d)(2) [subsection (3)(b) or (4)(b)]. Those provisions are designed to supplant the concepts of "constructive possession" and the like. A principal purpose of the "control" concept is to eliminate the uncertainty and confusion that results from attempting to apply common law possession concepts to modern securities holding practices.

The key to the control concept is that the purchaser has the ability to have the securities sold or transferred without further action by the transferor. There is no requirement that the powers held by the purchaser be exclusive. For example, in a secured lending arrangement, if the secured party wishes, it can allow the debtor to retain the right to make substitutions, to direct the disposition of the uncertificated security or security entitlement, or otherwise to give instructions or entitlement orders. (As explained in Section 8-102 [30-8-112], Comment 8, an entitlement order includes a direction under Section 8-508 [30-8-508] to the securities intermediary to transfer a financial asset to the account of the entitlement holder at another financial intermediary or to cause the financial asset to be transferred to the entitlement holder in the direct holding system (e.g., by delivery of a securities certificate registered in the name of the former entitlement holder).) Subsection (f) [subsection (6)] is included to make clear the general point stated in subsections (c) and (d) [subsections (3) and (4)] that the test of control is whether the purchaser has obtained the requisite power, not whether the debtor has retained other powers. There is no implication that retention by the debtor of powers other than those mentioned in subsection (f) [subsection (6)] is inconsistent with the purchaser having control. Nor is there a requirement that the purchaser's powers be unconditional, provided that further consent of the entitlement holder is not a condition.

Example 10. Debtor grants to Alpha Bank and to Beta Bank a security interest in a security entitlement that includes 1000 shares of XYZ Co. stock that Debtor holds through an account with Able & Co. By agreement among the parties, Alpha's security interest is senior and Beta's is junior. Able agrees to act on the entitlement orders of either Alpha or Beta. Alpha and Beta each has control under subsection (d)(2) [subsection (4)(b)]. Moreover, Beta has control notwithstanding a term of Able's agreement to the effect that Able's obligation to act on Beta's entitlement orders is conditioned on Alpha's consent. The crucial distinction is that Able's agreement to act on Beta's entitlement orders is not conditioned on Debtor's further consent.

Example 11. Debtor grants to Alpha Bank a security interest in a security entitlement that includes 1000 shares of XYZ Co. stock that Debtor holds through an account with Able & Co. Able agrees to act on the entitlement orders of Alpha, but Alpha's right to give entitlement orders to the securities intermediary is conditioned on the Debtor's default. Alternatively, Alpha's right to give entitlement orders is conditioned upon Alpha's statement to Able that Debtor is in default. Because Able's agreement to act on Beta's entitlement orders is not conditioned on Debtor's further consent, Alpha has control of the securities entitlement under either alternative.

In many situations, it will be better practice for both the securities intermediary and the purchaser to insist that any conditions relating in any way to the entitlement holder be effective only as between the purchaser and the entitlement holder. That practice would avoid the risk that the securities intermediary could be caught between conflicting assertions of the entitlement holder and the purchaser as to whether the conditions in fact have been met. Nonetheless, the existence of unfulfilled conditions effective against the intermediary would not preclude the purchaser from having control.

Compiler's Comments

1999 Amendment: Chapter 305 inserted (4)(c) concerning security entitlement on behalf of purchaser; and made minor changes in style. Amendment effective July 1, 2001.

30-8-117. Whether indorsement, instruction, or entitlement order is effective.

Official Comment

Source: Section 8-107, U.C.C.

Official Comment:

1. This section defines two concepts, "appropriate person" and "effective." Effectiveness is a broader concept than appropriate person. For example, if a security or securities account is registered in the name of Mary Roe, Mary Roe is the "appropriate person," but an indorsement, instruction, or entitlement order made by John Doe is "effective" if, under agency or other law, Mary Roe is precluded from denying Doe's authority. Treating these two concepts separately facilitates statement of the rules of Article 8 [Title 30, chapter 8] that state the legal effect of an indorsement, instruction, or entitlement order. For example, a securities intermediary is protected against liability if it acts on an effective entitlement order, but has a duty to comply with an entitlement order only if it is originated by an appropriate person. See Sections 8-115 and 8-507 [30-8-125 and 30-8-507].

One important application of the "effectiveness" concept is in the direct holding system rules on the rights of purchasers. A purchaser of a certificated security in registered form can qualify as a protected purchaser who takes free from adverse claims under Section 8-303 [30-8-333] only if the purchaser obtains "control." Section 8-106 [30-8-116] provides that a purchaser of a certificated security in registered form obtains control if there has been an "effective" indorsement.

2. Subsection (a) [subsection (1)] provides that the term "appropriate person" covers two categories: (1) the person who is actually designated as the person entitled to the security or security entitlement, and (2) the successor or legal representative of that person if that person has died or otherwise lacks capacity. Other law determines who has power to transfer a security on behalf of a person who lacks capacity. For example, if securities are registered in the name of more than one person and one of the designated persons dies, whether the survivor is the appropriate person depends on the form of tenancy. If the two were registered joint tenants with right of survivorship, the survivor would have that power under other law and thus would be the "appropriate person." If securities are registered in the name of an individual and the individual dies, the law of decedents' estates determines who has power to transfer the decedent's securities. That would ordinarily be the executor or administrator, but if a "small estate statute" permits a widow to transfer a decedent's securities without administration proceedings, she would be the appropriate person. If the registration of a security or a securities account contains a designation of a death beneficiary under the Uniform Transfer on Death Security Registration Act or comparable legislation, the designated beneficiary would, under that law, have power to transfer upon the person's death and so would be the appropriate person. Article 8 [Title 30, chapter 8] does not contain a list of such representatives, because any list is likely to become outdated by developments in other law.

3. Subsection (b) [subsection (2)] sets out the general rule that an indorsement, instruction, or entitlement order is effective if it is made by the appropriate person or by a person who has power to transfer under agency law or if the appropriate person is precluded from denying its effectiveness. The control rules in Section 8-106 [30-8-116] provide for arrangements where a person who holds securities through a securities intermediary, or holds uncertificated securities directly, enters into a control agreement giving the secured party the right to initiate entitlement orders of instructions. Paragraph 2 of subsection (b) [subsection (2)(b)] states explicitly that an entitlement order or instruction initiated by a person who has obtained such a control agreement is "effective."

Subsections (c), (d), and (e) [subsections (3), (4), and (5)] supplement the general rule of subsection (b) [subsection (2)] on effectiveness. The term "representative," used in subsections (c) and (d) [subsections (3) and (4)], is defined in Section 1-201(35) [30-1-201(35)].

4. Subsection (c) [subsection (3)] provides that an indorsement, instruction, or entitlement order made by a representative is effective even though the representative's action is a violation of duties. The following example illustrates this subsection:

Example 1. Certificated securities are registered in the name of John Doe. Doe dies and Mary Roe is appointed executor. Roe indorses the security certificate and transfers it to a purchaser in a transaction that is a violation of her duties as executor.

Roe's indorsement is effective, because Roe is the appropriate person under subsection (a)(4) [subsection (1)(d)]. This is so even though Roe's transfer violated her obligations as executor. The policies of free transferability of securities that underlie Article 8 [Title 30, chapter 8] dictate that neither a purchaser to whom Roe transfers the securities nor the issuer who registers transfer should be required to investigate the terms of the will to determine whether Roe is acting properly. Although Roe's indorsement is effective under this section, her breach of duty may be such that her beneficiary has an adverse claim to the securities that Roe transferred. The question whether that adverse claim can be asserted against purchasers is governed not by this section but by

Section 8-303 [30-8-333]. Under Section 8-404 [30-8-414], the issuer has no duties to an adverse claimant unless the claimant obtains legal process enjoining the issuer from registering transfer.

5. Subsection (d) [subsection (4)] deals with cases where a security or a securities account is registered in the name of a person specifically designated as a representative. The following example illustrates this subsection:

Example 2. Certificated securities are registered in the name of "John Jones, trustee of the Smith Family Trust." John Jones is removed as trustee and Martha Moe is appointed successor trustee. The securities, however, are not reregistered, but remain registered in the name of "John Jones, trustee of the Smith Family Trust." Jones indorses the security certificate and transfers it to a purchaser.

Subsection (d) [subsection (4)] provides that an indorsement by John Jones as trustee is effective even though Jones is no longer serving in that capacity. Since the securities were registered in the name of "John Jones, trustee of the Smith Family Trust," a purchaser, or the issuer when called upon to register transfer, should be entitled to assume without further inquiry that Jones has the power to act as trustee for the Smith Family Trust.

Note that subsection (d) [subsection (4)] does not apply to a case where the security or securities account is registered in the name of principal rather than the representative as such. The following example illustrates this point:

Example 3. Certificated securities are registered in the name of John Doe. John Doe dies and Mary Roe is appointed executor. The securities are not reregistered in the name of Mary Roe as executor. Later, Mary Roe is removed as executor and Martha Moe is appointed as her successor. After being removed, Mary Roe indorses the security certificate that is registered in the name of John Doe and transfers it to a purchaser.

Mary Roe's indorsement is not made effective by subsection (d) [subsection (4)], because the securities were not registered in the name of Mary Roe as representative. A purchaser or the issuer registering transfer should be required to determine whether Roe has power to act for John Doe. Purchasers and issuers can protect themselves in such cases by requiring signature guaranties. See Section 8-306 [30-8-336].

6. Subsection (e) [subsection (5)] provides that the effectiveness of an indorsement, instruction, or entitlement order is determined as of the date it is made. The following example illustrates this subsection:

Example 4. Certificated securities are registered in the name of John Doe. John Doe dies and Mary Roe is appointed executor. Mary Roe indorses the security certificate that is registered in the name of John Doe and transfers it to a purchaser. After the indorsement and transfer, but before the security certificate is presented to the issuer for registration of transfer, Mary Roe is removed as executor and Martha Moe is appointed as her successor.

Mary Roe's indorsement is effective, because at the time Roe indorsed she was the appropriate person under subsection (a)(4) [subsection (1)(d)]. Her later removal as executor does not render the indorsement ineffective. Accordingly, the issuer would not be liable for registering the transfer. See Section 8-404 [30-8-414].

30-8-118. Warranties in direct holding.

Official Comment

Source: Section 8-108, U.C.C.

Official Comment:

1. Subsections (a), (b), and (c) [subsections (1), (2), and (3)] deal with warranties by security transferors to purchasers. Subsections (d) and (e) [subsections (4) and (5)] deal with warranties by security transferors to issuers. Subsection (f) [subsection (6)] deals with presentment warranties.

2. Subsection (a) [subsection (1)] specifies the warranties made by a person who transfers a certificated security to a purchaser for value. Paragraphs (3), (4), and (5) [subsections (1)(c), (1)(d), and (1)(e)] make explicit several key points that are implicit in the general warranty of paragraph (6) [subsection (1)(f)] that the transfer is effective and rightful. Subsection (b) [subsection (2)] sets forth the warranties made to a purchaser for value by one who originates an instruction. These warranties are quite similar to those made by one transferring a certificated security, subsection (a) [subsection (1)], the principal difference being the absolute warranty of validity. If upon receipt of the instruction the issuer should dispute the validity of the security, the burden of proving validity is upon the transferor. Subsection (c) [subsection (3)] provides for the limited circumstances in which an uncertificated security could be transferred without an instruction, see Section 8-301(b)(2) [30-8-331(2)(b)]. Subsections (d) and (e) [subsections (4) and (5)] give the issuer the benefit of the warranties of an indorser or originator on those matters not within the issuer's knowledge.

3. Subsection (f) [subsection (6)] limits the warranties made by a purchaser for value without notice whose presentation of a security certificate is defective in some way but to whom the issuer does register transfer. The effect is to deny the issuer a remedy against such a person unless at the time of presentment the person had knowledge of an unauthorized signature in a necessary indorsement. The issuer can protect itself by refusing to make the transfer or, if it registers the transfer before it discovers the defect, by pursuing its remedy against a signature guarantor.

4. Subsection (g) [subsection (7)] eliminates all substantive warranties in the relatively unusual case of a delivery of certificated security by an agent of a disclosed principal where the agent delivers the exact certificate that it received from or for the principal. Subsection (h) [subsection (8)] limits the warranties given by a secured party who redelivers a certificate. Subsection (i) [subsection (9)] specifies the warranties of brokers in the more common scenarios.

5. Under Section 1-102(3) [30-1-102(3)] the warranty provisions apply "unless otherwise agreed" and the parties may enter into express agreements to allocate the risks of possible defects. Usual estoppel principles apply with respect to transfers of both certificated and uncertificated securities whenever the purchaser has knowledge of the defect, and these warranties will not be breached in such a case.

30-8-119. Warranties in indirect holding.

Official Comment

Source: Section 8-109, U.C.C.

Official Comment:

1. Subsection (a) [subsection (1)] provides that a person who originates an entitlement order warrants to the securities intermediary that the order is authorized, and warrants the absence of adverse claims. Subsection (b) [subsection (2)] specifies the warranties that are given when a person who holds securities directly has the holding converted into indirect form. A person who delivers a certificate to a securities intermediary or originates an instruction for an uncertificated security gives to the securities intermediary the transfer warranties under Section 8-108 [30-8-118]. If the securities intermediary in turn delivers the certificate to a higher level securities intermediary, it gives the same warranties.

2. Subsection (c) [subsection (3)] states the warranties that a securities intermediary gives when a customer who has been holding securities in an account with the securities intermediary requests that certificates be delivered or that uncertificated securities be registered in the customer's name. The warranties are the same as those that brokers make with respect to securities that the brokers sell to or buy on behalf of the customers. See Section 8-108(i) [30-8-118(9)].

3. As with the Section 8-108 [30-8-118] warranties, the warranties specified in this section may be modified by agreement under Section 1-102(3) [30-1-102(3)].

30-8-120. Applicability — choice of law.

Official Comment

Source: Section 8-110, U.C.C.

Official Comment:

1. This section deals with applicability and choice of law issues concerning Article 8 [Title 30, chapter 8]. The distinction between the direct and indirect holding systems plays a significant role in determining the governing law. An investor in the direct holding system is registered on the books of the issuer and/or has possession of a security certificate. Accordingly, the jurisdiction of incorporation of the issuer or location of the certificate determine the applicable law. By contrast, an investor in the indirect holding system has a security entitlement, which is a bundle of rights against the securities intermediary with respect to a security, rather than a direct interest in the underlying security. Accordingly, in the rules for the indirect holding system, the jurisdiction of incorporation of the issuer of the underlying security or the location of any certificates that might be held by the intermediary or a higher tier intermediary, do not determine the applicable law.

The phrase "local law" refers to the law of a jurisdiction other than its conflict of laws rules. See Restatement (Second) of Conflict of Laws § 4.

2. Subsection (a) [subsection (1)] provides that the law of an issuer's jurisdiction governs certain issues where the substantive rules of Article 8 [Title 30, chapter 8] determine the issuer's rights and duties. Paragraph (1) of subsection (a) [subsection (1)(a)] provides that the law of the issuer's jurisdiction governs the validity of the security. This ensures that a single body of law will govern the questions addressed in Part 2 of Article 8 [Title 30, chapter 8, part 2], concerning the circumstances in which an issuer can and cannot assert invalidity as a defense against purchasers. Similarly, paragraphs (2), (3), and (4) of subsection (a) [subsections (1)(b),

(1)(c), and (1)(d)] ensure that the issuer will be able to look to a single body of law on the questions addressed in Part 4 of Article 8 [Title 30, chapter 8, part 4], concerning the issuer's duties and liabilities with respect to registration of transfer.

Paragraph (5) of subsection (a) [subsection (1)(e)] applies the law of an issuer's jurisdiction to the question whether an adverse claim can be asserted against a purchaser to whom transfer has been registered, or who has obtained control over an uncertificated security. Although this issue deals with the rights of persons other than the issuer, the law of the issuer's jurisdiction applies because the purchasers to whom the provision applies are those whose protection against adverse claims depends on the fact that their interests have been recorded on the books of the issuer.

The principal policy reflected in the choice of law rules in subsection (a) [subsection (1)] is that an issuer and others should be able to look to a single body of law on the matters specified in subsection (a) [subsection (1)], rather than having to look to the law of all of the different jurisdictions in which security holders may reside. The choice of law policies reflected in this subsection do not require that the body of law governing all of the matters specified in subsection (a) [subsection (1)] be that of the jurisdiction in which the issuer is incorporated. Thus, subsection (d) [subsection (4)] provides that the term "issuer's jurisdiction" means the jurisdiction in which the issuer is organized, or, if permitted by that law, the law of another jurisdiction selected by the issuer. Subsection (d) [subsection (4)] also provides that issuers organized under the law of a State which adopts this Article [Title 30, chapter 8] may make such a selection, except as to the validity issue specified in paragraph (1) [subsection (1)(a)]. The question whether an issuer can assert the defense of invalidity may implicate significant policies of the issuer's jurisdiction of incorporation. See, e.g., Section 8-202 [30-8-212] and Comments thereto.

Although subsection (a) [subsection (1)] provides that the issuer's rights and duties concerning registration of transfer are governed by the law of the issuer's jurisdiction, other matters related to registration of transfer, such as appointment of a guardian for a registered owner or the existence of agency relationships, might be governed by another jurisdiction's law. Neither this section nor Section 1-105 [30-1-105, now repealed] deals with what law governs the appointment of the administrator or executor; that question is determined under generally applicable choice of law rules.

3. Subsection (b) [subsection (2)] provides that the law of the securities intermediary's jurisdiction governs the issues concerning the indirect holding system that are dealt with in Article 8 [Title 30, chapter 8]. Paragraphs (1) and (2) [subsections (2)(a) and (2)(b)] cover the matters dealt with in the Article 8 [Title 30, chapter 8] rules defining the concept of security entitlement and specifying the duties of securities intermediaries. Paragraph (3) [subsection (2)(c)] provides that the law of the security intermediary's jurisdiction determines whether the intermediary owes any duties to an adverse claimant. Paragraph (4) [subsection (2)(d)] provides that the law of the security intermediary's jurisdiction determines whether adverse claims can be asserted against entitlement holders and others.

Subsection (e) [subsection (5)] determines what is a "securities intermediary's jurisdiction." The policy of subsection (b) [subsection (2)] is to ensure that a securities intermediary and all of its entitlement holders can look to a single, readily-identifiable body of law to determine their rights and duties. Accordingly, subsection (e) [subsection (5)] sets out a sequential series of tests to facilitate identification of that body of law. Paragraph (1) of subsection (e) [subsection (5)(a)] permits specification of the securities intermediary's jurisdiction by agreement. In the absence of such a specification, the law chosen by the parties to govern the securities account determines the securities intermediary's jurisdiction. See paragraph (2) [subsection (2)(b)]. Because the policy of this section is to enable parties to determine, in advance and with certainty, what law will apply to transactions governed by this Article [chapter], the validation of the parties' selection of governing law by agreement is not conditioned upon a determination that the jurisdiction whose law is chosen bear a "reasonable relation" to the transaction. See Section 4A-507 [30-4A-507]; compare Section 1-105(1) [30-1-105(1), now repealed]. That is also true with respect to the similar provisions in subsection (d) [subsection (4)] of this section and in Section 9-305 [30-9A-305]. The remaining paragraphs in subsection (e) [subsection (5)] contain additional default rules for determining the securities intermediary's jurisdiction.

Subsection (f) [subsection (6)] makes explicit a point that is implicit in the Article 8 [Title 30, chapter 8] description of a security entitlement as a bundle of rights against the intermediary with respect to a security or other financial asset, rather than as a direct interest in the underlying security or other financial asset. The governing law for relationships in the indirect holding system is not determined by such matters as the jurisdiction of incorporation of the issuer of the securities held through the intermediary, or the location of any physical certificates held by the intermediary or a higher tier intermediary.

4. Subsection (c) [subsection (3)] provides a choice of law rule for adverse claim issues that may arise in connection with delivery of security certificates in the direct holding system. It applies the law of the place of delivery. If a certificated security issued by an Idaho corporation is sold, and the sale is settled by physical delivery of the certificate from Seller to Buyer in New York, under subsection (c) [subsection (3)], New York law determines whether Buyer takes free from adverse claims. The domicile of Seller, Buyer, and any adverse claimant is irrelevant.

5. The following examples illustrate how a court in a jurisdiction which has enacted this section would determine the governing law:

Example 1. John Doe, a resident of Kansas, maintains a securities account with Able & Co. Able is incorporated in Delaware. Its chief executive offices are located in Illinois. The office where Doe transacts business with Able is located in Missouri. The agreement between Doe and Able specifies that Illinois is the securities intermediary's (Able's) jurisdiction. Through the account, Doe holds securities of a Colorado corporation, which Able holds through Clearing Corporation. The rules of Clearing Corporation provide that the rights and duties of Clearing Corporation and its participants are governed by New York law. Subsection (a) [subsection (1)] specifies that a controversy concerning the rights and duties as between the issuer and Clearing Corporation is governed by Colorado law. Subsections (b) and (e) [subsections (2) and (5)] specify that a controversy concerning the rights and duties as between the Clearing Corporation and Able is governed by New York law, and that a controversy concerning the rights and duties as between Able and Doe is governed by Illinois law.

Example 2. Same facts as to Doe and Able as in Example 1. Through the account, Doe holds securities of a Senegalese corporation, which Able holds through Clearing Corporation. Clearing Corporation's operations are located in Belgium, and its rules and agreements with its participants provide that they are governed by Belgian law. Clearing Corporation holds the securities through a custodial account at the Paris branch office of Global Bank, which is organized under English law. The agreement between Clearing Corporation and Global Bank provides that it is governed by French law. Subsection (a) [subsection (1)] specifies that a controversy concerning the rights and duties as between the issuer and Global Bank is governed by Senegalese law. Subsections (b) and (e) [subsections (2) and (5)] specify that a controversy concerning the rights and duties as between Global Bank and Clearing Corporation is governed by French law, that a controversy concerning the rights and duties as between Clearing Corporation and Able is governed by Belgian law, and that a controversy concerning the rights and duties as between Able and Doe is governed by Illinois law.

6. To the extent that this section does not specify the governing law, general choice of law rules apply. For example, suppose that in either of the examples in the preceding Comment, Doe enters into an agreement with Roe, also a resident of Kansas, in which Doe agrees to transfer all of his interests in the securities held through Able to Roe. Article 8 [Title 30, chapter 8] does not deal with whether such an agreement is enforceable or whether it gives Roe some interest in Doe's security entitlement. This section specifies what jurisdiction's law governs the issues that are dealt with in Article 8 [Title 30, chapter 8]. Article 8 [Title 30, chapter 8], however, does specify that securities intermediaries have only limited duties with respect to adverse claims. See Section 8-115 [30-8-125]. Subsection (b)(3) [subsection (2)(c)] of this section provides that Illinois law governs whether Able owes any duties to an adverse claimant. Thus, if Illinois has adopted Revised Article 8 [Title 30, chapter 8], Section 8-115 [30-8-125] as enacted in Illinois determines whether Roe has any rights against Able.

7. The choice of law provisions concerning security interests in securities and security entitlements are set out in Section 9-305 [30-9A-305].

Compiler's Comments

1999 Amendment: Chapter 305 substituted (5) concerning rules for determining security intermediaries jurisdiction for former text that read: "(5) The following rules determine a "securities intermediary's jurisdiction" for purposes of this section:

(a) If an agreement between the securities intermediary and its entitlement holder specifies that it is governed by the law of a particular jurisdiction, that jurisdiction is the securities intermediary's jurisdiction.

(b) If an agreement between the securities intermediary and its entitlement holder does not specify the governing law as provided in subsection (5)(a), but expressly specifies that the securities account is maintained at an office in a particular jurisdiction, that jurisdiction is the securities intermediary's jurisdiction.

(c) If an agreement between the securities intermediary and its entitlement holder does not specify a jurisdiction as provided in subsection (5)(a) or (5)(b), the securities intermediary's jurisdiction is the jurisdiction in which is located the office identified in an account statement as the office serving the entitlement holder's account.

(d) If an agreement between the securities intermediary and its entitlement holder does not specify a jurisdiction as provided in subsection (5)(a) or (5)(b) and an account statement does not identify an office serving the entitlement holder's account as provided in subsection (5)(c), the securities intermediary's jurisdiction is the jurisdiction in which is located the chief executive office of the securities intermediary"; and made minor changes in style. Amendment effective July 1, 2001.

30-8-121. Clearing corporation rules.

Official Comment

Source: Section 8-111, U.C.C.

Official Comment:

1. The experience of the past few decades shows that securities holding and settlement practices may develop rapidly, and in unforeseeable directions. Accordingly, it is desirable that the rules of Article 8 [Title 30, chapter 8] be adaptable both to ensure that commercial law can conform to changing practices and to ensure that commercial law does not operate as an obstacle to developments in securities practice. Even if practices were unchanging, it would not be possible in a general statute to specify in detail the rules needed to provide certainty in the operations of the clearance and settlement system.

The provisions of this Article [chapter] and Article 1 [Title 30, chapter 1] on the effect of agreements provide considerable flexibility in the specification of the details of the rights and obligations of participants in the securities holding system by agreement. See Sections 8-504 through 8-509 [30-8-504 through 30-8-509], and Section 1-102(3) and (4) [30-8-102(3) and (4)]. Given the magnitude of the exposures involved in securities transactions, however, it may not be possible for the parties in developing practices to rely solely on private agreements, particularly with respect to matters that might affect others, such as creditors. For example, in order to be fully effective, rules of clearing corporations on the finality or reversibility of securities settlements must not only bind the participants in the clearing corporation but also be effective against their creditors. Section 8-111 [30-8-121] provides that clearing corporation rules are effective even if they indirectly affect third parties, such as creditors of a participant. This provision does not, however, permit rules to be adopted that would govern the rights and obligations of third parties other than as a consequence of rules that specify the rights and obligations of the clearing corporation and its participants.

2. The definition of clearing corporation in Section 8-102 [30-1-112] covers only federal reserve banks, entities registered as clearing agencies under the federal securities laws, and others subject to comparable regulation. The rules of registered clearing agencies are subject to regulatory oversight under the federal securities laws.

30-8-122. Creditor's legal process.

Official Comment

Source: Section 8-112, U.C.C.

Official Comment:

1. In dealing with certificated securities the instrument itself is the vital thing, and therefore a valid levy cannot be made unless all possibility of the certificate's wrongfully finding its way into a transferee's hands has been removed. This can be accomplished only when the certificate is in the possession of a public officer, the issuer, or an independent third party. A debtor who has been enjoined can still transfer the security in contempt of court. See Overlock v. Jerome-Portland Copper Mining Co., 29 Ariz. 560, 243 P. 400 (1926). Therefore, although injunctive relief is provided in subsection (e) [subsection (5)] so that creditors may use this method to gain control of the certificated security, the security certificate itself must be reached to constitute a proper levy whenever the debtor has possession.

2. Subsection (b) [subsection (2)] provides that when the security is uncertificated and registered in the debtor's name, the debtor's interest can be reached only by legal process upon the issuer. The most logical place to serve the issuer would be the place where the transfer records are maintained, but that location might be difficult to identify, especially when the separate elements of a computer network might be situated in different places. The chief executive office is selected as the appropriate place by analogy to Section 9-103(3)(d) [30-9-103(3)(d), now repealed, see 30-9A-307]. See Comment 5(c) to that section. This section indicates only how attachment

is to be made, not when it is legally justified. For that reason there is no conflict between this section and Shaffer v. Heitner, 433 U.S. 186 (1977).

3. Subsection (c) [subsection (3)] provides that a security entitlement can be reached only by legal process upon the debtor's security intermediary. Process is effective only if directed to the debtor's own security intermediary. If Debtor holds securities through Broker, and Broker in turn holds through Clearing Corporation, Debtor's property interest is a security entitlement against Broker. Accordingly, Debtor's creditor cannot reach Debtor's interest by legal process directed to the Clearing Corporation. See also Section 8-115 [30-8-125].

4. Subsection (d) [subsection (4)] provides that when a certificated security, an uncertificated security, or a security entitlement is controlled by a secured party, the debtor's interest can be reached by legal process upon the secured party. This section does not attempt to provide for rights as between the creditor and the secured party, as, for example, whether or when the secured party must liquidate the security.

30-8-123. Statute of frauds inapplicable.

Official Comment

Source: Section 8-113, U.C.C.

Official Comment:

This section provides that the statute of frauds does not apply to contracts for the sale of securities, reversing prior law which had a special statute of frauds in Section 8-319 (1978) [former 30-8-319]. With the increasing use of electronic means of communication, the statute of frauds is unsuited to the realities of the securities business. For securities transactions, whatever benefits a statute of frauds may play in filtering out fraudulent claims are outweighed by the obstacles it places in the development of modern commercial practices in the securities business.

Case Notes

Option Agreement: Evidence of payment of money pursuant to the purchase of real estate for the purpose of persuading seller to hold the deal open for a certain period of time, and the subsequent actions of the seller in holding the property off the market, were sufficient to establish a valid option agreement, as well as to show that the agreement had been fully performed. Lynch v. Shields, 165 M 396, 529 P2d 348 (1974).

30-8-124. Evidentiary rules concerning certificated securities.

Official Comment

Source: Section 8-114, U.C.C.

Official Comment:

This section adapts the rules of negotiable instruments law concerning procedure in actions on instruments, see Section 3-308 [30-3-308], to actions on certificated securities governed by this Article [chapter]. An "action on a security" includes any action or proceeding brought against the issuer to enforce a right or interest that is part of the security, such as an action to collect principal or interest or a dividend, or to establish a right to vote or to receive a new security under an exchange offer or plan of reorganization. This section applies only to certificated securities; actions on uncertificated securities are governed by general evidentiary principles.

30-8-125. Securities intermediary and others not liable to adverse claimant.

Official Comment

Source: Section 8-115, U.C.C.

Official Comment:

1. Other provisions of Article 8 [Title 30, chapter 8] protect certain purchasers against adverse claims, both for the direct holding system and the indirect holding system. See Sections 8-303 and 8-502 [30-8-333 and 30-8-502]. This section deals with the related question of the possible liability of a person who acted as the "conduit" for a securities transaction. It covers both securities intermediaries—the "conduits" in the indirect holding system—and brokers or other agents or bailees—the "conduits" in the direct holding system. The following examples illustrate its operation:

Example 1. John Doe is a customer of the brokerage firm of Able & Co. Doe delivers to Able a certificate for 100 shares of XYZ Co. common stock, registered in Doe's name and properly indorsed, and asks the firm to sell it for him. Able does so. Later, John Doe's spouse Mary Doe brings an action against Able asserting that Able's action was wrongful against her because the XYZ Co. stock was marital property in which she had an interest, and John Doe was acting wrongfully against her in transferring the securities.

Example 2. Mary Roe is a customer of the brokerage firm of Baker & Co. and holds her securities through a securities account with Baker. Roe instructs Baker to sell 100 shares of XYZ Co. common stock that she carried in her account. Baker does so. Later, Mary Roe's spouse John Roe brings an action against Baker asserting that Baker's action was wrongful against him because the XYZ Co. stock was marital property in which he had an interest, and Mary Roe was acting wrongfully against him in transferring the securities.

Under common law conversion principles, Mary Doe might be able to assert that Able & Co. is liable to her in Example 1 for exercising dominion over property inconsistent with her rights in it. On that or some similar theory John Roe might assert that Baker is liable to him in Example 2. Section 8-115 [30-8-125] protects both Able and Baker from liability.

2. The policy of this section is similar to that of many other rules of law that protect agents and bailees from liability as innocent converters. If a thief steals property and ships it by mail, express service, or carrier, to another person, the recipient of the property does not obtain good title, even though the recipient may have given value to the thief and had no notice or knowledge that the property was stolen. Accordingly, the true owner can recover the property from the recipient or obtain damages in a conversion or similar action. An action against the postal service, express company, or carrier presents entirely different policy considerations. Accordingly, general tort law protects agents or bailees who act on the instructions of their principals or bailors. See Restatement (Second) of Torts § 235. See also UCC Section 7-404 [30-7-404].

3. Except as provided in paragraph 3 [subsection (3)], this section applies even though the securities intermediary, or the broker or other agent or bailee, had notice or knowledge that another person asserts a claim to the securities. Consider the following examples:

Example 3. Same facts as in Example 1, except that before John Doe brought the XYZ Co. security certificate to Able for sale, Mary Doe telephoned or wrote to the firm asserting that she had an interest in all of John Doe's securities and demanding that they not trade for him.

Example 4. Same facts as in Example 2, except that before Mary Roe gave an entitlement order to Baker to sell the XYZ Co. securities from her account, John Doe telephoned or wrote to the firm asserting that he had an interest in all of Mary Roe's securities and demanding that they not trade for her.

Section 8-115 [30-8-125] protects Able and Baker from liability. The protections of Section 8-115 [30-8-125] do not depend on the presence or absence of notice of adverse claims. It is essential to the securities settlement system that brokers and securities intermediaries be able to act promptly on the directions of their customers. Even though a firm has notice that someone asserts a claim to a customer's securities or security entitlements, the firm should not be placed in the position of having to make a legal judgment about the validity of the claim at the risk of liability either to its customer or to the third party for guessing wrong. Under this section, the broker or securities intermediary is privileged to act on the instructions of its customer or entitlement holder, unless it has been served with a restraining order or other legal process enjoining it from doing so. This is already the law in many jurisdictions. For example a section of the New York Banking Law provides that banks need not recognize any adverse claim to funds or securities on deposit with them unless they have been served with legal process. N.Y. Banking Law § 134. Other sections of the UCC embody a similar policy. See Sections 3-602 and 5-114(2)(b) [30-3-603 and 30-5-134(2)(b)].

Paragraph (1) [subsection (1)] of this section refers only to a court order enjoining the securities intermediary or the broker or other agent or bailee from acting at the instructions of the customer. It does not apply to cases where the adverse claimant tells the intermediary or broker that the customer has been enjoined, or shows the intermediary or broker a copy of a court order binding the customer.

Paragraph (3) [subsection (3)] takes a different approach in one limited class of cases, those where a customer sells stolen certificated securities through a securities firm. Here the policies that lead to protection of securities firms against assertions of other sorts of claims must be weighed against the desirability of having securities firms guard against the disposition of stolen securities. Accordingly, paragraph (3) [subsection (3)] denies protection to a broker, custodian, or other agent or bailee who receives a stolen security certificate from its customer, if the broker, custodian, or other agent or bailee had notice of adverse claims. The circumstances that give notice of adverse claims are specified in Section 8-105 [30-8-115]. The result is that brokers, custodians, and other agents and bailees face the same liability for selling stolen certificated securities that purchasers face for buying them.

4. As applied to securities intermediaries, this section embodies one of the fundamental principles of the Article 8 [Title 30, chapter 8] indirect holding system rules—that a securities

intermediary owes duties only to its own entitlement holders. The following examples illustrate the operation of this section in the multi-tiered indirect holding system:

Example 5. Able & Co., a broker-dealer, holds 50,000 shares of XYZ Co. stock in its account at Clearing Corporation. Able acquired the XYZ shares from another firm, Baker & Co., in a transaction that Baker contends was tainted by fraud, giving Baker a right to rescind the transaction and recover the XYZ shares from Able. Baker sends notice to Clearing Corporation stating that Baker has a claim to the 50,000 shares of XYZ Co. in Able's account. Able then initiates an entitlement order directing Clearing Corporation to transfer the 50,000 shares of XYZ Co. to another firm in settlement of a trade. Under Section 8-115 [30-8-125], Clearing Corporation is privileged to comply with Able's entitlement order, without fear of liability to Baker. This is so even though Clearing Corporation has notice of Baker's claim, unless Baker obtains a court order enjoining Clearing Corporation from acting on Able's entitlement order.

Example 6. Able & Co., a broker-dealer, holds 50,000 shares of XYZ Co. stock in its account at Clearing Corporation. Able initiates an entitlement order directing Clearing Corporation to transfer the 50,000 shares of XYZ Co. to another firm in settlement of a trade. That trade was made by Able for its own account, and the proceeds were devoted to its own use. Able becomes insolvent, and it is discovered that Able has a shortfall in the shares of XYZ Co. stock that it should have been carrying for its customers. Able's customers bring an action against Clearing Corporation asserting that Clearing Corporation acted wrongfully in transferring the XYZ shares on Able's order because those were shares that should have been held by Able for its customers. Under Section 8-115 [30-8-125], Clearing Corporation is not liable to Able's customers, because Clearing Corporation acted on an effective entitlement order of its own entitlement holder, Able. Clearing Corporation's protection against liability does not depend on the presence or absence of notice or knowledge of the claim by Clearing Corporation.

5. If the conduct of a securities intermediary or a broker or other agent or bailee rises to a level of complicity in the wrongdoing of its customer or principal, the policies that favor protection against liability do not apply. Accordingly, paragraph (2) [subsection (2)] provides that the protections of this section do not apply if the securities intermediary or broker or other agent or bailee acted in collusion with the customer or principal in violating the rights of another person. The collusion test is intended to adopt a standard akin to the tort rules that determine whether a person is liable as an aider or abettor for the tortious conduct of a third party. See Restatement (Second) of Torts § 876.

Knowledge that the action of the customer is wrongful is a necessary but not sufficient condition of the collusion test. The aspect of the role of securities intermediaries and brokers that Article 8 [Title 30, chapter 8] deals with is the clerical or ministerial role of implementing and recording the securities transactions that their customers conduct. Faithful performance of this role consists of following the instructions of the customer. It is not the role of the record-keeper to police whether the transactions recorded are appropriate, so mere awareness that the customer may be acting wrongfully does not itself constitute collusion. That, of course, does not insulate an intermediary or broker from responsibility in egregious cases where its action goes beyond the ordinary standards of the business of implementing and recording transactions, and reaches a level of affirmative misconduct in assisting the customer in the commission of a wrong.

30-8-126. Securities intermediary as purchaser for value.

Official Comment

Source: Section 8-116, U.C.C.

Official Comment:

1. This section is intended to make explicit two points that, while implicit in other provisions, are of sufficient importance to the operation of the indirect holding system that they warrant explicit statement. First, it makes clear that a securities intermediary that receives a financial asset and establishes a security entitlement in respect thereof in favor of an entitlement holder is a "purchaser" of the financial asset that the securities intermediary received. Second, it makes clear that by establishing a security entitlement in favor of an entitlement holder a securities intermediary gives value for any corresponding financial asset that the securities intermediary receives or acquires from another party, whether the intermediary holds directly or indirectly.

In many cases a securities intermediary that receives a financial asset will also be transferring value to the person from whom the financial asset was received. That, however, is not always the case. Payment may occur through a different system than settlement of the securities side of the transaction, or the securities might be transferred without a corresponding payment, as when a person moves an account from one securities intermediary to another. Even though the securities intermediary does not give value to the transferor, it does give value by incurring obligations to its own entitlement holder. Although the general definition of value in Section 1-201(44)(d) [30-1-201(44)(d)] should be interpreted to cover the point, this section is included to make this point explicit.

2. The following examples illustrate the effect of this section:

Example 1. Buyer buys 1000 shares of XYZ Co. common stock through Buyer's broker Able & Co. to be held in Buyer's securities account. In settlement of the trade, the selling broker delivers to Able a security certificate in street name, indorsed in blank, for 1000 shares XYZ Co. stock, which Able holds in its vault. Able credits Buyer's account for securities in that amount. Section 8-116 [30-8-126] specifies that Able is a purchaser of the XYZ Co. stock certificate, and gave value for it. Thus, Able can obtain the benefit of Section 8-303 [30-8-333], which protects purchasers for value, if it satisfies the other requirements of that section.

Example 2. Buyer buys 1000 shares XYZ Co. common stock through Buyer's broker Able & Co. to be held in Buyer's securities account. The trade is settled by crediting 1000 shares XYZ Co. stock to Able's account at Clearing Corporation. Able credits Buyer's account for securities in that amount. When Clearing Corporation credits Able's account, Able acquires a security entitlement under Section 8-501 [30-8-501]. Section 8-116 [30-8-126] specifies that Able acquired this security entitlement for value. Thus, Able can obtain the benefit of Section 8-502 [30-8-502], which protects persons who acquire security entitlements for value, if it satisfies the other requirements of that section.

Example 3. Thief steals a certificated bearer bond from Owner. Thief sends the certificate to his broker Able & Co. to be held in his securities account, and Able credits Thief's account for the bond. Section 8-116 [30-8-126] specifies that Able is a purchaser of the bond and gave value for it. Thus, Able can obtain the benefit of Section 8-303 [30-8-333], which protects purchasers for value, if it satisfies the other requirements of that section.

Part 2
Issue and Issuer

30-8-211. Issuer.

Official Comment

Source: Section 8-201, U.C.C.

Official Comment:

1. The definition of "issuer" in this section functions primarily to describe the persons whose defenses may be cut off under the rules in Part 2 [Title 30, chapter 8, part 2]. In large measure it simply tracks the language of the definition of security in Section 8-102(a)(15) [30-8-112(1)(o)].

2. Subsection (b) [subsection (2)] distinguishes the obligations of a guarantor as issuer from those of the principal obligor. However, it does not exempt the guarantor from the impact of subsection (d) of Section 8-202 [30-8-212(4)]. Whether or not the obligation of the guarantor is noted on the security is immaterial. Typically, guarantors are parent corporations, or stand in some similar relationship to the principal obligor. If that relationship existed at the time the security was originally issued the guaranty would probably have been noted on the security. However, if the relationship arose afterward, e.g., through a purchase of stock or properties, or through merger or consolidation, probably the notation would not have been made. Nonetheless, the holder of the security is entitled to the benefit of the obligation of the guarantor.

3. Subsection (c) [subsection (3)] narrows the definition of "issuer" for purposes of Part 4 of this Article [Title 30, chapter 8, part 4] (registration of transfer). It is supplemented by Section 8-407 [30-8-417].

Case Notes

DECISIONS UNDER UNIFORM NEGOTIABLE INSTRUMENTS LAW

Qualifications of Officers: Qualifications of both stockholders and officers are matter of record, and being for protection of corporation and public, record is conclusive. In re Sharp Bros., 2 F. Supp. 227 (D.C. Mont. 1933).

30-8-212. Issuer's responsibility and defenses — notice of defect or defense.

Official Comment

Source: Section 8-202, U.C.C.

Official Comment:

1. In this Article [chapter] the rights of the purchaser for value without notice are divided into two aspects, those against the issuer, and those against other claimants to the security. Part

2 of this Article [Title 30, chapter 8, part 2], and especially this section, deal with rights against the issuer.

Subsection (a) [subsection (1)] states, in accordance with the prevailing case law, the right of the issuer (who prepares the text of the security) to include terms incorporated by adequate reference to an extrinsic source, so long as the terms so incorporated do not conflict with the stated terms. Thus, the standard practice of referring in a bond or debenture to the trust indenture under which it is issued without spelling out its necessarily complex and lengthy provisions is approved. Every stock certificate refers in some manner to the charter or articles of incorporation of the issuer. At least where there is more than one class of stock authorized applicable corporation codes specifically require a statement or summary as to preferences, voting powers and the like. References to constitutions, statutes, ordinances, rules, regulations or orders are not so common, except in the obligations of governments or governmental agencies or units; but where appropriate they fit into the rule here stated.

Courts have generally held that an issuer is estopped from denying representations made in the text of a security. Delaware-New Jersey Ferry Co. v. Leeds, 21 Del.Ch. 279, 186 A. 913 (1936). Nor is a defect in form or the invalidity of a security normally available to the issuer as a defense. Bonini v. Family Theatre Corporation, 327 Pa. 273, 194 A. 498 (1937); First National Bank of Fairbanks v. Alaska Airmotive, 119 F.2d 267 (C.C.A.Alaska 1941).

2. The rule in subsection (a) [subsection (1)] requiring that the terms of a security be noted or referred to on the certificate is based on practices and expectations in the direct holding system for certificated securities. This rule does not express a general rule or policy that the terms of a security are effective only if they are communicated to beneficial owners in some particular fashion. Rather, subsection (a) [subsection (1)] is based on the principle that a purchaser who does obtain a certificate is entitled to assume that the terms of the security have been noted or referred to on the certificate. That policy does not come into play in a securities holding system in which purchasers do not take delivery of certificates.

The provisions of subsection (a) [subsection (1)] concerning notation of terms on security certificates are necessary only because paper certificates play such an important role for certificated securities that a purchaser should be protected against assertion of any defenses or rights that are not noted on the certificate. No similar problem exists with respect to uncertificated securities. The last sentence of subsection (a) [subsection (1)] is, strictly speaking, unnecessary, since it only recognizes the fact that the terms of an uncertificated security are determined by whatever other law or agreement governs the security. It is included only to preclude any inference that uncertificated securities are subject to any requirement analogous to the requirement of notation of terms on security certificates.

The rule of subsection (a) [subsection (1)] applies to the indirect holding system only in the sense that if a certificated security has been delivered to the clearing corporation or other securities intermediary, the terms of the security should be noted or referred to on the certificate. If the security is uncertificated, that principle does not apply even at the issuer-clearing corporation level. The beneficial owners who hold securities through the clearing corporation are bound by the terms of the security, even though they do not actually see the certificate. Since entitlement holders in an indirect holding system have not taken delivery of certificates, the policy of subsection (a) [subsection (1)] does not apply.

3. The penultimate sentence of subsection (a) [subsection (1)] and all of subsection (b) [subsection (2)] embody the concept that it is the duty of the issuer, not of the purchaser, to make sure that the security complies with the law governing its issue. The penultimate sentence of subsection (a) [subsection (1)] makes clear that the issuer cannot, by incorporating a reference to a statute or other document, charge the purchaser with notice of the security's invalidity. Subsection (b) [subsection (2)] gives to a purchaser for value without notice of the defect the right to enforce the security against the issuer despite the presence of a defect that otherwise would render the security invalid. There are three circumstances in which a purchaser does not gain such rights: first, if the defect involves a violation of constitutional provisions, these rights accrue only to a subsequent purchaser, that is, one who takes other than by original issue. This Article [chapter] leaves to the law of each particular State the rights of a purchaser on original issue of a security with a constitutional defect. No negative implication is intended by the explicit grant of rights to a subsequent purchaser.

Second, governmental issuers are distinguished in subsection (b) [subsection (2)] from other issuers as a matter of public policy, and additional safeguards are imposed before governmental issues are validated. Governmental issuers are estopped from asserting defenses only if there has been substantial compliance with the legal requirements governing the issue or if substantial consideration has been received and a stated purpose of the issue is one for which the issuer has power to borrow money or issue the security. The purpose of the substantial compliance requirement is to make certain that a mere technicality as, e.g., in the manner of publishing election notices, shall not be a ground for depriving an innocent purchaser of rights in the security. The policy is here adopted of such cases as Tommie v. City of Gadsden, 229 Ala. 521, 158 So. 763 (1935), in which minor discrepancies in the form of the election ballot used were overlooked and the bonds were declared valid since there had been substantial compliance with the statute.

A long and well established line of federal cases recognizes the principle of estoppel in favor of purchasers for value without notices where municipalities issue bonds containing recitals of compliance with governing constitutional and statutory provisions, made by the municipal authorities entrusted with determining such compliance. Chaffee County v. Potter, 142 U.S. 355 (1892); Oregon v. Jennings, 119 U.S. 74 (1886); Gunnison County Commissioners v. Rollins, 173 U.S. 255 (1898). This rule has been qualified, however, by requiring that the municipality have power to issue the security. Anthony v. County of Jasper, 101 U.S. 693 (1879); Town of South Ottawa v. Perkins, 94 U.S. 260 (1876). This section follows the case law trend, simplifying the rule by setting up two conditions for an estoppel against a governmental issuer: (1) substantial consideration given, and (2) power in the issuer to borrow money or issue the security for the stated purpose. As a practical matter the problem of policing governmental issuers has been alleviated by the present practice of requiring legal opinions as to the validity of the issue. The bulk of the case law on this point is nearly 100 years old and it may be assumed that the question now seldom arises.

Section 8-210 [30-8-220], regarding overissue, provides the third exception to the rule that an innocent purchase for value takes a valid security despite the presence of a defect that would otherwise give rise to invalidity. See that section and its Comment for further explanation.

4. Subsection (e) [subsection (5)] is included to make clear that this section does not affect the presently recognized right of either party to a "when, as and if" or "when distributed" contract to cancel the contract on substantial change.

5. Subsection (f) [subsection (6)] has been added because the introduction of the security entitlement concept requires some adaptation of the Part 2 [Title 30, chapter 8, part 2] rules, particularly those that distinguish between purchasers who take by original issue and subsequent purchasers. The basic concept of Part 2 [Title 30, chapter 8, part 2] is to apply to investment securities the principle of negotiable instruments law that an obligor is precluded from asserting most defenses against purchasers for value without notice. Section 8-202 [30-8-212] describes in some detail which defenses issuers can raise against purchasers for value and subsequent purchasers for value. Because these rules were drafted with the direct holding system in mind, some interpretive problems might be presented in applying them to the indirect holding. For example, if a municipality issues a bond in book-entry only form, the only direct "purchaser" of that bond would be the clearing corporation. The policy of precluding the issuer from asserting defenses is, however, equally applicable. Subsection (f) [subsection (6)] is designed to ensure that the defense preclusion rules developed for the direct holding system will also apply to the indirect holding system.

Case Notes

DECISIONS UNDER UNIFORM NEGOTIABLE INSTRUMENTS LAW

Question for Jury: Where there was sufficient evidence for jury as to undue influence inducing execution of note by defendant suffering from mental disease, such defense was for jury, as against contention that defendant did not attempt to restore consideration. Stagg v. Stagg, 96 M 573, 32 P2d 856 (1934).

Endorsement After Maturity: Endorsement after maturity creates a new contract between the endorser and the endorsee and the Statute of Limitations begins to run in favor of the endorser at the date of the endorsement. Morgan v. Huffman, 76 M 396, 247 P 326 (1926).

Duress: That a promissory note was obtained by duress is a good defense as between the original parties. Averill Mach. Co. v. Taylor, 70 M 70, 223 P 218 (1924).

Conditional Delivery: Whether a delivery was conditional is, on conflicting evidence, a question for the jury. O'Meara v. McDermott, 40 M 38, 104 P 1049 (1909).

30-8-213. Staleness as notice of defect or defense.

Official Comment

Source: Section 8-203, U.C.C.

Official Comment:

1. The problem of matured or called securities is here dealt with in terms of the effect of such events in giving notice of the issuer's defenses and not in terms of "negotiability". The substance of this section applies only to certificated securities because certificates may be transferred to a purchaser by delivery after the security has matured, been called, or become redeemable or exchangeable. It is contemplated that uncertificated securities which have matured or been called will merely be canceled on the books of the issuer and the proceeds sent to the registered owner. Uncertificated securities which have become redeemable or exchangeable, at the option of the owner, may be transferred to a purchaser, but the transfer is effectuated only by registration of transfer, thus necessitating communication with the issuer. If defects or defenses in such securities exist, the issuer will necessarily have the opportunity to bring them to the attention of the purchaser.

2. The fact that a security certificate is in circulation long after it has been called for redemption or exchange must give rise to the question in a purchaser's mind as to why it has not been surrendered. After the lapse of a reasonable period of time a purchaser can no longer claim "no reason to know" of any defects or irregularities in its issue. Where funds are available for the redemption the security certificate is normally turned in more promptly and a shorter time is set as the "reasonable period" than is set where funds are not available.

Defaulted certificated securities may be traded on financial markets in the same manner as unmatured and undefaulted instruments and a purchaser might not be placed upon notice of irregularity by the mere fact of default. An issuer, however, should at some point be placed in a position to determine definitely its liability on an invalid or improper issue, and for this purpose a security under this section becomes "stale" two years after the default. A different rule applies when the question is notice not of issuer's defenses but of claims of ownership. Section 8-105 [30-8-115] and Comment.

3. Nothing in this section is designed to extend the life of preferred stocks called for redemption as "shares of stock" beyond the redemption date. After such a call, the security represents only a right to the funds set aside for redemption.

30-8-214. Effect of issuer's restriction on transfer.

Official Comment

Source: Section 8-204, U.C.C.

Official Comment:

1. Restrictions on transfer of securities are imposed by issuers in a variety of circumstances and for a variety of purposes, such as to retain control of a close corporation or to ensure compliance with federal securities laws. Other law determines whether such restrictions are permissible. This section deals only with the consequences of failure to note the restriction on a security certificate.

This section imposes no bar to enforcement of a restriction on transfer against a person who has actual knowledge of it.

2. A restriction on transfer of a certificated security is ineffective against a person without knowledge of the restriction unless the restriction is noted conspicuously on the certificate. The word "noted" is used to make clear that the restriction need not be set forth in full text. Refusal by an issuer to register a transfer on the basis of an unnoted restriction would be a violation of the issuer's duty to register under Section 8-401 [30-8-411].

3. The policy of this section is the same as in Section 8-202 [30-8-212]. A purchaser who takes delivery of a certificated security is entitled to rely on the terms stated on the certificate. That policy obviously does not apply to uncertificated securities. For uncertificated securities, this section requires only that the registered owner has been notified of the restriction. Suppose, for example, that A is the registered owner of an uncertificated security, and that the issuer has notified A of a restriction on transfer. A agrees to sell the security to B, in violation of the restriction. A completes a written instruction directing the issuer to register transfer to B, and B pays A for the security at the time A delivers the instruction to B. A does not inform B of the restriction, and B does not otherwise have notice or knowledge of it at the time B pays and receives the instruction. B presents the instruction to the issuer, but the issuer refuses to register the transfer on the grounds that it would violate the restriction. The issuer has complied with this section, because it did notify the registered owner A of the restriction. The issuer's refusal to register transfer is not wrongful. B has an action against A for breach of transfer warranty, see Section 8-108(b)(4)(iii) [30-8-118(2)(d)(iii)]. B's mistake was treating an uncertificated security transaction in the fashion appropriate only for a certificated security. The mechanism for transfer

of uncertificated securities is registration of transfer on the books of the issuer; handing over an instruction only initiates the process. The purchaser should make arrangements to ensure that the price is not paid until it knows that the issuer has or will register transfer.

4. In the indirect holding system, investors neither take physical delivery of security certificates nor have uncertificated securities registered in their names. So long as the requirements of this section have been satisfied at the level of the relationship between the issuer and the securities intermediary that is a direct holder, this section does not preclude the issuer from enforcing a restriction on transfer. See Section 8-202(a) [30-8-212(1)] and Comment 2 thereto.

5. This section deals only with restrictions imposed by the issuer. Restrictions imposed by statute are not affected. See Quiner v. Marblehead Social Co., 10 Mass. 476 (1813); Madison Bank v. Price, 79 Kan. 289, 100 P. 280 (1909); Healey v. Steele Center Creamery Ass'n, 115 Minn. 451, 133 N.W. 69 (1911). Nor does it deal with private agreements between stockholders containing restrictive covenants as to the sale of the security.

30-8-215. Effect of unauthorized signature on security certificate.

Official Comment

Source: Section 8-205, U.C.C.

Official Comment:

1. The problem of forged or unauthorized signatures may arise where an employee of the issuer, transfer agent, or registrar has access to securities which the employee is required to prepare for issue by affixing the corporate seal or by adding a signature necessary for issue. This section is based upon the issuer's duty to avoid the negligent entrusting of securities to such persons. Issuers have long been held responsible for signatures placed upon securities by parties whom they have held out to the public as authorized to prepare such securities. See Fifth Avenue Bank of New York v. The Forty-Second & Grand Street Ferry Railroad Co., 137 N.Y. 231, 33 N.E. 378, 19 L.R.A. 331, 33 Am.St.Rep. 712 (1893); Jarvis v. Manhattan Beach Co., 148 N.Y. 652, 43 N.E. 68, 31 L.R.A. 776, 51 Am.St.Rep. 727 (1896). The "apparent authority" concept of some of the case-law, however, is here extended and this section expressly rejects the technical distinction, made by courts reluctant to recognize forged signatures, between cases where forgers sign signatures they are authorized to sign under proper circumstances and those in which they sign signatures they are never authorized to sign. Citizens' & Southern National Bank v. Trust Co. of Georgia, 50 Ga.App. 681, 179 S.E. 278 (1935). Normally the purchaser is not in a position to determine which signature a forger, entrusted with the preparation of securities, has "apparent authority" to sign. The issuer, on the other hand, can protect itself against such fraud by the careful selection and bonding of agents and employees, or by action over against transfer agents and registrars who in turn may bond their personnel.

2. The issuer cannot be held liable for the honesty of employees not entrusted, directly or indirectly, with the signing, preparation, or responsible handling of similar securities and whose possible commission of forgery it has no reason to anticipate. The result in such cases as Hudson Trust Co. v. American Linseed Co., 232 N.Y. 350, 134 N.E. 178 (1922), and Dollar Savings Fund & Trust Co. v. Pittsburgh Plate Glass Co., 213 Pa. 307, 62 A. 916, 5 Ann.Cas. 248 (1906) is here adopted.

3. This section is not concerned with forged or unauthorized indorsements, but only with unauthorized signatures of issuers, transfer agents, etc., placed upon security certificates during the course of their issue. The protection here stated is available to all purchasers for value without notice and not merely to subsequent purchasers.

30-8-216. Completion of alteration of security certificate.

Official Comment

Source: Section 8-206, U.C.C.

Official Comment:

1. The problem of forged or unauthorized signatures necessary for the issue or transfer of a security is not involved here, and a person in possession of a blank certificate is not, by this section, given authority to fill in blanks with such signatures. Completion of blanks left in a transfer instruction is dealt with elsewhere (Section 8-305(a) [30-8-335(1)]).

2. Blanks left upon issue of a security certificate are the only ones dealt with here, and a purchaser for value without notice is protected. A purchaser is not in a good position to determine whether blanks were completed by the issuer or by some person not authorized to complete them. On the other hand the issuer can protect itself by not placing its signature on the writing until the blanks are completed or, if it does sign before all blanks are completed, by carefully selecting

the agents and employees to whom it entrusts the writing after authentication. With respect to a security certificate that is completed by the issuer but later is altered, the issuer has done everything it can to protect the purchaser and thus is not charged with the terms as altered. However, it is charged according to the original terms, since it is not thereby prejudiced. If the completion or alteration is obviously irregular, the purchaser may not qualify as a purchaser who took without notice under this section.

3. Only the purchaser who physically takes the certificate is directly protected. However, a transferee may receive protection indirectly through Section 8-302(a) [30-8-332(1)].

4. The protection granted a purchaser for value without notice under this section is modified to the extent that an overissue may result where an incorrect amount is inserted into a blank (Section 8-210 [30-8-220]).

30-8-217. Rights and duties of issuer with respect to registered owners.

Official Comment

Source: Section 8-207, U.C.C.

Official Comment:

1. Subsection (a) [subsection (1)] states the issuer's right to treat the registered owner of a security as the person entitled to exercise all the rights of an owner. This right of the issuer is limited by the provisions of Part 4 of this article [Title 30, chapter 8, part 4]. Once there has been due presentation for registration of transfer, the issuer has a duty to register ownership in the name of the transferee. Section 8-401 [30-8-411]. Thus its right to treat the old registered owner as exclusively entitled to the rights of ownership must cease.

The issuer may under this section make distributions of money or securities to the registered owners of securities without requiring further proof of ownership, provided that such distributions are distributable to the owners of all securities of the same issue and the terms of the security do not require surrender of a security certificate as a condition of payment or exchange. Any such distribution shall constitute a defense against a claim for the same distribution by a person, even if that person is in possession of the security certificate and is a protected purchaser of the security. See PEB Commentary No. 4, dated March 10, 1990.

2. Subsection (a) [subsection (1)] is permissive and does not require that the issuer deal exclusively with the registered owner. It is free to require proof of ownership before paying out dividends or the like if it chooses to. Barbato v. Breeze Corporation, 128 N.J.L. 309, 26 A.2d 53 (1942).

3. This section does not operate to determine who is finally entitled to exercise voting and other rights or to receive payments and distributions. The parties are still free to incorporate their own arrangements as to these matters in seller-purchaser agreements which may be definitive as between them.

4. No change in existing state laws as to the liability of registered owners for calls and assessments is here intended; nor is anything in this section designed to estop record holders from denying ownership when assessments are levied if they are otherwise entitled to do so under state law. See State ex rel. Squire v. Murfey, Blosson & Co., 131 Ohio St. 289, 2 N.E.2d 866 (1936); Willing v. Delaplaine, 23 F.Supp. 579 (1937).

5. No interference is intended with the common practice of closing the transfer books or taking a record date for dividend, voting, and other purposes, as provided for in by-laws, charters, and statutes.

Case Notes

DECISIONS UNDER UNIFORM STOCK TRANSFER ACT

Rights of Assignee: Where corporate officers wrongfully refuse to transfer stock on the books of the corporation at the request of an assignee thereof, its refusal constitutes a conversion of the stock and the assignee may sue for the recovery of its value. Gillies v. Robert E. Lee Min. Co., 78 M 402, 254 P 422 (1927).

30-8-218. Effect of signature of authenticating trustee, registrar, or transfer agent.

Official Comment

Source: Section 8-208, U.C.C.

Official Comment:

1. The warranties here stated express the current understanding and prevailing case law as to the effect of the signatures of authenticating trustees, transfer agents, and registrars. See Jarvis v. Manhattan Beach Co., 148 N.Y. 652, 43 N.E. 68, 31 L.R.A. 776, 51 Am.St.Rep. 727 (1896). Although it has generally been regarded as the particular obligation of the transfer agent

to determine whether securities are in proper form as provided by the by-laws and Articles of Incorporation, neither a registrar nor an authenticating trustee should properly place a signature upon a certificate without determining whether it is at least regular on its face. The obligations of these parties in this respect have therefore been made explicit in terms of due care. See Feldmeier v. Mortgage Securities, Inc., 34 Cal.App.2d 201, 93 P.2d 593 (1939).

2. Those cases which hold that an authenticating trustee is not liable for any defect in the mortgage or property which secures the bond or for any fraudulent misrepresentations made by the issuer are not here affected since these matters do not involve the genuineness or proper form of the security. Ainsa v. Mercantile Trust Co., 174 Cal. 504, 163 P. 898 (1917); Tschetinian v. City Trust Co., 186 N.Y. 432, 79 N.E. 401 (1906); Davidge v. Guardian Trust Co. of New York, 203 N.Y. 331, 96 N.E. 751 (1911).

3. The charter or an applicable statute may affect the capacity of a bank or other corporation undertaking to act as an authenticating trustee, registrar, or transfer agent. See, for example, the Federal Reserve Act (U.S.C.A., Title 12, Banks and Banking, Section 248) under which the Board of Governors of the Federal Reserve Bank is authorized to grant special permits to National Banks permitting them to act as trustees. Such corporations are therefore held to certify as to their legal capacity to act as well as to their authority.

4. Authenticating trustees, registrars, and transfer agents have normally been held liable for an issue in excess of the authorized amount. Jarvis v. Manhattan Beach Co., supra; Mullen v. Eastern Trust & Banking Co., 108 Me. 498, 81 A. 948 (1911). In imposing upon these parties a duty of due care with respect to the amount they are authorized to help issue, this section does not necessarily validate the security, but merely holds persons responsible for the excess issue liable in damages for any loss suffered by the purchaser.

5. Aside from questions of genuineness and excess issue, these parties are not held to certify as to the validity of the security unless they specifically undertake to do so. The case law which has recognized a unique responsibility on the transfer agent's part to testify as to the validity of any security which it countersigns is rejected.

6. This provision does not prevent a transfer agent or issuer from agreeing with a registrar of stock to protect the registrar in respect of the genuineness and proper form of a security certificate signed by the issuer or the transfer agent or both. Nor does it interfere with proper indemnity arrangements between the issuer and trustees, transfer agents, registrars, and the like.

7. An unauthorized signature is a signature for purposes of this section if and only if it is made effective by Section 8-205 [30-8-215].

30-8-219. Issuer's lien.

Official Comment

Source: Section 8-209, U.C.C.

Official Comment:

This section is similar to Sections 8-202 and 8-204 [30-8-212 and 30-8-214] which require that the terms of a certificated security and any restriction on transfer imposed by the issuer be noted on the security certificate. This section differs from those two sections in that the purchaser's knowledge of the issuer's claim is irrelevant. "Noted" makes clear that the text of the lien provisions need not be set forth in full. However, this would not override a provision of an applicable corporation code requiring statement in *haec verba*. This section does not apply to uncertificated securities. It applies to the indirect holding system in the same fashion as Sections 8-202 and 8-204 [30-8-212 and 30-8-214], see Comment 2 to Section 8-202 [30-8-212].

30-8-220. Overissue.

Official Comment

Source: Section 8-210, U.C.C.

Official Comment:

1. Deeply embedded in corporation law is the conception that "corporate power" to issue securities stems from the statute, either general or special, under which the corporation is organized. Corporation codes universally require that the charter or articles of incorporation state, at least as to capital shares, maximum limits in terms of number of shares or total dollar capital. Historically, special incorporation statutes are similarly drawn and sometimes similarly limit the face amount of authorized debt securities. The theory is that issue of securities in excess of the authorized amounts is prohibited. See, for example, McWilliams v. Geddes & Moss Undertaking Co., 169 So. 894 (1936, La.); Crawford v. Twin City Oil Co., 216 Ala. 216, 113 So. 61 (1927); New York and New Haven R.R. Co. v. Schuyler, 34 N.Y. 30 (1865). This conception

persists despite modern corporation codes under which, by action of directors and stockholders, additional shares can be authorized by charter amendment and thereafter issued. This section does not give a person entitled to validation, issue, or reissue of a security, the right to compel amendment of the charter to authorize additional shares. Therefore, in a case where issue of an additional security would require charter amendment, the plaintiff is limited to the two alternate remedies set forth in subsections (c) and (d) [subsections (3) and (4)]. The last clause of subsection (a) [subsection (1)], which is added in Revised Article 8 [Title 30, chapter 8], does, however, recognize that under modern conditions, overissue may be a relatively minor technical problem that can be cured by appropriate action under governing corporate law.

2. Where an identical security is reasonably available for purchase, whether because traded on an organized market, or because one or more security owners may be willing to sell at a not unreasonable price, the issuer, although unable to issue additional shares, will be able to purchase them and may be compelled to follow that procedure. West v. Tintic Standard Mining Co., 71 Utah 158, 263 P. 490 (1928).

3. The right to recover damages from an issuer who has permitted an overissue to occur is well settled. New York and New Haven R.R. Co. v. Schuyler, 34 N.Y. 30 (1865). The measure of such damages, however, has been open to question, some courts basing them upon the value of stock at the time registration is refused; some upon the value at the time of trial; and some upon the highest value between the time of refusal and the time of trial. Allen v. South Boston Railroad, 150 Mass. 200, 22 N.E. 917, 5 L.R.A. 716, 15 Am.St.Rep. 185 (1889); Commercial Bank v. Kortright, 22 Wend. (N.Y.) 348 (1839). The purchase price of the security to the last purchaser who gave value for it is here adopted as being the fairest means of reducing the possibility of speculation by the purchaser. Interest may be recovered by the best available measure of compensation for delay.

Part 3
Transfer of Certificated and Uncertificated Securities

30-8-331. Delivery.

Official Comment

Source: Section 8-301, U.C.C.

Official Comment:

1. This section specifies the requirements for "delivery" of securities. Delivery is used in Article 8 [Title 30, chapter 8] to describe the formal steps necessary for a purchaser to acquire a direct interest in a security under this Article [chapter]. The concept of delivery refers to the implementation of a transaction, not the legal categorization of the transaction which is consummated by delivery. Issuance and transfer are different kinds of transaction, though both may be implemented by delivery. Sale and pledge are different kinds of transfers, but both may be implemented by delivery.

2. Subsection (a) [subsection (1)] defines delivery with respect to certificated securities. Paragraph (1) [subsection (1)(a)] deals with simple cases where purchasers themselves acquire physical possession of certificates. Paragraphs (2) and (3) of subsection (a) [subsections (1)(b) and (1)(c)] specify the circumstances in which delivery to a purchaser can occur although the certificate is in the possession of a person other than the purchaser. Paragraph (2) [subsection (1)(b)] contains the general rule that a purchaser can take delivery through another person, so long as the other person is actually acting on behalf of the purchaser or acknowledges that it is holding on behalf of the purchaser. Paragraph (2) [subsection (1)(b)] does not apply to acquisition of possession by a securities intermediary, because a person who holds securities through a securities account acquires a security entitlement, rather than having a direct interest. See Section 8-501 [30-8-501]. Subsection (a)(3) [subsection (1)(c)] specifies the limited circumstances in which delivery of security certificates to a securities intermediary is treated as a delivery to the customer. Note that delivery is a method of perfecting a security interest in a certificated security. See Section 9-313(a), (e) [30-9A-313(1) and (5)].

3. Subsection (b) [subsection (2)] defines delivery with respect to uncertificated securities. Use of the term "delivery" with respect to uncertificated securities, does, at least on first hearing, seem a bit solecistic. The word "delivery" is, however, routinely used in the securities business in a broader sense than manual tradition. For example, settlement by entries on the books of a clearing corporation is commonly called "delivery," as in the expression "delivery versus payment." The diction of this section has the advantage of using the same term for uncertificated securities as for certificated securities, for which delivery is conventional usage. Paragraph (1)

of subsection (b) [subsection (2)(a)] provides that delivery occurs when the purchaser becomes the registered owner of an uncertificated security, either upon original issue or registration of transfer. Paragraph (2) [subsection (2)(b)] provides for delivery of an uncertificated security through a third person, in a fashion analogous to subsection (a)(2) [subsection (1)(b)].

Compiler's Comments

1999 Amendment: Chapter 305 inserted (1)(c)(i) concerning registration in name of purchaser; inserted (1)(c)(ii) concerning payability to order of purchaser; in (1)(c)(iii) at end inserted "and has not been indorsed to the securities intermediary or in blank"; and made minor changes in style. Amendment effective July 1, 2001.

Case Notes

DECISIONS UNDER UNIFORM STOCK TRANSFER ACT

Delivery of Shares:

Stocks which had been purchased by the deceased with his own funds and had been issued jointly to him and his son and daughter with right of survivorship and to son and daughter as tenants in common, deposited in safety deposit boxes rented in the names of the owners who had inspected the stock in the safety deposit boxes and included dividends from stocks in individual income tax returns, were delivered by the donor to the donees and did not belong to deceased at the time of his death so as to be a part of his estate. Marans v. Newland, 141 M 32, 374 P2d 721 (1962).

In suit to determine rights of respective administrators of estates of husband and wife, who had been killed in automobile accident, to unendorsed stock certificate in maiden name of wife, evidence of the finding of such unendorsed stock certificate in the joint safety-deposit box of both husband and wife, together with a separate assignment of the stock certificate to the husband signed by the wife, did not show a delivery to the husband so as to pass title. Lyons v. Freshman, 124 M 485, 226 P2d 775, 23 ALR 2d 1165 (1951).

30-8-332. Rights of purchaser.

Official Comment

Source: Section 8-302, U.C.C.

Official Comment:

1. Subsection (a) [subsection (1)] provides that a purchaser of a certificated or uncertificated security acquires all rights that the transferor had or had power to transfer. This statement of the familiar "shelter" principle is qualified by the exceptions that a purchaser of a limited interest acquires only that interest, subsection (b) [subsection (2)], and that a person who does not qualify as a protected purchaser cannot improve its position by taking from a subsequent protected purchaser, subsection (c) [subsection (3)].

2. Although this section provides that a purchaser acquires a property interest in a certificated or uncertificated security, it does not state that a person can acquire an interest in a security only by purchase. Article 8 [Title 30, chapter 8] also is not a comprehensive codification of all of the law governing the creation or transfer of interests in securities by purchase. For example, the grant of a security interest is a transfer of a property interest, but the formal steps necessary to effectuate such a transfer are governed by Article 9 [Title 30, chapter 9A] not by Article 8 [Title 30, chapter 8]. Under the Article 9 [Title 30, chapter 9A] rules, a security interest in a certificated or uncertificated security can be created by execution of a security agreement under Section 9-203 [30-9-203, now repealed, see 30-9A-203] and can be perfected by filing. A transfer of an Article 9 [Title 30, chapter 9A] security interest can be implemented by an Article 8 [Title 30, chapter 8] delivery, but need not be.

Similarly, Article 8 [Title 30, chapter 8] does not determine whether a property interest in certificated or uncertificated security is acquired under other law, such as the law of gifts, trusts, or equitable remedies. Nor does Article 8 [Title 30, chapter 8] deal with transfers by operation of law. For example, transfers from decedent to administrator, from ward to guardian, and from bankrupt to trustee in bankruptcy are governed by other law as to both the time they occur and the substance of the transfer. The Article 8 [Title 30, chapter 8] rules do, however, determine whether the issuer is obligated to recognize the rights that a third party, such as a transferee, may acquire under other law. See Sections 8-207, 8-401, and 8-404 [30-8-217, 30-8-411, 30-8-414].

Compiler's Comments

1999 Amendment: Chapter 305 in (1) after "(3)" substituted "a purchaser of a certificated or uncertificated security" for "upon delivery of a certificated or uncertificated security to a purchaser, the purchaser". Amendment effective July 1, 2001.

Case Notes

DECISIONS UNDER UNIFORM STOCK TRANSFER ACT

Foreclosure Sale: Sale of all corporation's stock in foreclosure without transfer of record or issuance of new certificates did not vacate presidency of incumbent of such office, so as to make service of process on him invalid as to corporation. In re Sharp Bros., 2 F. Supp. 227 (D.C. Mont. 1933).

If Corporation Has Notice of Transfer, Must Pay Dividend to Transferee: Stockholder of defendant pledged share to plaintiff and agreed dividends should be paid the pledgee. Pledgee notified defendant of the pledge but the stock was never transferred on the books of the corporation. In suit by pledgee to recover value of dividends declared, section 15-603, R.C.M. 1947 (now repealed), did not constitute a defense, and since the corporation had actual notice of pledgee's right to the dividends, although not an owner of record, the corporation was liable. Homestake Oil Co. v. Rigler, 39 F2d 40 (1930).

DECISIONS UNDER UNIFORM NEGOTIABLE INSTRUMENTS LAW

Failure to Call All Witnesses: Where all the persons concerned in the purchase of a note are called to testify to good faith, failure to call the president of the corporation does not as a matter of law make the proof of good faith insufficient. Grosfield v. First Nat'l Bank of Miles City, 73 M 219, 236 P 250 (1925).

30-8-333. Protected purchaser.

Official Comment

Source: Section 8-303, U.C.C.

Official Comment:

1. Subsection (a) [subsection (1)] lists the requirements that a purchaser must meet to qualify as a "protected purchaser." Subsection (b) [subsection (2)] provides that a protected purchaser takes its interest free from adverse claims. "Purchaser" is defined broadly in Section 1-201 [30-1-201]. A secured party as well as an outright buyer can qualify as a protected purchaser. Also, "purchase" includes taking by issue, so a person to whom a security is originally issued can qualify as a protected purchaser.

2. To qualify as a protected purchaser, a purchaser must give value, take without notice of any adverse claim, and obtain control. Value is used in the broad sense defined in Section 1-201(44) [30-1-201(44)]. See also Section 8-116 [30-8-126] (securities intermediary as purchaser for value). Adverse claim is defined in Section 8-102(a)(1) [30-8-112(1)(a)]. Section 8-105 [30-8-115] specifies whether a purchaser has notice of an adverse claim. Control is defined in Section 8-106 [30-8-116]. To qualify as a protected purchaser there must be a time at which all of the requirements are satisfied. Thus if a purchaser obtains notice of an adverse claim before giving value or satisfying the requirements for control, the purchaser cannot be a protected purchaser. See also Section 8-304(d) [30-8-334(4)].

The requirement that a protected purchaser obtain control expresses the point that to qualify for the adverse claim cut-off rule a purchaser must take through a transaction that is implemented by the appropriate mechanism. By contrast, the rules in Part 2 [Title 30, chapter 8, part 2] provide that any purchaser for value of a security without notice of a defense may take free of the issuer's defense based on that defense. See Section 8-202 [30-8-212].

3. The requirements for control differ depending on the form of the security. For securities represented by bearer certificates, a purchaser obtains control by delivery. See Sections 8-106(a) and 8-301(a) [30-8-116(1) and 30-8-331(1)]. For securities represented by certificates in registered form, the requirements for control are: (1) delivery as defined in Section 8-301(b) [30-8-331(2)], plus (2) either an effective indorsement or registration of transfer by the issuer. See Section 8-106(b) [30-8-116(2)]. Thus, a person who takes through a forged indorsement does not qualify as a protected purchaser by virtue of the delivery alone. If, however, the purchaser presents the certificate to the issuer for registration of transfer, and the issuer registers transfer over the forged indorsement, the purchaser can qualify as a protected purchaser of the new certificate. If the issuer registers transfer on a forged indorsement, the true owner will be able to recover from the issuer for wrongful registration, see Section 8-404 [30-8-414], unless the owner's delay in notifying the issuer of a loss or theft of the certificate results in preclusion under Section 8-406 [30-8-416].

For uncertificated securities, a purchaser can obtain control either by delivery, see Sections 8-106(c)(1) and 8-301(b) [30-8-116(3)(a) and 30-8-331(2)], or by obtaining an agreement pursuant to which the issuer agrees to act on instructions from the purchaser without further consent from the registered owner, see Section 8-106(c)(2) [30-8-116(3)(b)]. The control agreement device of Section 8-106(c)(2) [30-8-116(3)(b)] takes the place of the "registered pledge" concept of the 1978 version of Article 8 [Title 30, chapter 8]. A secured lender who obtains a control agreement under Section 8-106(c)(2) [30-8-116(3)(b)] can qualify as a protected purchaser of an uncertificated security.

4. This section states directly the rules determining whether one takes free from adverse claims without using the phrase "good faith." Whether a person who takes under suspicious circumstances is disqualified is determined by the rules of Section 8-105 [30-8-115] on notice of adverse claims. The term "protected purchaser," which replaces the term "bona fide purchaser" used in the prior version of Article 8 [Title 30, chapter 8], is derived from the term "protected holder" used in the Convention on International Bills and Notes prepared by the United Nations Commission on International Trade Law ("UNCITRAL").

Case Notes

DECISIONS UNDER UNIFORM NEGOTIABLE INSTRUMENTS LAW

Nature of Transaction: Knowledge of chattel mortgage on goods does not prevent bona fide purchase by bank of note for the price thereof, where the bank holds the mortgage on agreement to release it on receiving the proceeds of a sale of the goods. Fleming v. Consol. Motor Sales Co., 74 M 245, 240 P 376 (1925).

Notice of Warranty: Notice of warranty of goods forming the consideration for a note does not, without knowledge that the goods did not meet the warranty, impugn the good faith of the holder. Baker St. Bank v. Grant, 54 M 7, 166 P 27 (1917).

Crediting Proceeds of Instrument — Consideration For Notes: Notes given to a bank cashier in order that he may substitute them for notes of his own held by the bank are supported by sufficient consideration where they are thus substituted and the cashier's notes are withdrawn and the balance after paying such obligations is in part credited to the cashier's account and in part withdrawn in cash. St. Bank v. Forsyth, 41 M 249, 108 P 914, 28 L.R.A., N.S. 501 (1910).

30-8-334. Indorsement.

Official Comment

Source: Section 8-304, U.C.C.

Official Comment:

1. By virtue of the definition of indorsement in Section 8-102 [30-8-112] and the rules of this section, the simplified method of indorsing certificated securities previously set forth in the Uniform Stock Transfer Act is continued. Although more than one special indorsement on a given security certificate is possible, the desire for dividends or interest, as the case may be, should operate to bring the certificate home for registration of transfer within a reasonable period of time. The usual form of assignment which appears on the back of a stock certificate or in a separate "power" may be filled up either in the form of an assignment, a power of attorney to transfer, or both. If it is not filled up at all but merely signed, the indorsement is in blank. If filled up either as an assignment or as a power of attorney to transfer, the indorsement is special.

2. Subsection (b) [subsection (2)] recognizes the validity of a "partial" indorsement, e.g., as to fifty shares of the one hundred represented by a single certificate. The rights of a transferee under a partial indorsement to the status of a protected purchaser are left to the case law.

3. Subsection (c) [subsection (3)] deals with the effect of an indorsement without delivery. There must be a voluntary parting with control in order to effect a valid transfer of a certificated security as between the parties. Levey v. Nason, 279 Mass. 268, 181 N.E. 193 (1932), and National Surety Co. v. Indemnity Insurance Co. of North America, 237 App.Div. 485, 261 N.Y.S. 605 (1933). The provision in Section 10 of the Uniform Stock Transfer Act that an attempted transfer without delivery amounts to a promise to transfer is omitted. Even under that Act the effect of such a promise was left to the applicable law of contracts, and this Article by making no reference to such situations intends to achieve a similar result. With respect to delivery there is no counterpart to subsection (d) [subsection (4)] on right to compel indorsement, such as is envisaged in Johnson v. Johnson, 300 Mass. 24, 13 N.E.2d 788 (1938), where the transferee under a written assignment was given the right to compel a transfer of the certificate.

4. Subsection (d) [subsection (4)] deals with the effect of delivery without indorsement. As between the parties the transfer is made complete upon delivery, but the transferee cannot become a protected purchaser until indorsement is made. The indorsement does not operate retroactively, and notice may intervene between delivery and indorsement so as to prevent the transferee from becoming a protected purchaser. Although a purchaser taking without a

necessary indorsement may be subject to claims of ownership, any issuer's defense of which the purchaser had no notice at the time of delivery will be cut off, since the provisions of this Article protect all purchasers for value without notice (Section 8-202 [30-8-212]).

The transferee's right to compel an indorsement where a security certificate has been delivered with intent to transfer is recognized in the case law. See Coats v. Guaranty Bank & Trust Co., 170 La. 871, 129 So. 513 (1930). A proper indorsement is one of the requisites of transfer which a purchaser of a certificated security has a right to obtain (Section 8-307 [30-8-337]). A purchaser may not only compel an indorsement under that section but may also recover for any reasonable expense incurred by the transferor's failure to respond to the demand for an indorsement.

5. Subsection (e) [subsection (5)] deals with the significance of an indorsement on a security certificate in bearer form. The concept of indorsement applies only to registered securities. A purported indorsement of bearer paper is normally of no effect. An indorsement "for collection," "for surrender" or the like, charges a purchaser with notice of adverse claims (Section 8-105(d) [30-8-115(4)]) but does not operate beyond this to interfere with any right the holder may otherwise possess to have the security registered.

6. Subsection (f) [subsection (6)] makes clear that the indorser of a security certificate does not warrant that the issuer will honor the underlying obligation. In view of the nature of investment securities and the circumstances under which they are normally transferred, a transferor cannot be held to warrant as to the issuer's actions. As a transferor the indorser, of course, remains liable for breach of the warranties set forth in this Article (Section 8-108 [30-8-118]).

Case Notes

DECISIONS UNDER UNIFORM STOCK TRANSFER ACT

Gift of Stock Certificate: Although endorsement may not be absolutely necessary to valid gift of stock certificates, fact that alleged donor had not endorsed certificates as required under former law was evidence that no delivery occurred and hence there was no valid gift. Bodine v. Bodine, 149 M 29, 422 P2d 650 (1967).

Assignment of Stock Certificate: In suit to determine rights of respective administrators of estates of husband and wife, who had been killed in automobile accident, to unendorsed stock certificate in maiden name of wife, evidence of the finding of such unendorsed stock certificate in the joint safety-deposit box of both husband and wife together with a separate assignment of the stock certificate to the husband signed by the wife, did not show a delivery to the husband so as to pass title. Lyons v. Freshman, 124 M 485, 226 P2d 775, 23 ALR 2d 1165 (1951).

30-8-335. Instruction.

Official Comment

Source: Section 8-305, U.C.C.

Official Comment:

1. The term instruction is defined in Section 8-102(a)(12) [30-8-112(1)(l)] as a notification communicated to the issuer of an uncertificated security directing that transfer be registered. Section 8-107 [30-8-117] specifies who may initiate an effective instruction.

Functionally, presentation of an instruction is quite similar to the presentation of an indorsed certificate for registration. Note that instruction is defined in terms of "communicate," see Section 8-102(a)(6) [30-8-112(1)(f)]. Thus, the instruction may be in the form of a writing signed by the registered owner or in any other form agreed upon by the issuer and the registered owner. Allowing nonwritten forms of instructions will permit the development and employment of means of transmitting instructions electronically.

When a person who originates an instruction leaves a blank and the blank later is completed, subsection (a) [subsection (1)] gives the issuer the same rights it would have had against the originating person had that person completed the blank. This is true regardless of whether the person completing the instruction had authority to complete it. Compare Section 8-206 [30-8-216] and its Comment, dealing with blanks left upon issue.

2. Subsection (b) [subsection (2)] makes clear that the originator of an instruction, like the indorser of a security certificate, does not warrant that the issuer will honor the underlying obligation, but does make warranties as a transferor under Section 8-108 [30-8-118].

Case Notes

DECISIONS UNDER UNIFORM NEGOTIABLE INSTRUMENTS LAW

Forgery: A collecting bank which presents to the drawee bank a check on which the payee's endorsement is forged impliedly warrants the genuineness of the preceding endorsements and that it had good title. First Nat'l Bank in Miles City v. Fed. Reserve Bank of Minneapolis, 88 M 589, 294 P 1105 (1931).

Guarantor and Endorser — Liability Distinguished: While a grantor is liable for the debt, default, or miscarriage of the principal, an endorser engages, under 30-8-306 (now repealed), that on presentation of the obligation it will be accepted or paid or both, according to its tenure. Baroch v. Greater Mont. Oil Co., 70 M 93, 225 P 800 (1924).

30-8-336. Effect of guaranteeing signature, indorsement, or instruction.

Official Comment

Source: Section 8-306, U.C.C.

Official Comment:

1. Subsection (a) [subsection (1)] provides that a guarantor of the signature of the indorser of a security certificate warrants that the signature is genuine, that the signer is an appropriate person or has actual authority to indorse on behalf of the appropriate person, and that the signer has legal capacity. Subsection (b) [subsection (2)] provides similar, though not identical, warranties for the guarantor of a signature of the originator of an instruction for transfer of an uncertificated security.

Appropriate person is defined in Section 8-107(a) [30-8-117(1)] to include a successor or person who has power under other law to act for a person who is deceased or lacks capacity. Thus if a certificate registered in the name of Mary Roe is indorsed by Jane Doe as executor of Mary Roe, a guarantor of the signature of Jane Doe warrants that she has power to act as executor.

Although the definition of appropriate person in Section 8-107(a) [30-8-117(1)] does not itself include an agent, an indorsement by an agent is effective under Section 8-107(b) [30-8-117(2)] if the agent has authority to act for the appropriate person. Accordingly, this section provides an explicit warranty of authority for agents.

2. The rationale of the principle that a signature guarantor warrants the authority of the signer, rather than simply the genuineness of the signature, was explained in the leading case of Jennie Clarkson Home for Children v. Missouri, K. & T.R. Co., 182 N.Y. 47, 74 N.E. 571, 70 A.L.R. 787 (1905), which dealt with a guaranty of the signature of a person indorsing on behalf of a corporation. "If stock is held by an individual who is executing a power of attorney for its transfer, the member of the exchange who signs as a witness thereto guaranties not only the genuineness of the signature affixed to the power of attorney, but that the person signing is the individual in whose name the stock stands. With reference to stock standing in the name of a corporation, which can only sign a power of attorney through its authorized officers or agents, a different situation is presented. If the witnessing of the signature of the corporation is only that of the signature of a person who signs for the corporation, then the guaranty is of no value, and there is nothing to protect purchasers or the companies who are called upon to issue new stock in the place of that transferred from the frauds of persons who have signed the names of corporations without authority. If such is the only effect of the guaranty, purchasers and transfer agents must first go to the corporation in whose name the stock stands and ascertain whether the individual who signed the power of attorney had authority to do so. This will require time, and in many cases will necessitate the postponement of the completion of the purchase by the payment of the money until the facts can be ascertained. The broker who is acting for the owner has an opportunity to become acquainted with his customer, and may readily before sale ascertain, in case of a corporation, the name of the officer who is authorized to execute the power of attorney. It was therefore, we think, the purpose of the rule to cast upon the broker who witnesses the signature the duty of ascertaining whether the person signing the name of the corporation had authority to do so, and making the witness a guarantor that it is the signature of the corporation in whose name the stock stands."

3. Subsection (b) [subsection (2)] sets forth the warranties that can reasonably be expected from the guarantor of the signature of the originator of an instruction, who, though familiar with the signer, does not have any evidence that the purported owner is in fact the owner of the subject uncertificated security. This is in contrast to the position of the person guaranteeing a signature on a certificate who can see a certificate in the signer's possession in the name of or indorsed to the signer or in blank. Thus, the warranty in paragraph (2) of subsection (b) [subsection (2)(b)] is expressly conditioned on the actual registration's conforming to that represented by the originator. If the signer purports to be the owner, the guarantor under paragraph (2) [subsection (2)(b)], warrants only the identity of the signer. If, however, the signer is acting in a representative capacity, the guarantor warrants both the signer's identity and authority to act for the purported

owner. The issuer needs no warranty as to the facts of registration because those facts can be ascertained from the issuer's own records.

4. Subsection (c) [subsection (3)] sets forth a "special guaranty of signature" under which the guarantor additionally warrants both registered ownership and freedom from undisclosed defects of record. The guarantor of the signature of an indorser of a security certificate effectively makes these warranties to a purchaser for value on the evidence of a clean certificate issued in the name of the indorser, indorsed to the indorser or indorsed in blank. By specially guaranteeing under subsection (c) [subsection (3)], the guarantor warrants that the instruction will, when presented to the issuer, result in the requested registration free from defects not specified.

5. Subsection (d) [subsection (4)] makes clear that the warranties of a signature guarantor are limited to those specified in this section and do not include a general warranty of rightfulness. On the other hand subsections (e) and (f) [subsections (5) and (6)] provide that a person guaranteeing an indorsement or an instruction does warrant that the transfer is rightful in all respects.

6. Subsection (g) [subsection (7)] makes clear what can be inferred from the combination of Sections 8-401 and 8-402 [30-8-411 and 30-8-412], that the issuer may not require as a condition to transfer a guaranty of the indorsement or instruction nor may it require a special signature guaranty.

7. Subsection (h) [subsection (8)] specifies to whom the warranties in this section run, and also provides that a person who gives a guaranty under this section has an action against the indorser or originator for any loss suffered by the guarantor.

Case Notes

DECISIONS UNDER UNIFORM STOCK TRANSFER ACT

Transfer Books of Corporation: That equitable ownership of shares of stock might attach prior to evidence upon corporation's books of such ownership did not extinguish corporation's obligation to maintain its books and records in good faith so that records promptly reflected equitable ownership. Thisted v. Tower Management Corp., 147 M 1, 409 P2d 813 (1966).

Title of Transferee: Where seller's offer for sale of stock was accepted by buyer who made a $1,000 down payment thereon and seller delivered stock, duly certified and assigned, to his attorney for delivery to buyer upon payment of balance of purchase price and buyer as well as other stockholder took over corporation's assets and considered themselves at all times as sole owners of corporation, even though certificates of stock may not have actually been transferred on corporation's books, there was passage of title notwithstanding existence of attachment lien on stock unknown to seller who was willing to have that portion of purchase price applied on the above attachment as a cash bond to secure a buyer. Williams v. Kearns, 138 M 51, 353 P2d 748 (1960).

Transfer, Validity, Completeness: Delivery of stock certificate to assignee thereof must be proved by competent evidence to establish gift thereof to assignee. Lyons v. Freshman, 124 M 485, 226 P2d 775, 23 ALR 2d 1165 (1951).

30-8-337. Purchaser's right to requisites for registration of transfer.

Official Comment

Source: Section 8-307, U.C.C.

Official Comment:

1. Because registration of the transfer of a security is a matter of vital importance, a purchaser is here provided with the means of obtaining such formal requirements for registration as signature guaranties, proof of authority, transfer tax stamps and the like. The transferor is the one in a position to supply most conveniently whatever documentation may be requisite for registration of transfer, and the duty to do so upon demand within a reasonable time is here stated affirmatively. If an essential item is peculiarly within the province of the transferor so that the transferor is the only one who can obtain it, the purchaser may specifically enforce the right to obtain it. Compare Section 8-304(d) [30-8-334(4)]. If a transfer is not for value the transferor need not pay expenses.

2. If the transferor's duty is not performed the transferee may reject or rescind the contract to transfer. The transferee is not bound to do so. An action for damages for breach of contract may be preferred.

Part 4
Registration

30-8-411. Duty of issuer to register transfer.

Official Comment

Source: Section 8-401, U.C.C.

Official Comment:

1. This section states the duty of the issuer to register transfers. A duty exists only if certain preconditions exist. If any of the preconditions do not exist, there is no duty to register transfer. If an indorsement on a security certificate is a forgery, there is no duty. If an instruction to transfer an uncertificated security is not originated by an appropriate person, there is no duty. If there has not been compliance with applicable tax laws, there is no duty. If a security certificate is properly indorsed but nevertheless the transfer is in fact wrongful, there is no duty unless the transfer is to a protected purchaser (and the other preconditions exist).

This section does not constitute a mandate that the issuer must establish that all preconditions are met before the issuer registers a transfer. The issuer may waive the reasonable assurances specified in paragraph (a)(3) [subsection (1)(c)]. If it has confidence in the responsibility of the persons requesting transfer, it may ignore questions of compliance with tax laws. Although an issuer has no duty if the transfer is wrongful, the issuer has no duty to inquire into adverse claims, see Section 8-404 [30-8-414].

2. By subsection (b) [subsection (2)] the person entitled to registration may not only compel it but may hold the issuer liable in damages for unreasonable delay.

3. Section 8-201(c) [30-8-211(3)] provides that with respect to registration of transfer, "issuer" means the person on whose behalf transfer books are maintained. Transfer agents, registrars or the like within the scope of their respective functions have rights and duties under this Part similar to those of the issuer. See Section 8-407 [30-8-417].

30-8-412. Assurance that indorsement or instruction is effective.

Official Comment

Source: Section 8-402, U.C.C.

Official Comment:

1. An issuer is absolutely liable for wrongful registration of transfer if the indorsement or instruction is ineffective. See Section 8-404 [30-8-414]. Accordingly, an issuer is entitled to require such assurance as is reasonable under the circumstances that all necessary indorsements are effective, and thus to minimize its risk. This section establishes the requirements the issuer may make in terms of documentation which, except in the rarest of instances, should be easily furnished. Subsection (b) [subsection (2)] provides that an issuer may require additional assurances if that requirement is reasonable under the circumstances, but if the issuer demands more than reasonable assurance that the instruction or the necessary indorsements are genuine and authorized, the presenter may refuse the demand and sue for improper refusal to register. Section 8-401(b) [30-8-411(2)].

2. Under subsection (a)(1) [subsection (1)(a), the issuer may require in all cases a guaranty of signature. See Section 8-306 [30-8-336]. When an instruction is presented the issuer always may require reasonable assurance as to the identity of the originator. Subsection (c) [subsection (3)] allows the issuer to require that the person making these guaranties be one reasonably believed to be responsible, and the issuer may adopt standards of responsibility which are not manifestly unreasonable. Regulations under the federal securities laws, however, place limits on the requirements transfer agents may impose concerning the responsibility of eligible signature guarantors. See 17 CFR 240.17Ad15.

3. This section, by paragraphs (2) through (5) of subsection (a) [subsections (1)(b) through (1)(e)], permits the issuer to seek confirmation that the indorsement or instruction is genuine and authorized. The permitted methods act as a double check on matters which are within the warranties of the signature guarantor. See Section 8-306 [30-8-336]. Thus, an agent may be required to submit a power of attorney, a corporation to submit a certified resolution evidencing the authority of its signing officer to sign, an executor or administrator to submit the usual "shortform certificate," etc. But failure of a fiduciary to obtain court approval of the transfer or to comply with other requirements does not make the fiduciary's signature ineffective. Section 8-107(c) [30-8-117(3)]. Hence court orders and other controlling instruments are omitted from subsection (a) [subsection (1)].

Subsection (a)(3) [subsection (1)(c)] authorizes the issuer to require "appropriate evidence" of appointment or incumbency, and subsection (c) [subsection (3)] indicates what evidence will be "appropriate". In the case of a fiduciary appointed or qualified by a court that evidence will be a court certificate dated within sixty days before the date of presentation, subsection (c)(2)(i) [subsection (3)(b)(i)]. Where the fiduciary is not appointed or qualified by a court, as in the case of a successor trustee, subsection (c)(2)(ii) [subsection (3)(b)(ii)] applies. In that case, the issuer may require a copy of a trust instrument or other document showing the appointment, or it may require the certificate of a responsible person. In the absence of such a document or certificate, it may require other appropriate evidence. If the security is registered in the name of the fiduciary as such, the person's signature is effective even though the person is no longer serving in that capacity, see Section 8-107(d) [30-8-117(4)], hence no evidence of incumbency is needed.

4. Circumstances may indicate that a necessary signature was unauthorized or was not that of an appropriate person. Such circumstances would be ignored at risk of absolute liability. To minimize that risk the issuer may properly exercise the option given by subsection (b) [subsection (2)] to require assurance beyond that specified in subsection (a) [subsection (1)]. On the other hand, the facts at hand may reflect only on the rightfulness of the transfer. Such facts do not create a duty of inquiry, because the issuer is not liable to an adverse claimant unless the claimant obtains legal process. See Section 8-404 [30-8-414].

30-8-413. Demand that issuer not register transfer.

Official Comment

Source: Section 8-403, U.C.C.

Official Comment:

1. The general rule under this Article [chapter] is that if there has been an effective indorsement or instruction, a person who contends that registration of the transfer would be wrongful should not be able to interfere with the registration process merely by sending notice of the assertion to the issuer. Rather, the claimant must obtain legal process. See Section 8-404 [30-8-414]. Section 8-403 [30-8-413] is an exception to this general rule. It permits the registered owner—but not third parties—to demand that the issuer not register a transfer.

2. This section is intended to alleviate the problems faced by registered owners of certificated securities who lose or misplace their certificates. A registered owner who realizes that a certificate may have been lost or stolen should promptly report that fact to the issuer, lest the owner be precluded from asserting a claim for wrongful registration. See Section 8-406 [30-8-416]. The usual practice of issuers and transfer agents is that when a certificate is reported as lost, the owner is notified that a replacement can be obtained if the owner provides an indemnity bond. See Section 8-405 [30-8-415]. If the registered owner does not plan to transfer the securities, the owner might choose not to obtain a replacement, particularly if the owner suspects that the certificate has merely been misplaced.

Under this section, the owner's notification that the certificate has been lost would constitute a demand that the issuer not register transfer. No indemnity bond or legal process is necessary. If the original certificate is presented for registration of transfer, the issuer is required to notify the registered owner of that fact, and defer registration of transfer for a stated period. In order to prevent undue delay in the process of registration, the stated period may not exceed thirty days. This gives the registered owner an opportunity to either obtain legal process or post an indemnity bond and thereby prevent the issuer from registering transfer.

3. Subsection (e) [subsection (5)] makes clear that this section does not relieve an issuer from liability for registering a transfer pursuant to an ineffective indorsement. An issuer's liability for wrongful registration in such cases does not depend on the presence or absence of notice that the indorsement was ineffective. Registered owners who are confident that they neither indorsed the certificates, nor did anything that would preclude them from denying the effectiveness of another's indorsement, see Sections 8-107(b) and 8-406 [30-8-117(2) and 30-8-416], might prefer to pursue their rights against the issuer for wrongful registration rather than take advantage of the opportunity to post a bond or seek a restraining order when notified by the issuer under this section that their lost certificates have been presented for registration in apparently good order.

30-8-414. Wrongful registration.

Official Comment

Source: Section 8-404, U.C.C.

Official Comment:

1. Subsection (a)(1) [subsection (1)(a)] provides that an issuer is liable if it registers transfer pursuant to an indorsement or instruction that was not effective. For example, an issuer that

registers transfer on a forged indorsement is liable to the registered owner. The fact that the issuer had no reason to suspect that the indorsement was forged or that the issuer obtained the ordinary assurances under Section 8-402 [30-8-412] does not relieve the issuer from liability. The reason that issuers obtain signature guaranties and other assurances is that they are liable for wrongful registration.

Subsection (b) [subsection (2)] specifies the remedy for wrongful registration. PreCode cases established the registered owner's right to receive a new security where the issuer had wrongfully registered a transfer, but some cases also allowed the registered owner to elect between an equitable action to compel issue of a new security and an action for damages. Cf. Casper v. KaltZimmers Mfg. Co., 159 Wis. 517, 149 N.W. 754 (1914). Article 8 [Title 30, chapter 8] does not allow such election. The true owner of a certificated security is required to take a new security except where an overissue would result and a similar security is not reasonably available for purchase. See Section 8-210 [30-8-220]. The true owner of an uncertificated security is entitled and required to take restoration of the records to their proper state, with a similar exception for overissue.

2. Read together, subsections (c) and (a) [subsections (3) and (1)] have the effect of providing that an issuer has no duties to an adverse claimant unless the claimant serves legal process on the issuer to enjoin registration. Issuers, or their transfer agents, perform a record-keeping function for the direct holding system that is analogous to the functions performed by clearing corporations and securities intermediaries in the indirect holding system. This section applies to the record-keepers for the direct holding system the same standard that Section 8-115 [30-8-125] applies to the record-keepers for the indirect holding system. Thus, issuers are not liable to adverse claimants merely on the basis of notice. As in the case of the analogous rules for the indirect holding system, the policy of this section is to protect the right of investors to have their securities transfers processed without the disruption or delay that might result if the record-keepers risked liability to third parties. It would be undesirable to apply different standards to the direct and indirect holding systems, since doing so might operate as a disincentive to the development of a book-entry direct holding system.

3. This section changes prior law under which an issuer could be held liable, even though it registered transfer on an effective indorsement or instruction, if the issuer had in some fashion been notified that the transfer might be wrongful against a third party, and the issuer did not appropriately discharge its duty to inquire into the adverse claim. See Section 8-403 (1978) [former 30-8-403].

The rule of former Section 8-403 [former 30-8-403] was anomalous inasmuch as Section 8-207 [30-8-217] provides that the issuer is entitled to "treat the registered owner as the person exclusively entitled to vote, receive notifications, and otherwise exercise all the rights and powers of an owner." Under Section 8-207 [30-8-217], the fact that a third person notifies the issuer of a claim does not preclude the issuer from treating the registered owner as the person entitled to the security. See Kerrigan v. American Orthodontics Corp., 960 F.2d 43 (7th Cir.1992). The change made in the present version of Section 8-404 [30-8-414] ensures that the rights of registered owners and the duties of issuers with respect to registration of transfer will be protected against third-party interference in the same fashion as other rights of registered ownership.

Case Notes

Judgment Transferring Stock to Rightful Owner — Stock Equivalent to Compensatory Award for Purposes of Punitive Damages: The plaintiff owned stock in the defendant company as a joint tenant with right of survivorship with his father. Two days prior to the father's death, the father attempted to unilaterally transfer all of the stock from his son to his wife; however, he passed away before the proper signatures were made to allow for the transfer. Nevertheless, the defendant company transferred the stock to the decedent's wife without authorization from the son. After the son unsuccessfully attempted to have the stock transferred back to him, he filed an action alleging fraud and breach of fiduciary duty and sought punitive damages. The District Court ordered that all of the stock be transferred to the son and awarded punitive damages. The defendant company appealed, claiming that the transfer of stock could not be considered compensatory damages for purposes of awarding punitive damages. The Supreme Court affirmed, holding that the stock transfer was equivalent to the awarding of compensatory damages. In re Estate of Cote, 2019 MT 10, 394 Mont. 68, 433 P.3d 221.

30-8-415. Replacement of lost, destroyed, or wrongfully taken security certificate.

Official Comment

Source: Section 8-405, U.C.C.

Official Comment:

1. This section enables the owner to obtain a replacement of a lost, destroyed or stolen certificate, provided that reasonable requirements are satisfied and a sufficient indemnity bond supplied.

2. Where an "original" security certificate has reached the hands of a protected purchaser, the registered owner—who was in the best position to prevent the loss, destruction or theft of the security certificate—is now deprived of the new security certificate issued as a replacement. This changes the pre-UCC law under which the original certificate was ineffective after the issue of a replacement except insofar as it might represent an action for damages in the hands of a purchaser for value without notice. Keller v. Eureka Brick Mach. Mfg. Co., 43 Mo.App. 84, 11 L.R.A. 472 (1890). Where both the original and the new certificate have reached protected purchasers the issuer is required to honor both certificates unless an overissue would result and the security is not reasonably available for purchase. See Section 8-210 [30-8-220]. In the latter case alone, the protected purchaser of the original certificate is relegated to an action for damages. In either case, the issuer itself may recover on the indemnity bond.

30-8-416. Obligation to notify issuer of lost, destroyed, or wrongfully taken security certificate.

Official Comment

Source: Section 8-406, U.C.C.

Official Comment:

An owner who fails to notify the issuer within a reasonable time after the owner knows or has reason to know of the loss or theft of a security certificate is estopped from asserting the ineffectiveness of a forged or unauthorized indorsement and the wrongfulness of the registration of the transfer. If the lost certificate was indorsed by the owner, then the registration of the transfer was not wrongful under Section 8-404 [30-8-414], unless the owner made an effective demand that the issuer not register transfer under Section 8-403 [30-8-413].

30-8-417. Authenticating trustee, transfer agent, and registrar.

Official Comment

Source: Section 8-407, U.C.C.

Official Comment:

1. Transfer agents, registrars, and the like are here expressly held liable both to the issuer and to the owner for wrongful refusal to register a transfer as well as for wrongful registration of a transfer in any case within the scope of their respective functions where the issuer would itself be liable. Those cases which have regarded these parties solely as agents of the issuer and have therefore refused to recognize their liability to the owner for mere nonfeasance, i.e., refusal to register a transfer, are rejected. Hulse v. Consolidated Quicksilver Mining Corp., 65 Idaho 768, 154 P.2d 149 (1944); Nicholson v. Morgan, 119 Misc. 309, 196 N.Y.Supp. 147 (1922); Lewis v. Hargadine-McKittrick Dry Goods Co., 305 Mo. 396, 274 S.W. 1041 (1924).

2. The practice frequently followed by authenticating trustees of issuing certificates of indebtedness rather than authenticating duplicate certificates where securities have been lost or stolen became obsolete in view of the provisions of Section 8-405 [30-8-415], which makes express provision for the issue of substitute securities. It is not a breach of trust or lack of due diligence for trustees to authenticate new securities. Cf. Switzerland General Ins. Co. v. N.Y.C. & H.R.R. Co., 152 App.Div. 70, 136 N.Y.S. 726 (1912).

Part 5
Security Entitlements

30-8-501. Securities account — acquisition of security entitlement from securities intermediary.

Official Comment

Source: Section 8-501, U.C.C.

Official Comment:

1. Part 5 [Title 30, chapter 8, part 5] rules apply to security entitlements, and Section 8-501(b) [30-8-501(2)] provides that a person has a security entitlement when a financial asset has been credited to a "securities account." Thus, the term "securities account" specifies the type of arrangements between institutions and their customers that are covered by Part 5 [Title 30, chapter 8, part 5]. A securities account is a consensual arrangement in which the intermediary undertakes to treat the customer as entitled to exercise the rights that comprise the financial

asset. The consensual aspect is covered by the requirement that the account be established pursuant to agreement. The term agreement is used in the broad sense defined in Section 1-201(3) [30-1-201(3)]. There is no requirement that a formal or written agreement be signed.

As the securities business is presently conducted, several significant relationships clearly fall within the definition of a securities account, including the relationship between a clearing corporation and its participants, a broker and customers who leave securities with the broker, and a bank acting as securities custodian and its custodial customers. Given the enormous variety of arrangements concerning securities that exist today, and the certainty that new arrangements will evolve in the future, it is not possible to specify all of the arrangements to which the term does and does not apply.

Whether an arrangement between a firm and another person concerning a security or other financial asset is a "securities account" under this Article [chapter] depends on whether the firm has undertaken to treat the other person as entitled to exercise the rights that comprise the security or other financial asset. Section 1-102 [30-1-102], however, states the fundamental principle of interpretation that the Code provisions should be construed and applied to promote their underlying purposes and policies. Thus, the question whether a given arrangement is a securities account should be decided not by dictionary analysis of the words of the definition taken out of context, but by considering whether it promotes the objectives of Article 8 [Title 30, chapter 8] to include the arrangement within the term securities account.

The effect of concluding that an arrangement is a securities account is that the rules of Part 5 [Title 30, chapter 8, part 5] apply. Accordingly, the definition of "securities account" must be interpreted in light of the substantive provisions in Part 5 [Title 30, chapter 8, part 5], which describe the core features of the type of relationship for which the commercial law rules of Revised Article 8 [Title 30, chapter 8] concerning security entitlements were designed. There are many arrangements between institutions and other persons concerning securities or other financial assets which do not fall within the definition of "securities account" because the institutions have not undertaken to treat the other persons as entitled to exercise the ordinary rights of an entitlement holder specified in the Part 5 [Title 30, chapter 8, part 5] rules. For example, the term securities account does not cover the relationship between a bank and its depositors or the relationship between a trustee and the beneficiary of an ordinary trust, because those are not relationships in which the holder of a financial asset has undertaken to treat the other as entitled to exercise the rights that comprise the financial asset in the fashion contemplated by the Part 5 [Title 30, chapter 8, part 5] rules.

In short, the primary factor in deciding whether an arrangement is a securities account is whether application of the Part 5 rules is consistent with the expectations of the parties to the relationship. Relationships not governed by Part 5 [Title 30, chapter 8, part 5] may be governed by other parts of Article 8 [Title 30, chapter 8] if the relationship gives rise to a new security, or may be governed by other law entirely.

2. Subsection (b) [subsection (2)] of this section specifies what circumstances give rise to security entitlements. Paragraph (1) of subsection (b) [subsection (2)(a)] sets out the most important rule. It turns on the intermediary's conduct, reflecting a basic operating assumption of the indirect holding system that once a securities intermediary has acknowledged that it is carrying a position in a financial asset for its customer or participant, the intermediary is obligated to treat the customer or participant as entitled to the financial asset. Paragraph (1) [subsection (2)(a)] does not attempt to specify exactly what accounting, record-keeping, or information transmission steps suffice to indicate that the intermediary has credited the account. That is left to agreement, trade practice, or rule in order to provide the flexibility necessary to accommodate varying or changing accounting and information processing systems. The point of paragraph (1) [subsection (2)(a)] is that once an intermediary has acknowledged that it is carrying a position for the customer or participant, the customer or participant has a security entitlement. The precise form in which the intermediary manifests that acknowledgment is left to private ordering.

Paragraph (2) of subsection (b) [subsection (2)(b)] sets out a different operational test, turning not on the intermediary's accounting system but on the facts that accounting systems are supposed to represent. Under paragraph (b)(2) [subsection (2)(b)] a person has a security entitlement if the intermediary has received and accepted a financial asset for credit to the account of its customer or participant. For example, if a customer of a broker or bank custodian delivers a security certificate in proper form to the broker or bank to be held in the customer's account, the customer acquires a security entitlement. Paragraph (b)(2) [subsection (2)(b)] also covers circumstances in which the intermediary receives a financial asset from a third person for credit to the account of the customer or participant. Paragraph (b)(2) [subsection (2)(b)] is not limited to circumstances in which the intermediary receives security certificates or other financial assets in physical form. Paragraph (b)(2) [subsection (2)(b)] also covers circumstances in which the intermediary acquires a security entitlement with respect to a financial asset which is to be credited to the account of the intermediary's own customer. For example, if a customer transfers her account from Broker A to Broker B, she acquires security entitlements against Broker B once the clearing corporation has credited the positions to Broker B's account. It should be noted, however, that paragraph (b)(2) [subsection (2)(b)] provides that a person acquires a security entitlement when the intermediary not only receives but also accepts the financial asset for credit to the account. This limitation is included to take account of the fact that there may be circumstances in which an intermediary has received a financial asset but is not willing to undertake the obligations that flow from establishing a security entitlement. For example, a security certificate which is sent to an intermediary may not be in proper form, or may represent a type of financial asset which the intermediary is not willing to carry for others. It should be noted that in all but extremely unusual cases, th [sic] circumstances covered by paragraph (2) [subsection (2)(b)] will also be covered by paragraph (1) [subsection (2)(a)], because the intermediary will have credited the positions to the customer's account.

Paragraph (3) of subsection (b) [subsection (2)(c)] sets out a residual test, to avoid any implication that the failure of an intermediary to make the appropriate entries to credit a position to a customer's securities account would prevent the customer from acquiring the rights of an entitlement holder under Part 5 [Title 30, chapter 8, part 5]. As is the case with the paragraph (2) [subsection (2)(b)] test, the paragraph (3) [subsection (2)(c)] test would not be needed for the ordinary cases, since they are covered by paragraph (1) [subsection (2)(a)].

3. In a sense, Section 8-501(b) [30-8-501(2)] is analogous to the rules set out in the provisions of Sections 8-313(1)(d) and 8-320 [former 30-8-313(1)(d) and 30-8-320] of the prior version of Article 8 [Title 30, chapter 8] that specified what acts by a securities intermediary or clearing corporation sufficed as a transfer of securities held in fungible bulk. Unlike the prior version of Article 8 [Title 30, chapter 8], however, this section is not based on the idea that an entitlement holder acquires rights only by virtue of a "transfer" from the securities intermediary to the entitlement holder. In the indirect holding system, the significant fact is that the securities intermediary has undertaken to treat the customer as entitled to the financial asset. It is up to the securities intermediary to take the necessary steps to ensure that it will be able to perform its undertaking. It is, for example, entirely possible that a securities intermediary might make entries in a customer's account reflecting that customer's acquisition of a certain security at a time when the securities intermediary did not itself happen to hold any units of that security. The person from whom the securities intermediary bought the security might have failed to deliver and it might have taken some time to clear up the problem, or there may have been an operational gap in time between the crediting of a customer's account and the receipt of securities from another securities intermediary. The entitlement holder's rights against the securities intermediary do not depend on whether or when the securities intermediary acquired its interests. Subsection (c) [subsection (3)] is intended to make this point clear. Subsection (c) [subsection (3)] does not mean that the intermediary is free to create security entitlements without itself holding sufficient financial assets to satisfy its entitlement holders. The duty of a securities intermediary to maintain sufficient assets is governed by Section 8-504 [30-8-504] and regulatory law. Subsection (c) [subsection (3)] is included only to make it clear the question whether a person has acquired a security entitlement does not depend on whether the intermediary has complied with that duty.

4. Part 5 of Article 8 [Title 30, chapter 8, part 5] sets out a carefully designed system of rules for the indirect holding system. Persons who hold securities through brokers or custodians have security entitlements that are governed by Part 5 [Title 30, chapter 8, part 5], rather than being treated as the direct holders of securities. Subsection (d) [subsection (4)] specifies the limited circumstance in which a customer who leaves a financial asset with a broker or other securities intermediary has a direct interest in the financial asset, rather than a security entitlement.

The customer can be a direct holder only if the security certificate, or other financial asset, is registered in the name of, payable to the order of, or specially indorsed to the customer, and has not been indorsed by the customer to the securities intermediary or in blank. The distinction between those circumstances where the customer can be treated as direct owner and those where the customer has a security entitlement is essentially the same as the distinction drawn under the federal bankruptcy code between customer name securities and customer property. The distinction does not turn on any form of physical identification or segregation. A customer who delivers certificates to a broker with blank indorsements or stock powers is not a direct holder but has a security entitlement, even though the broker holds those certificates in some form of separate safe-keeping arrangement for that particular customer. The customer remains the direct holder only if there is no indorsement or stock power so that further action by the customer is required to place the certificates in a form where they can be transferred by the broker.

The rule of subsection (d) [subsection (4)] corresponds to the rule set out in Section 8-301(a)(3) [30-8-331(1)(c)] specifying when acquisition of possession of a certificate by a securities intermediary counts as "delivery" to the customer.

5. Subsection (e) [subsection (5)] is intended to make clear that Part 5 [Title 30, chapter 8, part 5] does not apply to an arrangement in which a security is issued representing an interest in underlying assets, as distinguished from arrangements in which the underlying assets are carried in a securities account. A common mechanism by which new financial instruments are devised is that a financial institution that holds some security, financial instrument, or pool thereof, creates interests in that asset or pool which are sold to others. In many such cases, the interests so created will fall within the definition of "security" in Section 8-102(a)(15) [30-8-112(1)(o)]. If so, then by virtue of subsection (e) of Section 8-501 [30-8-501(5)], the relationship between the institution that creates the interests and the persons who hold them is not a security entitlement to which the Part 5 [Title 30, chapter 8, part 5] rules apply. Accordingly, an arrangement such as an American depositary receipt facility which creates freely transferable interests in underlying securities will be issuance of a security under Article 8 [Title 30, chapter 8] rather than establishment of a security entitlement to the underlying securities.

The subsection (e) [subsection (5)] rule can be regarded as an aspect of the definitional rules specifying the meaning of securities account and security entitlement. Among the key components of the definition of security in Section 8-102(a)(15) [30-8-112(1)(o)] are the "transferability" and "divisibility" tests. Securities, in the Article 8 [Title 30, chapter 8] sense, are fungible interests or obligations that are intended to be tradable. The concept of security entitlement under Part 5 [Title 30, chapter 8, part 5] is quite different. A security entitlement is the package of rights that a person has against the person's own intermediary with respect to the positions carried in the person's securities account. That package of rights is not, as such, something that is traded. When a customer sells a security that she had held through a securities account, her security entitlement is terminated; when she buys a security that she will hold through her securities account, she acquires a security entitlement. In most cases, settlement of a securities trade will involve termination of one person's security entitlement and acquisition of a security entitlement by another person. That transaction, however, is not a "transfer" of the same entitlement from one person to another. That is not to say that an entitlement holder cannot transfer an interest in her security entitlement as such; granting a security interest in a security entitlement is such a transfer. On the other hand, the nature of a security entitlement is that the intermediary is undertaking duties only to the person identified as the entitlement holder.

30-8-502. Assertion of adverse claim against entitlement holder.

Official Comment

Source: Section 8-502, U.C.C.

Official Comment:

1. The section provides investors in the indirect holding system with protection against adverse claims by specifying that no adverse claim can be asserted against a person who acquires a security entitlement under Section 8-501 [30-8-501] for value and without notice of the adverse claim. It plays a role in the indirect holding system analogous to the rule of the direct holding system that protected purchasers take free from adverse claims (Section 8-303 [30-8-333]).

This section does not use the locution "takes free from adverse claims" because that could be confusing as applied to the indirect holding system. The nature of indirect holding system is that an entitlement holder has an interest in common with others who hold positions in the same financial asset through the same intermediary. Thus, a particular entitlement holder's interest in the financial assets held by its intermediary is necessarily "subject to" the interests of others. See Section 8-503 [30-8-503]. The rule stated in this section might have been expressed by saying that a person who acquires a security entitlement under Section 8-501 [30-8-501] for value and without notice of adverse claims takes "that security entitlement" free from adverse claims. That formulation has not been used, however, for fear that it would be misinterpreted as suggesting that the person acquires a right to the underlying financial assets that could not be affected by the competing rights of others claiming through common or higher tier intermediaries. A security entitlement is a complex bundle of rights. This section does not deal with the question of what rights are in the bundle. Rather, this section provides that once a person has acquired the bundle, someone else cannot take it away on the basis of assertion that the transaction in which the security entitlement was created involved a violation of the claimant's rights.

2. Because securities trades are typically settled on a net basis by book-entry movements, it would ordinarily be impossible for anyone to trace the path of any particular security, no matter how the interest of parties who hold through intermediaries is described. Suppose, for example, that S has a 1000 share position in XYZ common stock through an account with a broker, Able & Co. S's identical twin impersonates S and directs Able to sell the securities. That same day, B places an order with Baker & Co., to buy 1000 shares of XYZ common stock. Later, S discovers the wrongful act and seeks to recover "her shares." Even if S can show that, at the stage of the trade, her sell order was matched with B's buy order, that would not suffice to show that "her shares" went to B. Settlement between Able and Baker occurs on a net basis for all trades in XYZ that day; indeed Able's net position may have been such that it received rather than delivered shares in XYZ through the settlement system.

In the unlikely event that this was the only trade in XYZ common stock executed in the market that day, one could follow the shares from S's account to B's account. The plaintiff in an action in conversion or similar legal action to enforce a property interest must show that the defendant has an item of property that belongs to the plaintiff. In this example, B's security entitlement is not the same item of property that formerly was held by S, it is a new package of rights that B acquired against Baker under Section 8-501 [30-8-501]. Principles of equitable remedies might, however, provide S with a basis for contending that if the position B received was the traceable product of the wrongful taking of S's property by S's twin, a constructive trust should be imposed on B's property in favor of S. See G. Palmer, The Law of Restitution § 2.14. Section 8-502 [30-8-502] ensures that no such claims can be asserted against a person, such as B in this example, who acquires a security entitlement under Section 8-501 [30-8-501] for value and without notice, regardless of what theory of law or equity is used to describe the basis of the assertion of the adverse claim.

In the above example, S would ordinarily have no reason to pursue B unless Able is insolvent and S's claim will not be satisfied in the insolvency proceedings. Because S did not give an entitlement order for the disposition of her security entitlement, Able must recredit her account for the 1000 shares of XYZ common stock. See Section 8-507(b) [30-8-507(2)].

3. The following examples illustrate the operation of Section 8-502 [30-8-502].

Example 1. Thief steals bearer bonds from Owner. Thief delivers the bonds to Broker for credit to Thief's securities account, thereby acquiring a security entitlement under Section 8-501(b) [30-8-501(2)]. Under other law, Owner may have a claim to have a constructive trust imposed on the security entitlement as the traceable product of the bonds that Thief misappropriated. Because Thief was himself the wrongdoer, Thief obviously had notice of Owner's adverse claim. Accordingly, Section 8-502 [30-8-502] does not preclude Owner from asserting an adverse claim against Thief.

Example 2. Thief steals bearer bonds from Owner. Thief owes a personal debt to Creditor. Creditor has a securities account with Broker. Thief agrees to transfer the bonds to Creditor as security for or in satisfaction of his debt to Creditor. Thief does so by sending the bonds to Broker for credit to Creditor's securities account. Creditor thereby acquires a security entitlement under Section 8-501(b) [30-8-501(2)]. Under other law, Owner may have a claim to have a constructive trust imposed on the security entitlement as the traceable product of the bonds that Thief misappropriated. Creditor acquired the security entitlement for value, since Creditor acquired it as security for or in satisfaction of Thief's debt to Creditor. See Section 1-201(44) [30-1-201(44)]. If Creditor did not have notice of Owner's claim, Section 8-502 [30-8-502] precludes any action by Owner against Creditor, whether framed in constructive trust or other theory. Section 8-105 [30-8-115] specifies what counts as notice of an adverse claim.

Example 3. Father, as trustee for Son, holds XYZ Co. shares in a securities account with Able & Co. In violation of his fiduciary duties, Father sells the XYZ Co. shares and uses the proceeds for personal purposes. Father dies, and his estate is insolvent. Assume implausibly that Son is able to trace the XYZ Co. shares and show that the "same shares" ended up in Buyer's securities account with Baker & Co. Section 8-502 [30-8-502] precludes any action by Son against Buyer, whether framed in constructive trust or other theory, provided that Buyer acquired the security entitlement for value and without notice of adverse claims.

Example 4. Debtor holds XYZ Co. shares in a securities account with Able & Co. As collateral for a loan from Bank, Debtor grants Bank a security interest in the security entitlement to the XYZ Co. shares. Bank perfects by a method which leaves Debtor with the ability to dispose of the shares. See Section 9-312 [30-9A-312]. In violation of the security agreement, Debtor sells the XYZ Co. shares and absconds with the proceeds. Assume implausibly that Bank is able to trace the XYZ Co. shares and show that the "same shares" ended up in Buyer's securities account with Baker & Co. Section 8-502 [30-8-502] precludes any action by Bank against Buyer, whether framed in constructive trust or other theory, provided that Buyer acquired the security entitlement for value and without notice of adverse claims.

Example 5. Debtor owns controlling interests in various public companies, including Acme and Ajax. Acme owns 60% of the stock of another public company, Beta. Debtor causes the Beta stock to be pledged to Lending Bank as collateral for Ajax's debt. Acme holds the Beta stock through an account with a securities custodian, C Bank, which in turn holds through Clearing Corporation. Lending Bank is also a Clearing Corporation participant. The pledge of the Beta stock is implemented by Acme instructing C Bank to instruct Clearing Corporation to debit C Bank's account and credit Lending Bank's account. Acme and Ajax both become insolvent. The Beta stock is still valuable. Acme's liquidator asserts that the pledge of the Beta stock for Ajax's debt was wrongful as against Acme and seeks to recover the Beta stock from Lending Bank. Because the pledge was implemented by an outright transfer into Lending Bank's account at Clearing Corporation, Lending Bank acquired a security entitlement to the Beta stock under Section 8-501 [30-8-501]. Lending Bank acquired the security entitlement for value, since it acquired it as security for a debt. See Section 1-201(44) [30-1-201(44)]. If Lending Bank did not have notice of Acme's claim, Section 8-502 [30-8-502] will preclude any action by Acme against Lending Bank, whether framed in constructive trust or other theory.

Example 6. Debtor grants Alpha Co. a security interest in a security entitlement that includes 1000 shares of XYZ Co. stock that Debtor holds through an account with Able & Co. Alpha also has an account with Able. Debtor instructs Able to transfer the shares to Alpha, and Able does so by crediting the shares to Alpha's account. Alpha has control of the 1000 shares under Section 8-106(d) [30-8-116(4)]. (The facts to this point are identical to those in Section 8-106 [30-8-116], Comment 4, Example 1, except that Alpha Co. was Alpha Bank.) Alpha next grants Beta Co. a security interest in the 1000 shares included in Alpha's security entitlement. See Section 9-207(c)(3) [30-9A-207(3)(c)]. Alpha instructs Able to transfer the shares to Gamma Co., Beta's custodian. Able does so, and Gamma credits the 1000 shares to Beta's account. Beta now has control under Section 8-106(d) [30-8-116(4)]. By virtue of Debtor's explicit permission or by virtue of the permission inherent in Debtor's creation of a security interest in favor of Alpha and Alpha's resulting power to grant a security interest under Section 9-207 [30-9A-207], Debtor has no adverse claim to assert against Beta, assuming implausibly that Debtor could "trace" an interest to the Gamma account. Moreover, even if Debtor did hold an adverse claim, if Beta did not have notice of Debtor's claim, Section 8-502 [30-8-502] will preclude any action by Debtor against Beta, whether framed in constructive trust or other theory.

4. Although this section protects entitlement holders against adverse claims, it does not protect them against the risk that their securities intermediary will not itself have sufficient financial assets to satisfy the claims of all of its entitlement holders. Suppose that Customer A holds 1000 shares of XYZ Co. stock in an account with her broker, Able & Co. Able in turn holds 1000 shares of XYZ Co. through its account with Clearing Corporation, but has no other positions in XYZ Co. shares, either for other customers or for its own proprietary account. Customer B places an order with Able for the purchase of 1000 shares of XYZ Co. stock, and pays the purchase price. Able credits B's account with a 1000 share position in XYZ Co. stock, but Able does not itself buy any additional XYZ Co. shares. Able fails, having only 1000 shares to satisfy the claims of A and B. Unless other insolvency law establishes a different distributional rule, A and B would share the 1000 shares held by Able pro rata, without regard to the time that their respective entitlements were established. See Section 8-503(b) [30-8-503(2)]. Section 8-502 [30-8-502] protects entitlement holders, such as A and B, against adverse claimants. In this case, however, the problem that A and B face is not that someone is trying to take away their entitlements, but that the entitlements are not worth what they thought. The only role that Section 8-502 [30-8-502] plays in this case is to preclude any assertion that A has some form of claim against B by virtue of the fact that Able's establishment of an entitlement in favor of B diluted A's rights to the limited assets held by Able.

30-8-503. Property interest of entitlement holder in financial asset held by securities intermediary.

Official Comment

Source: Section 8-503, U.C.C.

Official Comment:

1. This section specifies the sense in which a security entitlement is an interest in the property held by the securities intermediary. It expresses the ordinary understanding that securities that a firm holds for its customers are not general assets of the firm subject to the claims of creditors. Since securities intermediaries generally do not segregate securities in such fashion that one could identify particular securities as the ones held for customers, it would not be realistic for this section to state that "customers' securities" are not subject to creditors' claims. Rather subsection (a) [subsection (1)] provides that to the extent necessary to satisfy all customer claims, all units of that security held by the firm are held for the entitlement holders, are not property of the securities intermediary, and are not subject to creditors' claims, except as otherwise provided in Section 8-511 [30-8-511].

An entitlement holder's property interest under this section is an interest with respect to a specific issue of securities or financial assets. For example, customers of a firm who have positions in XYZ common stock have security entitlements with respect to the XYZ common stock held by the intermediary, while other customers who have positions in ABC common stock have security entitlements with respect to the ABC common stock held by the intermediary.

Subsection (b) [subsection (2)] makes clear that the property interest described in subsection (a) [subsection (1)] is an interest held in common by all entitlement holders who have entitlements to a particular security or other financial asset. Temporal factors are irrelevant. One entitlement holder cannot claim that its rights to the assets held by the intermediary are superior to the rights of another entitlement holder by virtue of having acquired those rights before, or after, the other entitlement holder. Nor does it matter whether the intermediary had sufficient assets to satisfy all entitlement holders' claims at one point, but no longer does. Rather, all entitlement holders have a pro rata interest in whatever positions in that financial asset the intermediary holds.

Although this section describes the property interest of entitlement holders in the assets held by the intermediary, it does not necessarily determine how property held by a failed intermediary will be distributed in insolvency proceedings. If the intermediary fails and its affairs are being administered in an insolvency proceeding, the applicable insolvency law governs how the various parties having claims against the firm are treated. For example, the distributional rules for stockbroker liquidation proceedings under the Bankruptcy Code and Securities Investor Protection Act ("SIPA") provide that all customer property is distributed pro rata among all customers in proportion to the dollar value of their total positions, rather than dividing the property on an issue by issue basis. For intermediaries that are not subject to the Bankruptcy Code and SIPA, other insolvency law would determine what distributional rule is applied.

2. Although this section recognizes that the entitlement holders of a securities intermediary have a property interest in the financial assets held by the intermediary, the incidents of this property interest are established by the rules of Article 8 [Title 30, chapter 8], not by common law property concepts. The traditional Article 8 [Title 30, chapter 8] rules on certificated securities were based on the idea that a paper certificate could be regarded as a nearly complete reification of the underlying right. The rules on transfer and the consequences of wrongful transfer could then be written using the same basic concepts as the rules for physical chattels. A person's claim of ownership of a certificated security is a right to a specific identifiable physical object, and that right can be asserted against any person who ends up in possession of that physical certificate, unless cut off by the rules protecting purchasers for value without notice. Those concepts do not work for the indirect holding system. A security entitlement is not a claim to a specific identifiable thing; it is a package of rights and interests that a person has against the person's securities intermediary and the property held by the intermediary. The idea that discrete objects might be traced through the hands of different persons has no place in the Revised Article 8 [Title 30, chapter 8] rules for the indirect holding system. The fundamental principles of the indirect holding system rules are that an entitlement holder's own intermediary has the obligation to see to it that the entitlement holder receives all of the economic and corporate rights that comprise the financial asset, and that the entitlement holder can look only to that intermediary for performance of the obligations. The entitlement holder cannot assert rights directly against other persons, such as other intermediaries through whom the intermediary holds the positions, or third parties to whom the intermediary may have wrongfully transferred interests, except in extremely unusual circumstances where the third party was itself a participant in the wrongdoing. Subsections (c) through (e) [subsections 3 through 5] reflect these fundamental principles.

Subsection (c) [subsection (3)] provides that an entitlement holder's property interest can be enforced against the intermediary only by exercise of the entitlement holder's rights under

Sections 8-505 through 8-508 [30-8-505 through 30-8-508]. These are the provisions that set out the duty of an intermediary to see to it that the entitlement holder receives all of the economic and corporate rights that comprise the security. If the intermediary is in insolvency proceedings and can no longer perform in accordance with the ordinary Part 5 [Title 30, chapter 8, part 5] rules, the applicable insolvency law will determine how the intermediary's assets are to be distributed.

Subsections (d) and (e) [subsections (4) and (5)] specify the limited circumstances in which an entitlement holder's property interest can be asserted against a third person to whom the intermediary transferred a financial asset that was subject to the entitlement holder's claim when held by the intermediary. Subsection (d) [subsection (4)] provides that the property interest of entitlement holders cannot be asserted against any transferee except in the circumstances therein specified. So long as the intermediary is solvent, the entitlement holders must look to the intermediary to satisfy their claims. If the intermediary does not hold financial assets corresponding to the entitlement holders' claims, the intermediary has the duty to acquire them. See Section 8-504 [30-8-504]. Thus, paragraphs (1), (2), and (3) of subsection (d) [subsections (4)(a), (4)(b), and (4)(c)] specify that the only occasion in which the entitlement holders can pursue transferees is when the intermediary is unable to perform its obligation, and the transfer to the transferee was a violation of those obligations. Even in that case, a transferee who gave value and obtained control is protected by virtue of the rule in subsection (e) [subsection (5)], unless the transferee acted in collusion with the intermediary.

Subsections (d) and (e) [subsections (4) and (5)] have the effect of protecting transferees from an intermediary against adverse claims arising out of assertions by the intermediary's entitlement holders that the intermediary acted wrongfully in transferring the financial assets. These rules, however, operate in a slightly different fashion than traditional adverse claim cut-off rules. Rather than specifying that a certain class of transferee takes free from all claims, subsections (d) and (e) [subsections (4) and (5)] specify the circumstances in which this particular form of claim can be asserted against a transferee. Revised Article 8 [Title 30, chapter 8] also contains general adverse claim cut-off rules for the indirect holding system. See Sections 8-502 and 8-510 [30-8-502 and 30-8-510]. The rule of subsections (d) and (e) [subsections (4) and (5)] takes precedence over the general cut-off rules of those sections, because Section 8-503 [30-8-503] itself defines and sets limits on the assertion of the property interest of entitlement holders. Thus, the question whether entitlement holders' property interest can be asserted as an adverse claim against a transferee from the intermediary is governed by the collusion test of Section 8-503(e) [30-8-503(5)], rather than by the "without notice" test of Sections 8-502 and 8-510 [30-8-502 and 30-8-510].

3. The limitations that subsections (c) through (e) [subsections (3) through (5)] place on the ability of customers of a failed intermediary to recover securities or other financial assets from transferees are consistent with the fundamental policies of investor protection that underlie this Article [chapter] and other bodies of law governing the securities business. The commercial law rules for the securities holding and transfer system must be assessed from the forward-looking perspective of their impact on the vast number of transactions in which no wrongful conduct occurred or will occur, rather than from the *post hoc* perspective of what rule might be most advantageous to a particular class of persons in litigation that might arise out of the occasional case in which someone has acted wrongfully. Although one can devise hypothetical scenarios where particular customers might find it advantageous to be able to assert rights against someone other than the customers' own intermediary, commercial law rules that permitted customers to do so would impair rather than promote the interest of investors and the safe and efficient operation of the clearance and settlement system. Suppose, for example, that Intermediary A transfers securities to B, that Intermediary A acted wrongfully as against its customers in so doing, and that after the transaction Intermediary A did not have sufficient securities to satisfy its obligations to its entitlement holders. Viewed solely from the standpoint of the customers of Intermediary A, it would seem that permitting the property to be recovered from B, would be good for investors. That, however, is not the case. B may itself be an intermediary with its own customers, or may be some other institution through which individuals invest, such as a pension fund or investment company. There is no reason to think that rules permitting customers of an intermediary to trace and recover securities that their intermediary wrongfully transferred work to the advantage of investors in general. To the contrary, application of such rules would often merely shift losses from one set of investors to another. The uncertainties that would result from rules permitting such recoveries would work to the disadvantage of all participants in the securities markets.

The use of the collusion test in Section 8-503(e) [30-8-503(5)] furthers the interests of investors generally in the sound and efficient operation of the securities holding and settlement system. The effect of the choice of this standard is that customers of a failed intermediary must show that the transferee from whom they seek to recover was affirmatively engaged in wrongful conduct, rather than casting on the transferee any burden of showing that the transferee had no awareness of wrongful conduct by the failed intermediary. The rule of Section 8-503(e) [30-8-503(5)] is based on the long-standing policy that it is undesirable to impose upon purchasers of securities any duty to investigate whether their sellers may be acting wrongfully.

Rather than imposing duties to investigate, the general policy of the commercial law of the securities holding and transfer system has been to eliminate legal rules that might induce participants to conduct investigations of the authority of persons transferring securities on behalf of others for fear that they might be held liable for participating in a wrongful transfer. The rules in Part 4 of Article 8 [Title 30, chapter 8, part 4] concerning transfers by fiduciaries provide a good example. Under Lowry v. Commercial & Farmers' Bank, 15 F.Cas. 1040 (C.C.D.Md.1848) (No. 8581), an issuer could be held liable for wrongful transfer if it registered transfer of securities by a fiduciary under circumstances where it had any reason to believe that the fiduciary may have been acting improperly. In one sense that seems to be advantageous for beneficiaries who might be harmed by wrongful conduct by fiduciaries. The consequence of the Lowry rule, however, was that in order to protect against risk of such liability, issuers developed the practice of requiring extensive documentation for fiduciary stock transfers, making such transfers cumbersome and time consuming. Accordingly, the rules in Part 4 of Article 8 [Title 30, chapter 8, part 4], and in the prior fiduciary transfer statutes, were designed to discourage transfer agents from conducting investigations into the rightfulness of transfers by fiduciaries.

The rules of Revised Article 8 [Title 30, chapter 8] implement for the indirect holding system the same policies that the rules on protected purchasers and registration of transfer adopt for the direct holding system. A securities intermediary is, by definition, a person who is holding securities on behalf of other persons. There is nothing unusual or suspicious about a transaction in which a securities intermediary sells securities that it was holding for its customers. That is exactly what securities intermediaries are in business to do. The interests of customers of securities intermediaries would not be served by a rule that required counterparties to transfers from securities intermediaries to investigate whether the intermediary was acting wrongfully against its customers. Quite the contrary, such a rule would impair the ability of securities intermediaries to perform the function that customers want.

The rules of Section 8-503(c) through (e) [30-8-503(3) through (5)] apply to transferees generally, including pledgees. The reasons for treating pledgees in the same fashion as other transferees are discussed in the Comments to Section 8-511 [30-8-511]. The statement in subsection (a) [subsection (1)] that an intermediary holds financial assets for customers and not as its own property does not, of course, mean that the intermediary lacks power to transfer the financial assets to others. For example, although Article 9 [Title 30, chapter 9A] provides that for a security interest to attach the debtor must have "rights" in the collateral, see Section 9-203 [30-9-203, now repealed, see 30-9A-203], the fact that an intermediary is holding a financial asset in a form that permits ready transfer means that it has such rights, even if the intermediary is acting wrongfully against its entitlement holders in granting the security interest. The question whether the secured party takes subject to the entitlement holder's claim in such a case is governed by Section 8-511 [30-8-511], which is an application to secured transactions of the general principles expressed in subsections (d) and (e) [subsections (4) and (5)] of this section.

30-8-504. Duty of securities intermediary to maintain financial asset.

Official Comment

Source: Section 8-504, U.C.C.

Official Comment:

1. This section expresses one of the core elements of the relationships for which the Part 5 [Title 30, chapter 8, part 5] rules were designed, to wit, that a securities intermediary undertakes to hold financial assets corresponding to the security entitlements of its entitlement holders. The locution "shall promptly obtain and shall thereafter maintain" is taken from the corresponding regulation under federal securities law, 17 C.F.R. § 240.15c3-3. This section recognizes the reality that as the securities business is conducted today, it is not possible to identify particular securities as belonging to customers as distinguished from other particular securities that are the firm's own property. Securities firms typically keep all securities in fungible form, and may maintain their inventory of a particular security in various locations and forms, including

physical securities held in vaults or in transit to transfer agents, and book entry positions at one or more clearing corporations. Accordingly, this section states that a securities intermediary shall maintain a quantity of financial assets corresponding to the aggregate of all security entitlements it has established. The last sentence of subsection (a) [subsection (1)] provides explicitly that the securities intermediary may hold directly or indirectly. That point is implicit in the use of the term "financial asset," inasmuch as Section 8-102(a)(9) [30-8-112(1)(i)] provides that the term "financial asset" may refer either to the underlying asset or the means by which it is held, including both security certificates and security entitlements.

2. Subsection (b) [subsection (2)] states explicitly a point that is implicit in the notion that a securities intermediary must maintain financial assets corresponding to the security entitlements of its entitlement holders, to wit, that it is wrongful for a securities intermediary to grant security interests in positions that it needs to satisfy customers' claims, except as authorized by the customers. This statement does not determine the rights of a secured party to whom a securities intermediary wrongfully grants a security interest; that issue is governed by Sections 8-503 and 8-511 [30-8-503 and 30-8-511].

Margin accounts are common examples of arrangements in which an entitlement holder authorizes the securities intermediary to grant security interests in the positions held for the entitlement holder. Securities firms commonly obtain the funds needed to provide margin loans to their customers by "rehypothecating" the customers' securities. In order to facilitate rehypothecation, agreements between margin customers and their brokers commonly authorize the broker to commingle securities of all margin customers for rehypothecation to the lender who provides the financing. Brokers commonly rehypothecate customer securities having a value somewhat greater than the amount of the loan made to the customer, since the lenders who provide the necessary financing to the broker need some cushion of protection against the risk of decline in the value of the rehypothecated securities. The extent and manner in which a firm may rehypothecate customers' securities are determined by the agreement between the intermediary and the entitlement holder and by applicable regulatory law. Current regulations under the federal securities laws require that brokers obtain the explicit consent of customers before pledging customer securities or commingling different customers' securities for pledge. Federal regulations also limit the extent to which a broker may rehypothecate customer securities to 110% of the aggregate amount of the borrowings of all customers.

3. The statement in this section that an intermediary must obtain and maintain financial assets corresponding to the aggregate of all security entitlements it has established is intended only to capture the general point that one of the key elements that distinguishes securities accounts from other relationships, such as deposit accounts, is that the intermediary undertakes to maintain a direct correspondence between the positions it holds and the claims of its customers. This section is not intended as a detailed specification of precisely how the intermediary is to perform this duty, nor whether there may be special circumstances in which an intermediary's general duty is excused. Accordingly, the general statement of the duties of a securities intermediary in this and the following sections is supplemented by two other provisions. First, each of Sections 8-504 through 8-508 [30-8-504 through 30-8-508] contains an "agreement/due care" provision. Second, Section 8-509 [30-8-509] sets out general qualifications on the duties stated in these sections, including the important point that compliance with corresponding regulatory provisions constitutes compliance with the Article 8 [Title 30, chapter 8] duties.

4. The "agreement/due care" provision in subsection (c) [subsection (3)] of this section is necessary to provide sufficient flexibility to accommodate the general duty stated in subsection (a) [subsection (1)] to the wide variety of circumstances that may be encountered in the modern securities holding system. For the most common forms of publicly traded securities, the modern depository-based indirect holding system has made the likelihood of an actual loss of securities remote, though correctable errors in accounting or temporary interruptions of data processing facilities may occur. Indeed, one of the reasons for the evolution of book-entry systems is to eliminate the risk of loss or destruction of physical certificates. There are, however, some forms of securities and other financial assets which must still be held in physical certificated form, with the attendant risk of loss or destruction. Risk of loss or delay may be a more significant consideration in connection with foreign securities. An American securities intermediary may well be willing to hold a foreign security in a securities account for its customer, but the intermediary may have relatively little choice of or control over foreign intermediaries through which the security must in turn be held. Accordingly, it is common for American securities intermediaries to disclaim responsibility for custodial risk of holding through foreign intermediaries.

Subsection (c)(1) [subsection (3)(a)] provides that a securities intermediary satisfies the duty stated in subsection (a) [subsection (1)] if the intermediary acts with respect to that duty in accordance with the agreement between the intermediary and the entitlement holder. Subsection (c)(2) [subsection (3)(b)] provides that if there is no agreement on the matter, the intermediary satisfies the subsection (a) [subsection (1)] duty if the intermediary exercises due care in accordance with reasonable commercial standards to obtain and maintain the financial asset in question. This formulation does not state that the intermediary has a universally applicable statutory duty of due care. Section 1-102(3) [30-1-102(3)] provides that statutory duties of due care cannot be disclaimed by agreement, but the "agreement/due care" formula contemplates that there may be particular circumstances where the parties do not wish to create a specific duty of due care, for example, with respect to foreign securities. Under subsection (c)(1) [subsection (3)(a)], compliance with the agreement constitutes satisfaction of the subsection (a) [subsection (1)] duty, whether or not the agreement provides that the intermediary will exercise due care.

In each of the sections where the "agreement/due care" formula is used, it provides that entering into an agreement and performing in accordance with that agreement is a method by which the securities intermediary may satisfy the statutory duty stated in that section. Accordingly, the general obligation of good faith performance of statutory and contract duties, see Sections 1-203 and 8-102(a)(10) [30-1-203 and 30-8-112(1)(j)], would apply to such an agreement. It would not be consistent with the obligation of good faith performance for an agreement to purport to establish the usual sort of arrangement between an intermediary and entitlement holder, yet disclaim altogether one of the basic elements that define that relationship. For example, an agreement stating that an intermediary assumes no responsibilities whatsoever for the safekeeping any of the entitlement holder's securities positions would not be consistent with good faith performance of the intermediary's duty to obtain and maintain financial assets corresponding to the entitlement holder's security entitlements.

To the extent that no agreement under subsection (c)(1) [subsection (3)(a)] has specified the details of the intermediary's performance of the subsection (a) [subsection (1)] duty, subsection (c)(2) [subsection (3)(b)] provides that the intermediary satisfies that duty if it exercises due care in accordance with reasonable commercial standards. The duty of care includes both care in the intermediary's own operations and care in the selection of other intermediaries through whom the intermediary holds the assets in question. The statement of the obligation of due care is meant to incorporate the principles of the common law under which the specific actions or precautions necessary to meet the obligation of care are determined by such factors as the nature and value of the property, the customs and practices of the business, and the like.

5. This section necessarily states the duty of a securities intermediary to obtain and maintain financial assets only at the very general and abstract level. For the most part, these matters are specified in great detail by regulatory law. Broker-dealers registered under the federal securities laws are subject to detailed regulation concerning the safeguarding of customer securities. See 17 C.F.R. § 240.15c3-3. Section 8-509(a) [30-8-509(1)] provides explicitly that if a securities intermediary complies with such regulatory law, that constitutes compliance with Section 8-503 [30-8-503]. In certain circumstances, these rules permit a firm to be in a position where it temporarily lacks a sufficient quantity of financial assets to satisfy all customer claims. For example, if another firm has failed to make a delivery to the firm in settlement of a trade, the firm is permitted a certain period of time to clear up the problem before it is obligated to obtain the necessary securities from some other source.

6. Subsection (d) [subsection (4)] is intended to recognize that there are some circumstances, where the duty to maintain a sufficient quantity of financial assets does not apply because the intermediary is not holding anything on behalf of others. For example, the Options Clearing Corporation is treated as a "securities intermediary" under this Article [chapter], although it does not itself hold options on behalf of its participants. Rather, it becomes the issuer of the options, by virtue of guaranteeing the obligations of participants in the clearing corporation who have written or purchased the options cleared through it. See Section 8-103(e) [30-8-113(5)]. Accordingly, the general duty of an intermediary under subsection (a) [subsection (1)] does not apply, nor would other provisions of Part 5 [Title 30, chapter 8, part 5] that depend upon the existence of a requirement that the securities intermediary hold financial assets, such as Sections 8-503 and 8-508 [30-8-503 and 30-8-508].

30-8-505. Duty of securities intermediary with respect to payments and distributions.

Official Comment

Source: Section 8-505, U.C.C.

Official Comment:

1. One of the core elements of the securities account relationships for which the Part 5 [Title 30, chapter 8, part 5] rules were designed is that the securities intermediary passes through to the entitlement holders the economic benefit of ownership of the financial asset, such as payments and distributions made by the issuer. Subsection (a) [subsection (1)] expresses the ordinary understanding that a securities intermediary will take appropriate action to see to it that any payments or distributions made by the issuer are received. One of the main reasons that investors make use of securities intermediaries is to obtain the services of a professional in performing the record-keeping and other functions necessary to ensure that payments and other distributions are received.

2. Subsection (a) [subsection (1)] incorporates the same "agreement/due care" formula as the other provisions of Part 5 [Title 30, chapter 8, part 5] dealing with the duties of a securities intermediary. See Comment 4 to Section 8-504 [30-8-504]. This formulation permits the parties to specify by agreement what action, if any, the intermediary is to take with respect to the duty to obtain payments and distributions. In the absence of specification by agreement, the intermediary satisfies the duty if the intermediary exercises due care in accordance with reasonable commercial standards. The provisions of Section 8-509 [30-8-509] also apply to the Section 8-505 [30-8-505] duty, so that compliance with applicable regulatory requirements constitutes compliance with the Section 8-505 [30-8-505] duty.

3. Subsection (b) [subsection (2)] provides that a securities intermediary is obligated to its entitlement holder for those payments or distributions made by the issuer that are in fact received by the intermediary. It does not deal with the details of the time and manner of payment. Moreover, as with any other monetary obligation, the obligation to pay may be subject to other rights of the obligor, by way of set-off counterclaim or the like. Section 8-509(c) [30-8-509(3)] makes this point explicit.

30-8-506. Duty of securities intermediary to exercise rights as directed by entitlement holder.

Official Comment

Source: Section 8-506, U.C.C.

Official Comment:

1. Another of the core elements of the securities account relationships for which the Part 5 [Title 30, chapter 8, part 5] rules were designed is that although the intermediary may, by virtue of the structure of the indirect holding system, be the party who has the power to exercise the corporate and other rights that come from holding the security, the intermediary exercises these powers as representative of the entitlement holder rather than at its own discretion. This characteristic is one of the things that distinguishes a securities account from other arrangements where one person holds securities "on behalf of" another, such as the relationship between a mutual fund and its shareholders or a trustee and its beneficiary.

2. The fact that the intermediary exercises the rights of security holding as representative of the entitlement holder does not, of course, preclude the entitlement holder from conferring discretionary authority upon the intermediary. Arrangements are not uncommon in which investors do not wish to have their intermediaries forward proxy materials or other information. Thus, this section provides that the intermediary shall exercise corporate and other rights "if directed to do so" by the entitlement holder. Moreover, as with the other Part 5 [Title 30, chapter 8, part 5] duties, the "agreement/due care" formulation is used in stating how the intermediary is to perform this duty. This section also provides that the intermediary satisfies the duty if it places the entitlement holder in a position to exercise the rights directly. This is to take account of the fact that some of the rights attendant upon ownership of the security, such as rights to bring derivative and other litigation, are far removed from the matters that intermediaries are expected to perform.

3. This section, and the two that follow, deal with the aspects of securities holding that are related to investment decisions. For example, one of the rights of holding a particular security that would fall within the purview of this section would be the right to exercise a conversion right for a convertible security. It is quite common for investors to confer discretionary authority upon another person, such as an investment adviser, with respect to these rights and other investment decisions. Because this section, and the other sections of Part 5 [Title 30, chapter 8, part 5], all

specify that a securities intermediary satisfies the Part 5 [Title 30, chapter 8, part 5] duties if it acts in accordance with the entitlement holder's agreement, there is no inconsistency between the statement of duties of a securities intermediary and these common arrangements.

4. Section 8-509 [30-8-509] also applies to the Section 8-506 [30-8-506] duty, so that compliance with applicable regulatory requirements constitutes compliance with this duty. This is quite important in this context, since the federal securities laws establish a comprehensive system of regulation of the distribution of proxy materials and exercise of voting rights with respect to securities held through brokers and other intermediaries. By virtue of Section 8-509(a) [30-8-509(1)], compliance with such regulatory requirement constitutes compliance with the Section 8-506 [30-8-506] duty.

30-8-507. Duty of securities intermediary to comply with entitlement order.

Official Comment

Source: Section 8-507, U.C.C.

Official Comment:

1. Subsection (a) [subsection (1)] of this section states another aspect of duties of securities intermediaries that make up security entitlements—the securities intermediary's duty to comply with entitlement orders. One of the main reasons for holding securities through securities intermediaries is to enable rapid transfer in settlement of trades. Thus the right to have one's orders for disposition of the security entitlement honored is an inherent part of the relationship. Subsection (b) [subsection (2)] states the correlative liability of a securities intermediary for transferring a financial asset from an entitlement holder's account pursuant to an entitlement order that was not effective.

2. The duty to comply with entitlement orders is subject to several qualifications. The intermediary has a duty only with respect to an entitlement order that is in fact originated by the appropriate person. Moreover, the intermediary has a duty only if it has had reasonable opportunity to assure itself that the order is genuine and authorized, and reasonable opportunity to comply with the order. The same "agreement/due care" formula is used in this section as in the other Part 5 [Title 30, chapter 8, part 5] sections on the duties of intermediaries, and the rules of Section 8-509 [30-8-509] apply to the Section 8-507 [30-8-507] duty.

3. Appropriate person is defined in Section 8-107 [30-8-117]. In the usual case, the appropriate person is the entitlement holder, see Section 8-107(a)(3) [30-8-117(1)(c)]. Entitlement holder is defined in Section 8-102(a)(7) [30-8-112(1)(g)] as the person "identified in the records of a securities intermediary as the person having a security entitlement." Thus, the general rule is that an intermediary's duty with respect to entitlement orders runs only to the person with whom the intermediary has established a relationship. One of the basic principles of the indirect holding system is that securities intermediaries owe duties only to their own customers. See also Section 8-115 [30-8-125]. The only situation in which a securities intermediary has a duty to comply with entitlement orders originated by a person other than the person with whom the intermediary established a relationship is covered by Section 8-107(a)(4) and (a)(5) [30-8-117(1)(d) and (1)(e)], which provide that the term "appropriate person" includes the successor or personal representative of a decedent, or the custodian or guardian of a person who lacks capacity. If the entitlement holder is competent, another person does not fall within the defined term "appropriate person" merely by virtue of having power to act as an agent for the entitlement holder. Thus, an intermediary is not required to determine at its peril whether a person who purports to be authorized to act for an entitlement holder is in fact authorized to do so. If an entitlement holder wishes to be able to act through agents, the entitlement holder can establish appropriate arrangements in advance with the securities intermediary.

One important application of this principle is that if an entitlement holder grants a security interest in its security entitlements to a third-party lender, the intermediary owes no duties to the secured party, unless the intermediary has entered into a "control" agreement in which it agrees to act on entitlement orders originated by the secured party. See Section 8-106 [30-8-116]. Even though the security agreement or some other document may give the secured party authority to act as agent for the debtor, that would not make the secured party an "appropriate person" to whom the security intermediary owes duties. If the entitlement holder and securities intermediary have agreed to such a control arrangement, then the intermediary's action in following instructions from the secured party would satisfy the subsection (a) [subsection (1)] duty. Although an agent, such as the secured party in this example, is not an "appropriate person," an entitlement order is "effective" if originated by an authorized person. See Section 8-107(a) and (b) [30-8-117(1) and

(2)]. Moreover, Section 8-507(a) [30-8-507(1)] provides that the intermediary satisfies its duty if it acts in accordance with the entitlement holder's agreement.

4. Subsection (b) [subsection (2)] provides that an intermediary is liable for a wrongful transfer if the entitlement order was "ineffective." Section 8-107 [30-8-117] specifies whether an entitlement order is effective. An "effective entitlement order" is different from an "entitlement order originated by an appropriate person." An entitlement order is effective under Section 8-107(b) [30-8-117(2)] if it is made by the appropriate person, or by a person who has power to act for the appropriate person under the law of agency, or if the appropriate person has ratified the entitlement order or is precluded from denying its effectiveness. Thus, although a securities intermediary does not have a duty to act on an entitlement order originated by the entitlement holder's agent, the intermediary is not liable for wrongful transfer if it does so.

Subsection (b) [subsection (2)], together with Section 8-107 [30-8-117], has the effect of leaving to other law most of the questions of the sort dealt with by Article 4A [Title 30, chapter 4A] for wire transfers of funds, such as allocation between the securities intermediary and the entitlement holder of the risk of fraudulent entitlement orders.

5. The term entitlement order does not cover all directions that a customer might give a broker concerning securities held through the broker. Article 8 [Title 30, chapter 8] is not a codification of all of the law of customers and stockbrokers. Article 8 [Title 30, chapter 8] deals with the settlement of securities trades, not the trades. The term entitlement order does not refer to instructions to a broker to make trades, that is, enter into contracts for the purchase or sale of securities. Rather, the entitlement order is the mechanism of transfer for securities held through intermediaries, just as indorsements and instructions are the mechanism for securities held directly. In the ordinary case the customer's direction to the broker to deliver the securities at settlement is implicit in the customer's instruction to the broker to sell. The distinction is, however, significant in that this section has no application to the relationship between the customer and broker with respect to the trade itself. For example, assertions by a customer that it was damaged by a broker's failure to execute a trading order sufficiently rapidly or in the proper manner are not governed by this Article [chapter].

30-8-508. Duty of securities intermediary to change entitlement holder's position to other form of security holding.

Official Comment

Source: Section 8-508, U.C.C.

Official Comment:

1. This section states another aspect of the duties of securities intermediaries that make up security entitlements—the obligation of the securities intermediary to change an entitlement holder's position into any other form of holding for which the entitlement holder is eligible or to transfer the entitlement holder's position to an account at another intermediary. This section does not state unconditionally that the securities intermediary is obligated to turn over a certificate to the customer or to cause the customer to be registered on the books of the issuer, because the customer may not be eligible to hold the security directly. For example, municipal bonds are now commonly issued in "book-entry only" form, in which the only entity that the issuer will register on its own books is a depository.

If security certificates in registered form are issued for the security, and individuals are eligible to have the security registered in their own name, the entitlement holder can request that the intermediary deliver or cause to be delivered to the entitlement holder a certificate registered in the name of the entitlement holder or a certificate indorsed in blank or specially indorsed to the entitlement holder. If security certificates in bearer form are issued for the security, the entitlement holder can request that the intermediary deliver or cause to be delivered a certificate in bearer form. If the security can be held by individuals directly in uncertificated form, the entitlement holder can request that the security be registered in its name. The specification of this duty does not determine the pricing terms of the agreement in which the duty arises.

2. The same "agreement/due care" formula is used in this section as in the other Part 5 [Title 30, chapter 8, part 5] sections on the duties of intermediaries. So too, the rules of Section 8-509 [30-8-509] apply to the Section 8-508 [30-8-508] duty.

30-8-509. Specification of duties of securities intermediary by other statute or regulation — manner of performance of duties of securities intermediary and exercise of rights of entitlement holder.

Official Comment

Source: Section 8-509, U.C.C.

Official Comment:

This Article [chapter] is not a comprehensive statement of the law governing the relationship between broker-dealers or other securities intermediaries and their customers. Most of the law governing that relationship is the common law of contract and agency, supplemented or supplanted by regulatory law. This Article [chapter] deals only with the most basic commercial/property law principles governing the relationship. Although Sections 8-504 through 8-508 [30-8-504 through 30-8-508] specify certain duties of securities intermediaries to entitlement holders, the point of these sections is to identify what it means to have a security entitlement, not to specify the details of performance of these duties.

For many intermediaries, regulatory law specifies in great detail the intermediary's obligations on such matters as safekeeping of customer property, distribution of proxy materials, and the like. To avoid any conflict between the general statement of duties in this Article [chapter] and the specific statement of intermediaries' obligations in such regulatory schemes, subsection (a) [subsection (1)] provides that compliance with applicable regulation constitutes compliance with the duties specified in Sections 8-504 through 8-508 [30-8-504 through 30-8-508].

30-8-510. Rights of purchaser of security entitlement from entitlement holder.

Official Comment

Source: Section 8-510, U.C.C.

Official Comment:

1. This section specifies certain rules concerning the rights of persons who purchase interests in security entitlements from entitlement holders. The rules of this section are provided to take account of cases where the purchaser's rights are derivative from the rights of another person who is and continues to be the entitlement holder.

2. Subsection (a) [subsection (1)] provides that no adverse claim can be asserted against a purchaser of an interest in a security entitlement if the purchaser gives value, obtains control, and does not have notice of the adverse claim. The primary purpose of this rule is to give adverse claim protection to persons who take security interests in security entitlements and obtain control, but do not themselves become entitlement holders.

The following examples illustrate subsection (a) [subsection (1)]:

Example 1. X steals a certificated bearer bond from Owner. X delivers the certificate to Able & Co. for credit to X's securities account. Later, X borrows from Bank and grants bank a security interest in the security entitlement. Bank obtains control under Section 8-106(d)(2) [30-8-116(4)(b)] by virtue of an agreement in which Able agrees to comply with entitlement orders originated by Bank. X absconds.

Example 2. Same facts as in Example 1, except that Bank does not obtain a control agreement. Instead, Bank perfects by filing a financing statement.

In both of these examples, when X deposited the bonds X acquired a security entitlement under Section 8-501 [30-8-501]. Under other law, Owner may be able to have a constructive trust imposed on the security entitlement as the traceable product of the bonds that X misappropriated. X granted a security interest in that entitlement to Bank. Bank was a purchaser of an interest in the security entitlement from X. In Example 1, although Bank was not a person who acquired a security entitlement from the intermediary, Bank did obtain control. If Bank did not have notice of Owner's claim, Section 8-510(a) [30-8-510(1)] precludes Owner from asserting an adverse claim against Bank. In Example 2, Bank had a perfected security interest, but did not obtain control. Accordingly, Section 8-510(a) [30-8-510(1)] does not preclude Owner from asserting its adverse claim against Bank.

3. Subsection (b) [subsection (2)] applies to the indirect holding system a limited version of the "shelter principle." The following example illustrates the relatively limited class of cases for which it may be needed:

Example 3. Thief steals a certificated bearer bond from Owner. Thief delivers the certificate to Able & Co. for credit to Thief's securities account. Able forwards the certificate to a clearing corporation for credit to Able's account. Later Thief instructs Able to sell the positions in the bonds. Able sells to Baker & Co., acting as broker for Buyer. The trade is settled by book-entries in the accounts of Able and Baker at the clearing corporation, and in the accounts of Thief and

Buyer at Able and Baker respectively. Owner may be able to reconstruct the trade records to show that settlement occurred in such fashion that the "same bonds" that were carried in Thief's account at Able are traceable into Buyer's account at Baker. Buyer later decides to donate the bonds to Alma Mater University and executes an assignment of its rights as entitlement holder to Alma Mater.

Buyer had a position in the bonds, which Buyer held in the form of a security entitlement against Baker. Buyer then made a gift of the position to Alma Mater. Although Alma Mater is a purchaser, Section 1-201(33) [30-1-201(33)], it did not give value. Thus, Alma Mater is a person who purchased a security entitlement, or an interest therein, from an entitlement holder (Buyer). Buyer was protected against Owner's adverse claim by the Section 8-502 [30-8-502] rule. Thus, by virtue of Section 8-510(b) [30-8-510(2)], Owner is also precluded from asserting an adverse claim against Alma Mater.

4. Subsection (c) [subsection (3)] specifies a priority rule for cases where an entitlement holder transfers conflicting interests in the same security entitlement to different purchasers. It follows the same principle as the Article 9 [Title 30, chapter 9A] priority rule for investment property, that is, control trumps non-control. Indeed, the most significant category of conflicting "purchasers" may be secured parties. Priority questions for security interests, however, are governed by the rules in Article 9 [Title 30, chapter 9A]. Subsection (c) [subsection (3)] applies only to cases not covered by the Article 9 [Title 30, chapter 9A] rules. It is intended primarily for disputes over conflicting claims arising out of repurchase agreement transactions that are not covered by the other rules set out in Articles 8 and 9 [Title 30, chapters 8 and 9A].

The following example illustrates subsection (c) [subsection (3)]:

Example 4. Dealer holds securities through an account at Alpha Bank. Alpha Bank in turns holds through a clearing corporation account. Dealer transfers securities to RP1 in a "hold in custody" repo transaction. Dealer then transfers the same securities to RP2 in another repo transaction. The repo to RP2 is implemented by transferring the securities from Dealer's regular account at Alpha Bank to a special account maintained by Alpha Bank for Dealer and RP2. The agreement among Dealer, RP2, and Alpha Bank provides that Dealer can make substitutions for the securities but RP2 can direct Alpha Bank to sell any securities held in the special account. Dealer becomes insolvent. RP1 claims a prior interest in the securities transferred to RP2.

In this example Dealer remained the entitlement holder but agreed that RP2 could initiate entitlement orders to Dealer's security intermediary, Alpha Bank. If RP2 had become the entitlement holder, the adverse claim rule of Section 8-502 [30-8-502] would apply. Even if RP2 does not become the entitlement holder, the arrangement among Dealer, Alpha Bank, and RP2 does suffice to give RP2 control. Thus, under Section 8-510(c) [30-8-510(3)], RP2 has priority over RP1, because RP2 is a purchaser who obtained control, and RP1 is a purchaser who did not obtain control. The same result could be reached under Section 8-510(a) [30-8-510(1)] which provides that RP1's earlier in time interest cannot be asserted as an adverse claim against RP2. The same result would follow under the Article 9 [Title 30, chapter 9A] priority rules if the interests of RP1 and RP2 are characterized as "security interests," see Section 9-328(1) [30-9A-328(1)]. The main point of the rules of Section 8-510(c) [30-8-510(3)] is to ensure that there will be clear rules to cover the conflicting claims of RP1 and RP2 without characterizing their interests as Article 9 [Title 30, chapter 9A] security interests.

The priority rules in Article 9 [Title 30, chapter 9A] for conflicting security interests also include a default temporal priority rule for cases where multiple secured parties have obtained control but omitted to specify their respective rights by agreement. See Section 9-328(2) [30-9A-328(2)] and Comment 5 to Section 9-328 [30-9A-328]. Because the purchaser priority rule in Section 8-510(c) [30-8-510(3)] is intended to track the Article 9 [Title 30, chapter 9A] priority rules, it too has a temporal priority rule for cases where multiple non-secured party purchasers have obtained control but omitted to specify their respective rights by agreement. The rule is patterned on Section 9-328(2) [30-9A-328(2)].

5. If a securities intermediary itself is a purchaser, subsection (d) [subsection (4)] provides that it has priority over the interest of another purchaser who has control. Article 9 [Title 30, chapter 9A] contains a similar rule. See Section 9-328(3) [30-9A-328(3)].

Compiler's Comments

1999 Amendment: Chapter 305 at beginning inserted "In an action not covered by the priority rules in chapter 9 [renumbered chapter 9A] or the rules stated in subsection (3)"; in (3) at beginning of second sentence inserted exception clause and after "rank" substituted "according to the priority in time of" for "equally, except that"; inserted (3)(a) through (3)(c) outlining priority determination; and made minor changes in style. Amendment effective July 1, 2001.

30-8-511. Priority among security interests and entitlement holders.

Official Comment

Source: Section 8-511, U.C.C.

Official Comment:

1. This section sets out priority rules for circumstances in which a securities intermediary fails leaving an insufficient quantity of securities or other financial assets to satisfy the claims of its entitlement holders and the claims of creditors to whom it has granted security interests in financial assets held by it. Subsection (a) [subsection (1)] provides that entitlement holders' claims have priority except as otherwise provided in subsection (b) [subsection (2)], and subsection (b) [subsection (2)] provides that the secured creditor's claim has priority if the secured creditor obtains control, as defined in Section 8-106 [30-8-116]. The following examples illustrate the operation of these rules.

Example 1. Able & Co., a broker, borrows from Alpha Bank and grants Alpha Bank a security interest pursuant to a written agreement which identifies certain securities that are to be collateral for the loan, either specifically or by category. Able holds these securities in a clearing corporation account. Able becomes insolvent and it is discovered that Able holds insufficient securities to satisfy the claims of customers who have paid for securities that they held in accounts with Able and the collateral claims of Alpha Bank. Alpha Bank's security interest in the security entitlements that Able holds through the clearing corporation account may be perfected under the automatic perfection rule of Section 9-115(4)(c) [30-9-115(4)(c), now repealed, see 30-9A-309], but Alpha Bank did not obtain control under Section 8-106 [30-8-116]. Thus, under Section 8-511(a) [30-8-511(1)] the entitlement holders' claims have priority over Alpha Bank's claim.

Example 2. Able & Co., a broker, borrows from Beta Bank and grants Beta Bank a security interest in securities that Able holds in a clearing corporation account. Pursuant to the security agreement, the securities are debited from Alpha's account and credited to Beta's account in the clearing corporation account. Able becomes insolvent and it is discovered that Able holds insufficient securities to satisfy the claims of customers who have paid for securities that they held in accounts with Able and the collateral claims of Alpha Bank. Although the transaction between Able and Beta took the form of an outright transfer on the clearing corporation's books, as between Able and Beta, Able remains the owner and Beta has a security interest. In that respect the situation is no different than if Able had delivered bearer bonds to Beta in pledge to secure a loan. Beta's security interest is perfected, and Beta obtained control. See Sections 8-106 and 9-115 [30-8-116 and 30-9-115, now repealed, see 30-9A-308, 30-9A-309, 30-9A-313, and 30-9A-314]. Under Section 8-511(b) [30-8-511(2)], Beta Bank's security interest has priority over claims of Able's customers.

The result in Example 2 is an application to this particular setting of the general principle expressed in Section 8-503 [30-8-503], and explained in the Comments thereto, that the entitlement holders of a securities intermediary cannot assert rights against third parties to whom the intermediary has wrongfully transferred interests, except in extremely unusual circumstances where the third party was itself a participant in the transferor's wrongdoing. Under subsection (b) [subsection (2)] the claim of a secured creditor of a securities intermediary has priority over the claims of entitlement holders if the secured creditor has obtained control. If, however, the secured creditor acted in collusion with the intermediary in violating the intermediary's obligation to its entitlement holders, then under Section 8-503(e) [30-8-503(5)], the entitlement holders, through their representative in insolvency proceedings, could recover the interest from the secured creditor, that is, set aside the security interest.

2. The risk that investors who hold through an intermediary will suffer a loss as a result of a wrongful pledge by the intermediary is no different than the risk that the intermediary might fail and not have the securities that it was supposed to be holding on behalf of its customers, either because the securities were never acquired by the intermediary or because the intermediary wrongfully sold securities that should have been kept to satisfy customers' claims. Investors are protected against that risk by the regulatory regimes under which securities intermediaries operate. Intermediaries are required to maintain custody, through clearing corporation accounts or in other approved locations, of their customers' securities and are prohibited from using customers' securities in their own business activities. Securities firms who are carrying both customer and proprietary positions are not permitted to grant blanket liens to lenders covering all securities which they hold, for their own account or for their customers. Rather, securities firms designate specifically which positions they are pledging. Under SEC Rules 8c1 and 15c21, customers' securities can be pledged only to fund loans to customers, and only with the consent of the customers. Customers' securities cannot be pledged for loans for the firm's proprietary

business; only proprietary positions can be pledged for proprietary loans. SEC Rule 15c33 implements these prohibitions in a fashion tailored to modern securities firm accounting systems by requiring brokers to maintain a sufficient inventory of securities, free from any liens, to satisfy the claims of all of their customers for fully paid and excess margin securities. Revised Article 8 [Title 30, chapter 8] mirrors that requirement, specifying in Section 8-504 [30-8-504] that a securities intermediary must maintain a sufficient quantity of investment property to satisfy all security entitlements, and may not grant security interests in the positions it is required to hold for customers, except as authorized by the customers.

If a failed brokerage has violated the customer protection regulations and does not have sufficient securities to satisfy customers' claims, its customers are protected against loss from a shortfall by the Securities Investor Protection Act ("SIPA"). Securities firms required to register as brokers or dealers are also required to become members of the Securities Investor Protection Corporation ("SIPC"), which provides their customers with protection somewhat similar to that provided by FDIC and other deposit insurance programs for bank depositors. When a member firm fails, SIPC is authorized to initiate a liquidation proceeding under the provisions of SIPA. If the assets of the securities firm are insufficient to satisfy all customer claims, SIPA makes contributions to the estate from a fund financed by assessments on its members to protect customers against losses up to $500,000 for cash and securities held at member firms.

Article 8 [Title 30, chapter 8] is premised on the view that the important policy of protecting investors against the risk of wrongful conduct by their intermediaries is sufficiently treated by other law.

3. Subsection (c) [subsection (3)] sets out a special rule for secured financing provided to enable clearing corporations to complete settlement. The reasons that secured financing arrangements are needed in such circumstances are explained in Comment 7 to Section 9-115 [30-9-115, now repealed, see 30-9A-308, 30-9A-309, 30-9A-313, and 30-9A-314]. In order to permit clearing corporations to establish liquidity facilities where necessary to ensure completion of settlement, subsection (c) [subsection (3)] provides a priority for secured lenders to such clearing corporations. Subsection (c) [subsection (3)] does not turn on control because the clearing corporation may be the top tier securities intermediary for the securities pledged, so that there may be no practicable method for conferring control on the lender.

CHAPTER 9A
UNIFORM COMMERCIAL CODE SECURED TRANSACTIONS

Chapter Official Comment

Official Comments to Transition Provisions

[Effective Date — Section 171, Ch. 305, L. 1999]

A uniform law as complex as Article 9 [Title 30, chapter 9] necessarily gives rise to difficult problems and uncertainties during the transition to the new law. As is customary for uniform laws, this Article [Title 30, chapter 9] is based on the general assumption that all States will have enacted substantially identical versions. While always important, uniformity is essential to the success of this Article [Title 30, chapter 9]. If former Article 9 [Title 30, chapter 9] is in effect in some jurisdictions, and this Article [Title 30, chapter 9] is in effect in others, horrendous complications may arise. For example, the proper place in which to file to perfect a security interest (and thus the status of a particular security interest as perfected or unperfected) would depend on whether the matter was litigated in a State in which former Article 9 [Title 30, chapter 9] was in effect or a State in which this Article [Title 30, chapter 9] was in effect. Accordingly, this section contemplates that States will adopt a uniform effective date for this Article [Title 30, chapter 9]. Any one State's failure to adopt the uniform effective date will greatly increase the cost and uncertainty surrounding the transition.

Other problems arise from transactions and relationships that were entered into under former Article 9 [Title 30, chapter 9] or under non-UCC law and which remain outstanding on the effective date of this Article [Title 30, chapter 9]. The difficulties arise primarily because this Article [Title 30, chapter 9] expands the scope of former Article 9 [Title 30, chapter 9] to cover additional types of collateral and transactions and because it provides new methods of perfection for some types of collateral, different priority rules, and different choice-of-law rules governing perfection and priority. This Section and the other sections in this Part [not codified] address primarily this second set of problems.

[Savings Provisions — Section 169, Ch. 305, L. 1999]

1. **Pre-Effective-Date Transactions.** Subsection (a) [subsection 1] contains the general rule that this Article [Title 30, chapter 9] applies to transactions, security interests, and other liens within its scope (see Section 9-109 [30-9-129]), even if the transaction or lien was entered into or created before the effective date. Thus, secured transactions entered into under former Article 9 [Title 30, chapter 9] must be terminated, completed, consummated, and enforced under this Article [Title 30, chapter 9]. Subsection (b) [subsection 2] is an exception to the general rule. It applies to valid, pre-effective-date transactions and liens that were not governed by former Article 9 [Title 30, chapter 9] but would be governed by this Article [Title 30, chapter 9] if they had been entered into or created after this Article [Title 30, chapter 9] takes effect. Under subsection (b) [subsection (2)], these valid transactions, such as the creation of agricultural liens and security interests in commercial tort claims, retain their validity under this Article [Title 30, chapter 9] and may be terminated, completed, consummated, and enforced under this Article [Title 30, chapter 9]. However, these transactions also may be terminated, completed, consummated, and enforced by the law that otherwise would apply had this Article [Title 30, chapter 9] not taken effect.

2. **Judicial Proceedings Commenced Before Effective Date.** As is usual in transition provisions, subsection (c) [subsection (3)] provides that this Article [Title 30, chapter 9] does not affect litigation pending on the effective date.

[Security Interest Perfected Before Effective Date — Section 162, Ch. 305, L. 1999]

1. **Perfected Security Interests Under Former Article 9 [Title 30, chapter 9] and this Article [Title 30, chapter 9].** This section deals with security interests that are perfected (i.e., that are enforceable and have priority over the rights of a lien creditor) under former Article 9 [Title 30, chapter 9] or other applicable law immediately before this Article [Title 30, chapter 9] takes effect. Subsection (a) [subsection 1] provides, not surprisingly, that if the security interest would be a perfected security interest under this Article [Title 30, chapter 9] (i.e., if the transaction satisfies this Article's [Title 30, chapter 9] requirements for enforceability (attachment) and perfection), no further action need be taken for the security interest to be a perfected security interest.

2. **Security Interests Enforceable and Perfected Under Former Article 9 [Title 30, chapter 9] but Unenforceable or Unperfected Under this Article [Title 30, chapter 9].** Subsection (b) [subsection 2] deals with security interests that are enforceable and perfected under former Article 9 [Title 30, chapter 9] or other applicable law immediately before this Article [Title 30, chapter 9] takes effect but do not satisfy the requirements for enforceability (attachment) or perfection under this Article [Title 30, chapter 9]. Except as otherwise provided in Section 9-705 [sec. 164, Ch. 305, L. 1999], these security interests are perfected security interests for one year after the effective date. If the security interest satisfies the requirements for attachment and perfection within that period, the security interest remains perfected thereafter. If the security interest satisfies only the requirements for attachment within that period, the security interest becomes unperfected at the end of the one-year period.

Example 1: A pre-effective-date security agreement in a consumer transaction covers "all securities accounts." The security interest is properly perfected. The collateral description was adequate under former Article 9 [Title 30, chapter 9] (see former Section 9-115(3) [30-9-115(3)]) but is insufficient under this Article [Title 30, chapter 9] (see Section 9-108(e)(2) [30-9-128(5)(b)]). Unless the debtor authenticates a new security agreement describing the collateral other than by "type" (or Section 9-203(b)(3) [30-9-213(2)(c)] otherwise is satisfied) within the one-year period following the effective date, the security interest becomes unenforceable at the end of that period.

Other examples under former Article 9 [Title 30, chapter 9] or other applicable law that may be effective as attachment or enforceability steps but may be ineffective under this Article [Title 30, chapter 9] include an oral agreement to sell a payment intangible or possession by virtue of a notification to a bailee under former Section 9-305 [30-9-305]. Neither the oral agreement nor the notification would satisfy the revised Section 9-203 [30-9-213] requirements for attachment.

Example 2: A pre-effective-date possessory security interest in instruments is perfected by a bailee's receipt of notification under former 9-305 [30-9-305]. The bailee has not, however, acknowledged that it holds for the secured party's benefit under revised Section 9-313 [30-9-333]. Unless the bailee authenticates a record acknowledging that it holds for the secured party (or another appropriate perfection step is taken) within the one-year period following the effective date, the security interest becomes unperfected at the end of that period.

3. **Interpretation of Pre-Effective-Date Security Agreements.** Section 9-102 [30-9-122] defines "security agreement" as "an agreement that creates or provides for a security interest."

Under Section 1-201(3) [30-1-201(3)], an "agreement" is a "bargain of the parties in fact." If parties to a pre-effective-date security agreement describe the collateral by using a term defined in former Article 9 [Title 30, chapter 9] in one way and defined in this Article [Title 30, chapter 9] in another way, in most cases it should be presumed that the bargain of the parties contemplated the meaning of the term under former Article 9 [Title 30, chapter 9].

Example 3: A pre-effective-date security agreement covers "all accounts" of a debtor. As defined under former Article 9 [Title 30, chapter 9], an "account" did not include a right to payment for lottery winnings. These rights to payment are "accounts" under this Article [Title 30, chapter 9], however. The agreement of the parties presumptively created a security interest in "accounts" as defined in former Article 9 [Title 30, chapter 9]. A different result might be appropriate, for example, if the security agreement explicitly contemplated future changes in the Article 9 [Title 30, chapter 9] definitions of types of collateral-e.g., "'Accounts' means 'accounts' as defined in the UCC Article 9 [Title 30, chapter 9] of [State X], as that definition may be amended from time to time." Whether a different approach is appropriate in any given case depends on the bargain of the parties, as determined by applying ordinary principles of contract construction.

[Security Interest Unperfected Before Effective Date — Section 163, C. 305, L. 1999]

This section deals with security interests that are enforceable but unperfected (i.e., subordinate to the rights of a person who becomes a lien creditor) under former Article 9 [Title 30, chapter 9] or other applicable law immediately before this Article [Title 30, chapter 9] takes effect. These security interests remain enforceable for one year after the effective date, and thereafter if the appropriate steps for attachment under this Article [Title 30, chapter 9] are taken before the one-year period expires. (This section's treatment of enforceability is the same as that of Section 9-703 [sec. 162, Ch. 305, L. 1999].) The security interest becomes a perfected security interest on the effective date if, at that time, the security interest satisfies the requirements for perfection under this Article [Title 30, chapter 9]. If the security interest does not satisfy the requirements for perfection until sometime thereafter, it becomes a perfected security interest at that later time.

Example: A security interest has attached under former Article 9 [Title 30, chapter 9] but is unperfected because the filed financing statement covers "all of debtor's personal property" and controlling case law in the applicable jurisdiction has determined that this identification of collateral in a financing statement is insufficient. Upon the effective date of this Article [Title 30, chapter 9], the financing statement becomes sufficient under Section 9-504(2) [30-9-524(2)]. On that date the security interest becomes perfected. (This assumes, of course, that the financing statement is filed in the proper filing office under this Article [Title 30, chapter 9].)

[Effectiveness of Action Taken Before Effective Date of Act — Section 164, Ch. 305, L. 1999]

1. **General.** This section addresses primarily the situation in which the perfection step is taken under former Article 9 [Title 30, chapter 9] or other applicable law before the effective date of this Article [Title 30, chapter 9], but the security interest does not attach until after that date.

2. **Perfection Other Than by Filing.** Subsection (a) [subsection 1] applies when the perfection step is a step other than the filing of a financing statement. If the step that would be a valid perfection step under former Article 9 [Title 30, chapter 9] or other law is taken before this Article [Title 30, chapter 9] takes effect, and if a security interest attaches within one year after this Article [Title 30, chapter 9] takes effect, then the security interest becomes a perfected security interest upon attachment. However, the security interest becomes unperfected one year after the effective date unless the requirements for attachment and perfection under this Article [Title 30, chapter 9] are satisfied within that period.

3. **Perfection by Filing: Ineffective Filings Made Effective.** Subsection (b) [subsection 2] deals with financing statements that were filed under former Article 9 [Title 30, chapter 9] and which would not have perfected a security interest under the former Article [Title 30, chapter 9] (because, e.g., they did not accurately describe the collateral or were filed in the wrong place), but which would perfect a security interest under this Article [Title 30, chapter 9]. Under subsection (b) [subsection (2)], such a financing statement is effective to perfect a security interest to the extent it complies with this Article [Title 30, chapter 9]. Subsection (b) [subsection 2] applies regardless of the reason for the filing. For example, a secured party need not wait until the effective date to respond to the change this Article [Title 30, chapter 9] makes with respect to the jurisdiction whose law governs perfection of certain security interests. Rather, a secured party may wish to prepare for this change by filing a financing statement before the effective date in the jurisdiction whose law governs perfection under this Article [Title 30, chapter 9]. When this Article [Title 30, chapter 9] takes effect, the filing becomes effective to perfect a security interest (assuming the filing satisfies the perfection requirements of this Article [Title 30, chapter 9]).

Note, however, that Section 9-706 [sec. 165, Ch. 305, L. 1999] determines whether a financing statement filed before the effective date operates to continue the effectiveness of a financing statement filed in another office before the effective date.

4. **Perfection by Filing: Change in Applicable Law.** Subsection (c) [subsection (3)] provides that a financing statement filed in the proper jurisdiction under former Section 9-103 [30-9-103] remains effective for all purposes, despite the fact that Part 3 of this Article [Title 30, chapter 9, part 3] would require filing of a financing statement in a different jurisdiction. This means that, during the early years of this Article's [Title 30, chapter 9] effectiveness, it may be necessary to search the files not only in the jurisdiction whose law governs perfection under this Article [Title 30, chapter 9] but also (if different) in the jurisdiction(s) whose law governed perfection under former Article 9 [Title 30, chapter 9]. To limit this burden, subsection (c) [subsection (3)] provides that a financing statement filed in the jurisdiction determined by former Section 9-103 [30-9-103] becomes ineffective at the earlier of the time it would become ineffective under the law of that jurisdiction or June 30, 2006. The June 30, 2006, limitation addresses some nonuniform versions of former Article 9 [Title 30, chapter 9] that extended the effectiveness of a financing statement beyond five years. Note that a financing statement filed before the effective date may remain effective beyond June 30, 2006, if subsection (d) [subsections (3) and (4)] (concerning continuation statements) or (e) [not adopted in Montana] (concerning transmitting utilities) or Section 9-706 [sec. 165, Ch. 305, L. 1999] (concerning initial financing statements that operate to continue pre-effective-date financing statements) so provides.

Subsection (c) [subsection (3)] is an exception to Section 9-703(b) [sec. 162(2), Ch. 305, L. 1999]. Under the general rule in Section 9-703(b) [sec. 162(2), Ch. 305, L. 1999], a security interest that is enforceable and perfected on the effective date of this Article [Title 30, chapter 9] is a perfected security interest for one year after this Article [Title 30, chapter 9] takes effect, even if the security interest is not enforceable under this Article [Title 30, chapter 9] and the applicable requirements for perfection under this Article [Title 30, chapter 9] have not been met. However, in some cases subsection (c) [subsection (3)] may shorten the one-year period of perfection; in others, if the security interest is enforceable under Section 9-203 [30-9-213], it may extend the period of perfection. A financing statement that remains effective under subsection (c) [subsection (3)] may be amended (but generally may not be continued) after this Article [Title 30, chapter 9] takes effect by filing an amendment in the office where the financing statement was filed.

Example 1: On July 3, 1996, D, a State X corporation, creates a security interest in certain manufacturing equipment located in State Y. On July 6, 1996, SP perfects a security interest in the equipment under former Article 9 [Title 30, chapter 9] by filing in the office of the State Y Secretary of State. See former Section 9-103(1)(b) [30-9-103(1)(b)]. This Article [Title 30, chapter 9] takes effect in States X and Y on July 1, 2001. Under Section 9-705(c) [subsection (3)], the financing statement remains effective for the first five days of July, 2001, after which it lapses. See former Section 9-403 [30-9-403]. Had SP continued the effectiveness of the financing statement by filing a continuation statement in State Y under former Article 9 [Title 30, chapter 9] before July 1, 2001, the financing statement would have remained effective to perfect the security interest through June 30, 2006. See subsection (c)(2) [subsection (3)(a)(ii)]. Alternatively, SP could have filed an initial financing statement in State X under subsection (b) [subsection (2)] or Section 9-706 [sec. 165, Ch. 305, L. 1999] before the State Y financing statement lapsed. Had SP done so, the security interest would have remained perfected without interruption until the State X financing statement lapsed.

5. **Continuing Effectiveness of Filed Financing Statement.** A financing statement filed before the effective date of this Article [Title 30, chapter 9] may be continued only by filing in the State and office designated by this Article [Title 30, chapter 9]. This result is accomplished in the following manner: Subsection (d) [subsection (5)(b)] indicates that, as a general matter, a continuation statement filed after the effective date of this Article [July 1, 2001] does not continue the effectiveness of a financing statement filed under the law designated by former Section 9-103 [30-9-103]. Instead, an initial financing statement must be filed under Section 9-706 [sec. 165, Ch. 305, L. 1999]. The second sentence of subsection (d) [subsection (5)] contains an exception to the general rule. It provides that a continuation statement is effective to continue the effectiveness of a financing statement filed before this Article [Title 30, chapter 9] takes effect if this Article [Title 30, chapter 9] prescribes not only the same jurisdiction but also the same filing office.

Example 2: On November 8, 2000, D, a State X corporation, creates a security interest in certain manufacturing equipment located in State Y. On November 15, 2000, SP perfects a security interest in the equipment under former Article 9 [Title 30, chapter 9] by filing in office of the State Y Secretary of State. See former Section 9-103(1)(b) [30-9-103(1)(b)]. This Article [Title 30, chapter 9] takes effect in States X and Y on July 1, 2001. Under Section 9-705(c) [subsection (3)(a)(ii)], the financing statement ceases to be effective in November, 2005, when it lapses. See Section 9-515 [30-9-535]. Under this Article [Title 30, chapter 9], the law of D's location (State X, see Section 9-307 [30-9-327]) governs perfection. See Section 9-301 [30-9-321]. Thus, the filing of a continuation statement in State Y after the effective date would not continue the effectiveness of the financing statement. See subsection (d) [subsection (4)]. However, the effectiveness of the financing statement could be continued under Section 9-706 [sec. 165, Ch. 305, L. 1999].

Example 3: The facts are as in Example 2, except that D is a State Y corporation. Assume State Y adopted former Section 9-401(1) [30-9-401(1)] (second alternative). State Y law governs perfection under Part 3 of this Article [Title 30, chapter 9, part 3]. (See Sections 9-301, 9-307 [30-9-321, 30-9-327].) Under the second sentence of subsection (d) [subsection (4) (no second sentence)], the timely filing of a continuation statement in accordance with the law of State Y continues the effectiveness of the financing statement.

Example 4: The facts are as in Example 3, except that the collateral is equipment used in farming operations and, in accordance with former Section 9-401(1) [30-9-401(1)] (second alternative) as enacted in State Y, the financing statement was filed in State Y, in the office of the Shelby County Recorder of Deeds. Under this Article [Title 30, chapter 9], a continuation statement must be filed in the office of the State Y Secretary of State. See Section 9-501(a)(2) [30-9-521(1)(b)]. Under the second sentence of subsection (d) [first sentence of subsection (5)], the timely filing of a continuation statement in accordance with the law of State Y operates to continue a pre-effective-date financing statement only if the continuation statement is filed in the same office as the financing statement. Accordingly, the continuation statement is not effective in this case, but the financing statement may be continued under Section 9-706 [sec. 165, Ch. 305, L. 1999].

Example 5: The facts are as in Example 3, except that State Y enacted former Section 9-401(1) [30-9-401(1)] (third alternative). As required by former Section 9-401(1) [30-9-401(1)], SP filed financing statements in both the office of the State Y Secretary of State and the office of the Shelby County Recorder of Deeds. Under this Article [Title 30, chapter 9], a continuation statement must be filed in the office of the State Y Secretary of State. See Section 9-501(a)(2) [30-9-521(1)(b)]. The timely filing of a continuation statement in that office after this Article [Title 30, chapter 9] takes effect would be effective to continue the effectiveness of the financing statement (and thus continue the perfection of the security interest), even if the financing statement filed with the County Recorder lapses.

6. **Continuation Statements.** In some cases, this Article [Title 30, chapter 9] reclassifies collateral covered by a financing statement filed under former Article 9 [Title 30, chapter 9]. For example, collateral consisting of the right to payment for real property sold would be a "general intangible" under the former Article [Title 30, chapter 9] but an "account" under this Article [Title 30, chapter 9]. To continue perfection under those circumstances, a continuation statement must comply with the normal requirements for a continuation statement. See Section 9-515 [30-9-535]. In addition, the pre-effective-date financing statement and continuation statement, taken together, must satisfy the requirements of this Article [Title 30, chapter 9] concerning the sufficiency of the debtor's name, secured party's name, and indication of collateral. See subsection (f) [subsection (7)].

Example 6: A pre-effective-date financing statement covers "all general intangibles" of a debtor. As defined under former Article 9 [Title 30, chapter 9], a "general intangible," would include rights to payment for lottery winnings. These rights to payment are "accounts" under this Article [Title 30, chapter 9], however. A post-effective-date continuation statement will not continue the effectiveness of the pre-effective-date financing statement with respect to lottery winnings unless it amends the indication of collateral covered to include lottery winnings (e.g., by adding "accounts," "rights to payment for lottery winnings," or the like). If the continuation statement does not amend the indication of collateral, the continuation statement will be effective to continue the effectiveness of the financing statement only with respect to "general intangibles" as defined in this Article [Title 30, chapter 9].

Example 7: The facts are as in Example 6, except that the pre-effective-date financing statement covers "all accounts and general intangibles." Even though rights to payment for lottery winnings are "general intangibles" under former Article 9 [Title 30, chapter 9] and "accounts" under this Article [Title 30, chapter 9], a post-effective-date continuation statement would continue the effectiveness of the pre-effective-date financing statement with respect to lottery winnings. There would be no need to amend the indication of collateral covered, inasmuch as the indication ("accounts") satisfies the requirements of this Article [Title 30, chapter 9].

[When Initial Financing Statement Suffices as Continuation Statement — Section 165, Ch. 305, L. 1999]

1. **Continuation of Financing Statements Not Filed in Proper Filing Office Under this Article [Title 30, chapter 9].** This section deals with continuing the effectiveness of financing statements that are filed in the proper State and office under former Article 9 [Title 30, chapter 9], but which would be filed in the wrong State or in the wrong office of the proper State under this Article [Title 30, chapter 9]. Section 9-705(d) [sec. 164(5)(b), Ch. 305, L. 1999] provides that, under these circumstances, filing a continuation statement after the effective date of this Article [July 1, 2001] in the office designated by former Article 9 [Title 30, chapter 9] would not be effective. This section provides the means by which the effectiveness of such a financing statement can be continued if this Article [Title 30, chapter 9] governs perfection under the applicable choice-of-law rule: filing an initial financing statement in the office specified by Section 9-501 [30-9-521].

Although it has the effect of continuing the effectiveness of a pre-effective-date financing statement, an initial financing statement described in this section is not a continuation statement. Rather, it is governed by the rules applicable to initial financing statements. (However, the debtor need not authorize the filing. See Section 9-707 [sec. 166, Ch. 305, L. 1999].) Unlike a continuation statement, the initial financing statement described in this section may be filed any time during the effectiveness of the pre-effective-date financing statement-even before this Article [Title 30, chapter 9] is enacted- and not only within the six months immediately prior to lapse. In contrast to a continuation statement, which extends the lapse date of a filed financing statement for five years, the initial financing statement has its own lapse date, which bears no relation to the lapse date of the pre-effective-date financing statement whose effectiveness the initial financing statement continues. See subsection (b) [subsection (2)].

As subsection (a) [subsection (1)] makes clear, the filing of an initial financing statement under this section continues the effectiveness of a pre-effective-date financing statement. If the effectiveness of a pre-effective-date financing statement lapses before the initial financing statement is filed, the effectiveness of the pre-effective-date financing statement cannot be continued. Rather, unless the security interest is perfected otherwise, there will be a period during which the security interest is unperfected before becoming perfected again by the filing of the initial financing statement under this section.

If an initial financing statement is filed under this section before the effective date of this Article [Title 30, chapter 9], it takes effect when this Article [Title 30, chapter 9] takes effect (assuming that it is ineffective under former Article 9 [Title 30, chapter 9]). Note, however, that former Article 9 [Title 30, chapter 9] determines whether the filing office is obligated to accept such an initial financing statement. For the reason given in the preceding paragraph, an initial financing statement filed before the effective date of this Article [Title 30, chapter 9] does not continue the effectiveness of a pre-effective-date financing statement unless the latter remains effective on the effective date of this Article [Title 30, chapter 9]. Thus, for example, if the effectiveness of the pre-effective-date financing statement lapses before this Article [Title 30, chapter 9] takes effect, the initial financing statement would not continue its effectiveness.

2. **Requirements of Initial Financing Statement Filed in Lieu of Continuation Statement.** Subsection (c) [subsection (2)] sets forth the requirements for the initial financing statement under subsection (a) [subsection (1)]. These requirements are needed to inform searchers that the initial financing statement operates to continue a financing statement filed elsewhere and to enable searchers to locate and discover the attributes of the other financing statement. A single initial financing statement may continue the effectiveness of more than one financing statement filed before this Article's effective date [July 1, 2001]. See Section 1-102(5)(a) [30-1-102(5)(a)] (words in the singular include the plural). If under this Article [Title 30, chapter 9] the collateral is of a type different from its type under former Article 9 [Title 30, chapter 9]-as would be the case, e.g., with a right to payment of lottery winnings (a "general intangible" under former Article 9 [Title 30, chapter 9] and an "account" under this Article [Title 30, chapter 9]), then subsection (c) [subsection (2)(a)] requires that the initial financing statement indicate the type under this Article [Title 30, chapter 9].

[Persons Entitled to File Initial Financing Statement or Continuation of Statement — Section 166, Ch. 305, L. 1999]

This section permits a secured party to file an initial financing statement or continuation statement necessary under this Part [not codified] to continue the effectiveness of a financing statement filed before this Article [Title 30, chapter 9] takes effect or to perfect or otherwise continue the perfection of a security interest. Because a filing described in this section typically operates to continue the effectiveness of a financing statement whose filing the debtor already has authorized, this section does not require authorization from the debtor.

[Priority — Section 167, Ch. 305, L. 1997]

1. **Law Governing Priority.** Ordinarily, this Article [Title 30, chapter 9] determines the priority of conflicting claims to collateral. However, when the relative priorities of the claims were established before this Article [Title 30, chapter 9] takes effect, former Article 9 [Title 30, chapter 9] governs.

Example 1: In 1999, SP-1 obtains a security interest in a right to payment for goods sold ("account"). SP-1 fails to file a financing statement. This Article [Title 30, chapter 9] takes effect on July 1, 2001. Thereafter, on August 1, 2001, D creates a security interest in the same account in favor of SP-2, who files a financing statement. This Article [Title 30, chapter 9] determines the relative priorities of the claims. SP-2's security interest has priority under Section 9-322(a)(1) [30-9-342(1)(a)].

Example 2: In 1999, SP-1 obtains a security interest in a right to payment for goods sold ("account"). SP-1 fails to file a financing statement. In 2000, D creates a security interest in the same account in favor of SP-2, who likewise fails to file a financing statement. This Article [Title 30, chapter 9] takes effect on July 1, 2001. Because the relative priorities of the security interests were established before the effective date of this Article [Title 30, chapter 9], former Article 9 [Title 30, chapter 9] governs priority, and SP-1's security interest has priority under former Section 9-312(5)(b) [30-9-312(5)(b)].

Example 3: The facts are as in Example 2, except that, on August 1, 2001, SP-2 files a proper financing statement under this Article [Title 30, chapter 9]. Until August 1, 2001, the relative priorities of the security interests were established before the effective date of this Article [Title 30, chapter 9], as in Example 2. However, by taking the affirmative step of filing a financing statement, SP-2 established anew the relative priority of the conflicting claims after the effective date. Thus, this Article [Title 30, chapter 9] determines priority. SP-2's security interest has priority under Section 9-322(a)(1) [30-9-342(1)(a)].

As Example 3 illustrates, relative priorities that are "established" before the effective date do not necessarily remain unchanged following the effective date. Of course, unlike priority contests among unperfected security interests, some priorities are established permanently, e.g., the rights of a buyer of property who took free of a security interest under former Article 9 [Title 30, chapter 9].

One consequence of the rule in subsection (a) [subsection (1)] is that the mere taking effect of this Article [Title 30, chapter 9] does not of itself adversely affect the priority of conflicting claims to collateral.

Example 4: In 1999, SP-1 obtains a security interest in a right to payment for lottery winnings (a "general intangible" as defined in former Article 9 [Title 30, chapter 9] but an "account" as defined in this Article [Title 30, chapter 9]). SP-1's security interest is unperfected because its filed financing statement covers only "accounts." In 2000, D creates a security interest in the same right to payment in favor of SP-2, who files a financing statement covering "accounts and general intangibles." Before this Article [Title 30, chapter 9] takes effect on July 1, 2001, SP-2's perfected security interest has priority over SP-1's unperfected security interest under former 9-312(5) [30-9-312(5)]. Because the relative priorities of the security interests were established before the effective date of this Article [Title 30, chapter 9], former Article 9 [Title 30, chapter 9] continues to govern priority after this Article [Title 30, chapter 9] takes effect. Thus, SP-2's priority is not adversely affected by this Article's [Title 30, chapter 9] having taken effect.

Note that were this Article [Title 30, chapter 9] to govern priority, SP-2 would become subordinated to SP-1 under Section 9-322(a)(1) [30-9-342(1)(a)], even though nothing changes other than this Article's [Title 30, chapter 9] having taken effect. Under Section 9-704 [sec. 163, Ch. 305, L. 1999], SP-1's security interest would become perfected; the financing statement covering "accounts" adequately covers the lottery winnings and complies with the other perfection requirements of this Article [Title 30, chapter 9], e.g., it is filed in the proper office.

Example 5: In 1999, SP-1 obtains a security interest in a right to payment for lottery winnings-a "general intangible" (as defined under former Article 9 [Title 30, chapter 9]). SP-1's security interest is unperfected because its filed financing statement covers only "accounts." In 2000, D creates a security interest in the same right to payment in favor of SP-2, who makes the same mistake and also files a financing statement covering only "accounts." Before this Article [Title 30, chapter 9] takes effect on July 1, 2001, SP-1's unperfected security interest has priority over SP-2's unperfected security interest, because SP-1's security interest was the first to attach. See former Section 9-312(5)(b) [30-9-312(5)(b)]. Because the relative priorities of the security interests were established before the effective date of this Article [Title 30, chapter 9], former Article 9 [Title 30, chapter 9] continues to govern priority after this Article [Title 30, chapter 9] takes effect. Although Section 9-704 [sec. 163, Ch. 305, L. 1999] makes both security interests perfected for purposes of this Article [Title 30, chapter 9], both are unperfected under former Article 9 [Title 30, chapter 9], which determines their relative priorities.

2. **Financing Statements Ineffective Under Former Article 9 [Title 30, chapter 9] but Effective Under this Article [Title 30, chapter 9].** If this Article [Title 30, chapter 9] determines priority, subsection (b) [subsection (2)] may apply. It deals with the case in which a filing that occurs before the effective date of this Article [Title 30, chapter 9] would be ineffective to perfect a security interest under former Article 9 [Title 30, chapter 9] but effective under this Article [Title 30, chapter 9]. For purposes of Section 9-322(a) [30-9-342(1)], the priority of a security interest that attaches after this Article [Title 30, chapter 9] takes effect and is perfected in this manner dates from the time this Article [Title 30, chapter 9] takes effect.

Example 6: In 1999, SP-1 obtains a security interest in D's existing and after-acquired instruments and files a financing statement covering "instruments." In 2000, D grants a security interest in its existing and after-acquired accounts in favor of SP-2, who files a financing statement covering "accounts." After this Article [Title 30, chapter 9] takes effect on July 1, 2001, one of D's account debtors gives D a negotiable note to evidence its obligation to pay an overdue account. Under the first-to-file-or-perfect rule in Section 9-322(a) [30-9-342(1)], SP-1 would have priority in the instrument, which constitutes SP-2's proceeds. SP-1's filing in 1999 was earlier than SP-2's in 2000. However, subsection (b) [subsection (2)] provides that, for purposes of Section 9-322(a) [30-9-342(1)], SP-1's priority dates from the time this Article [Title 30, chapter 9] takes effect (July 1, 2001). Under Section 9-322(b) [30-9-342(2)], SP-2's priority with respect to the proceeds (instrument) dates from its filing as to the original collateral (accounts). Accordingly, SP-2's security interest would be senior.

Subsection (b) [subsection 2] does not apply to conflicting security interests each of which is perfected by a pre-effective-date filing that was not effective under former Article 9 [Title 30, chapter 9] but is effective under this Article [Title 30, chapter 9].

Example 7: In 1999, SP-1 obtains a security interest in D's existing and after-acquired instruments and files a financing statement covering "instruments." In 2000, D grants a security interest in its existing and after-acquired instruments in favor of SP-2, who files a financing statement covering "instruments." After this Article [Title 30, chapter 9] takes effect on July 1, 2001, one of D's account debtors gives D a negotiable note to evidence its obligation to pay an overdue account. Under the first-to-file-or-perfect rule in Section 9-322(a) [30-9-342(1)], SP-1 would have priority in the instrument. Both filings are effective under this Article [Title 30, chapter 9], see Section 9-705(b) [sec. 164(2), Ch. 305, L. 1999], and SP-1's filing in 1999 was earlier than SP-2's in 2000. Subsection (b) [subsection 2] does not change this result.

Chapter Compiler's Comments

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Chapter Case Notes

Security Interest Created in Mobile Home — U.C.C. Secured Transactions Provisions Applicable: The debtors entered an installment contract to buy a mobile home from the sellers. They became delinquent on monthly payments, and eventually the seller invoked the acceleration clause and demanded the outstanding balance due plus notice fees. The debtors returned the mobile home to the seller, who sold it to a new buyer 2 months later. The debtors then sued, alleging violation of multiple provisions under Article 9A of Montana's adopted version of the Uniform Commercial Code (U.C.C.). The District Court denied the debtors' motion for summary judgment, in part because it concluded that there were material facts in dispute as to whether the U.C.C. applied. The Supreme Court found that the District Court had erred because the mobile home was a consumer good and the creation of a security interest in the mobile home triggered the applicability of Title 30, ch. 9A. Christman v. Clause, 2019 MT 132, 396 Mont. 142, 443 P.3d 472.

Part 1
General Provisions

Part Compiler's Comments

Saving Clause: Section 169, Ch. 305, L. 1999, provided: "(1) Except as otherwise provided in [sections 164 through 169] [sections 162 through 167—30-9A-703 through 30-9A-706, 30-9A-708, and 30-9A-709], [this act] applies to a transaction or lien within its scope, even if the transaction or lien was entered into or created before [this act] takes effect.

(2) Except as otherwise provided in subsection (3) and [sections 164 through 169] [sections 162 through 167—30-9A-703 through 30-9A-706, 30-9A-708, and 30-9A-709]:

(a) transactions and liens that were not governed by [former chapter 9, now repealed] were validly entered into or created before [this act] takes effect and would be subject to [this act] if they had been entered into or created after [this act] takes effect, and the rights, duties, and interests flowing from those transactions and liens remain valid after [this act] takes effect; and

(b) the transactions and liens may be terminated, completed, consummated, or enforced as required or permitted by [this act] or by the law that otherwise would apply if [this act] did not take effect.

(3) [This act] does not affect an action, case, or proceeding commenced before [this act] takes effect."

30-9A-101. Short title.

Official Comment

1. **Source.** This Article [Title 30, chapter 9A] supersedes former Uniform Commercial Code (UCC) Article 9 [Title 30, chapter 9, now repealed]. As did its predecessor, it provides a comprehensive scheme for the regulation of security interests in personal property and fixtures. For the most part this Article [Title 30, chapter 9A] follows the general approach and retains much of the terminology of former Article 9 [Title 30, chapter 9, now repealed]. In addition to describing many aspects of the operation and interpretation of this Article [Title 30, chapter 9A], these Comments explain the material changes that this Article [Title 30, chapter 9A] makes to former Article 9 [Title 30, chapter 9, now repealed]. Former Article 9 [Title 30, chapter 9, now repealed] superseded the wide variety of pre-UCC security devices. Unlike the Comments to former Article 9 [Title 30, chapter 9, now repealed], however, these Comments dwell very little on the pre-UCC state of the law. For that reason, the Comments to former Article 9 [Title 30, chapter 9, now repealed] will remain of substantial historical value and interest. They also will remain useful in understanding the background and general conceptual approach of this Article [Title 30, chapter 9A].

Citations to "Bankruptcy Code Section" in these Comments are to Title 11 of the United States Code as in effect on July 1, 2010.

2. **Background and History.** In 1990, the Permanent Editorial Board for the UCC with the support of its sponsors, The American Law Institute and the National Conference of Commissioners on Uniform State Laws, established a committee to study Article 9 [Title 30, chapter 9, now repealed] of the UCC. The study committee issued its report as of December 1, 1992, recommending the creation of a drafting committee for the revision of Article 9 [Title 30, chapter 9, now repealed] and also recommending numerous specific changes to Article 9 [Title 30, chapter 9, now repealed]. Organized in 1993, a drafting committee met fifteen times from 1993 to 1998. This Article [Title 30, chapter 9, now repealed] was approved by its sponsors in 1998. This Article [Title 30, chapter 9A] was conformed to revised Article 1 [Title 30, chapter 1] in 2001 and to amendments to Article 7 [Title 30, chapter 7] in 2003. The sponsors approved amendments to selected sections of this Article [Title 30, chapter 9A] in 2010.

3. **Reorganization and Renumbering; Captions; Style.** This Article [Title 30, chapter 9A] reflects a substantial reorganization of former Article 9 [Title 30, chapter 9, now repealed] and renumbering of most sections. New Part 4 [Title 30, chapter 9A, part 4] deals with several aspects of third-party rights and duties that are unrelated to perfection and priority. Some of these were covered by Part 3 of former Article 9 [Title 30, chapter 9, part 3, now repealed]. Part 5 [Title 30, chapter 9A, part 5] deals with filing (covered by former Part 4 [Title 30, chapter 9, part 4, now repealed]) and Part 6 [Title 30, chapter 9A, part 6] deals with default and enforcement (covered by former Part 5 [Title 30, chapter 9, part 5, now repealed]). Appendix I contains conforming revisions to other articles of the UCC, and Appendix II contains model provisions for production-money priority.

This Article [Title 30, chapter 9A] also includes headings for the subsections as an aid to readers. Unlike section captions, which are part of the UCC, see Section 1-107 [30-1-107], subsection headings are not a part of the official text itself and have not been approved by the sponsors. Each jurisdiction in which this Article [Title 30, chapter 9A] is introduced may consider whether to adopt the headings as a part of the statute and whether to adopt a provision clarifying the effect, if any, to be given to the headings. This Article [Title 30, chapter 9A] also has been conformed to current style conventions.

4. **Summary of Revisions.** Following is a brief summary of some of the more significant revisions of Article 9 [Title 30, chapter 9, now repealed] that are included in the 1998 revision of this Article [Title 30, chapter 9A].

a. **Scope of Article 9 [Title 30, chapter 9A].** This Article [Title 30, chapter 9A] expands the scope of Article 9 [Title 30, chapter 9, now repealed] in several respects.

Deposit accounts. Section 9-109 [30-9A-109] includes within this Article's [Title 30, chapter 9A] scope deposit accounts as original collateral, except in consumer transactions. Former Article 9 [Title 30, chapter 9, now repealed] dealt with deposit accounts only as proceeds of other collateral.

Sales of payment intangibles and promissory notes. Section 9-109 [30-9A-109] also includes within the scope of this Article [Title 30, chapter 9A] most sales of "payment intangibles" (defined in Section 9-102 [30-9A-102] as general intangibles under which an account debtor's principal obligation is monetary) and "promissory notes" (also defined in Section 9-102 [30-9A-102]). Former Article 9 [Title 30, chapter 9, now repealed] included sales of accounts and chattel paper, but not sales of payment intangibles or promissory notes. In its inclusion of sales of payment intangibles and promissory notes, this Article [Title 30, chapter 9A] continues the drafting convention found in former Article 9 [Title 30, chapter 9, now repealed]; it provides that the sale of accounts, chattel paper, payment intangibles, or promissory notes creates a "security interest." The definition of "account" in Section 9-102 [30-9A-102] also has been expanded to include various rights to payment that were general intangibles under former Article 9 [Title 30, chapter 9, now repealed].

Health-care-insurance receivables. Section 9-109 [30-9A-109] narrows Article 9's [Title 30, chapter 9A] exclusion of transfers of interests in insurance policies by carving out of the exclusion "health-care-insurance receivables" (defined in Section 9-102 [30-9A-102]). A health-care-insurance receivable is included within the definition of "account" in Section 9-102 [30-9A-102].

Nonpossessory statutory agricultural liens. Section 9-109 [30-9A-109] also brings nonpossessory statutory agricultural liens within the scope of Article 9 [Title 30, chapter 9A].

Consignments. Section 9-109 [30-9A-109] provides that "true" consignments-bailments for the purpose of sale by the bailee-are security interests covered by Article 9 [Title 30, chapter 9A], with certain exceptions. See Section 9-102 [30-9A-102] (defining "consignment"). Currently, many consignments are subject to Article 9's [Title 30, chapter 9A] filing requirements by operation of former Section 2-326 [30-2-326].

Supporting obligations and property securing rights to payment. This Article [Title 30, chapter 9A] also addresses explicitly (i) obligations, such as guaranties and letters of credit, that support payment or performance of collateral such as accounts, chattel paper, and payment intangibles, and (ii) any property (including real property) that secures a right to payment or performance that is subject to an Article 9 [Title 30, chapter 9A] security interest. See Sections 9-203, 9-308 [30-9A-203 and 30-9A-308].

Commercial tort claims. Section 9-109 [30-9A-109] expands the scope of Article 9 [Title 30, chapter 9A] to include the assignment of commercial tort claims by narrowing the exclusion of tort claims generally. However, this Article [Title 30, chapter 9A] continues to exclude tort claims for bodily injury and other non-business tort claims of a natural person. See Section 9-102 [30-9A-102] (defining "commercial tort claim").

Transfers by States and governmental units of States. Section 9-109 [30-9A-109] narrows the exclusion of transfers by States and their governmental units. It excludes only transfers covered by another statute (other than a statute generally applicable to security interests) to the extent the statute governs the creation, perfection, priority, or enforcement of security interests.

Nonassignable general intangibles, promissory notes, health-care-insurance receivables, and letter-of-credit rights. This Article [Title 30, chapter 9A] enables a security interest to attach to letter-of-credit rights, health-care-insurance receivables, promissory notes, and general intangibles, including contracts, permits, licenses, and franchises, notwithstanding a contractual or statutory prohibition against or limitation on assignment. This Article [Title 30, chapter 9A] explicitly protects third parties against any adverse effect of the creation or attempted enforcement of the security interest. See Sections 9-408, 9-409 [30-9A-408 and 30-9A-409].

Subject to Sections 9-408 and 9-409 [30-9A-408 and 30-9A-409] and two other exceptions (Sections 9-406 [30-9A-406], concerning accounts, chattel paper, and payment intangibles, and 9-407 [30-9A-407], concerning interests in leased goods), Section 9-401 [30-9A-401] establishes a baseline rule that the inclusion of transactions and collateral within the scope of Article 9 [Title 30, chapter 9A] has no effect on non-Article 9 [non-Title 30, chapter 9A] law dealing with the alienability or inalienability of property. For example, if a commercial tort claim is nonassignable under other applicable law, the fact that a security interest in the claim is within the scope of Article 9 [Title 30, chapter 9A] does not override the other applicable law's effective prohibition of assignment.

b. **Duties of Secured Party.** This Article [Title 30, chapter 9A] provides for expanded duties of secured parties.

Release of control. Section 9-208 [30-9A-208] imposes upon a secured party having control of a deposit account, investment property, or a letter-of-credit right the duty to release control when there is no secured obligation and no commitment to give value. Section 9-209 [30-9A-209] contains analogous provisions when an account debtor has been notified to pay a secured party.

Information. Section 9-210 [30-9A-210] expands a secured party's duties to provide the debtor with information concerning collateral and the obligations that it secures.

Default and enforcement. Part 6 [Title 30, chapter 9A, part 6] also includes some additional duties of secured parties in connection with default and enforcement. See, e.g., Section 9-616 [30-9A-616] (duty to explain calculation of deficiency or surplus in a consumer-goods transaction).

c. **Choice of Law.** The choice-of-law rules for the law governing perfection, the effect of perfection or nonperfection, and priority are found in Part 3, Subpart 1 (Sections 9-301 through 9-307 [30-9A-301 through 30-9A-307]). See also Section 9-316 [30-9A-316].

Where to file: Location of debtor. This Article [Title 30, chapter 9A] changes the choice-of-law rule governing perfection (i.e., where to file) for most collateral to the law of the jurisdiction where the debtor is located. See Section 9-301 [30-9A-301]. Under former Article 9 [Title 30, chapter 9, now repealed], the jurisdiction of the debtor's location governed only perfection and priority of a security interest in accounts, general intangibles, mobile goods, and, for purposes of perfection by filing, chattel paper and investment property.

Determining debtor's location. As a baseline rule, Section 9-307 [30-9A-307] follows former Section 9-103 [30-9-103, now repealed, see 30-9A-307], under which the location of the debtor is the debtor's place of business (or chief executive office, if the debtor has more than one place of business). Section 9-307 [30-9A-307] contains three major exceptions. First, a "registered organization," such as a corporation or limited liability company, is located in the State under whose law the debtor is organized, e.g., a corporate debtor's State of incorporation. Second, an individual debtor is located at his or her principal residence. Third, there are special rules for determining the location of the United States and registered organizations organized under the law of the United States.

Location of non-U.S. debtors. If, applying the foregoing rules, a debtor is located in a jurisdiction whose law does not require public notice as a condition of perfection of a nonpossessory security interest, the entity is deemed located in the District of Columbia. See Section 9-307 [30-9A-307]. Thus, to the extent that this Article [Title 30, chapter 9A] applies to non-U.S. debtors, perfection could be accomplished in many cases by a domestic filing.

Priority. For tangible collateral such as goods and instruments, Section 9-301 [30-9A-301] provides that the law applicable to priority and the effect of perfection or nonperfection will remain the law of the jurisdiction where the collateral is located, as under former Section 9-103 [30-9-103, now repealed, see 30-9A-301] (but without the confusing "last event" test). For intangible collateral, such as accounts, the applicable law for priority will be that of the jurisdiction in which the debtor is located.

Possessory security interests; agricultural liens. Perfection, the effect of perfection or nonperfection, and priority of a possessory security interest or an agricultural lien are governed by the law of the jurisdiction where the collateral subject to the security interest or lien is located. See Sections 9-301, 9-302 [30-9A-301 and 30-9A-302].

Goods covered by certificates of title; deposit accounts; letter-of-credit rights; investment property. This Article [Title 30, chapter 9A] includes several refinements to the treatment of choice-of-law matters for goods covered by certificates of title. See Section 9-303 [30-9A-303]. It also provides special choice-of-law rules, similar to those for investment property under current Articles 8 and 9 [Title 30, chapters 8 and 9A], for deposit accounts (Section 9-304 [30-9A-304]), investment property (Section 9-305 [30-9A-305]), and letter-of-credit rights (Section 9-306 [30-9A-306]).

Change in applicable law. Section 9-316 [30-9A-316] addresses perfection following a change in applicable law.

d. **Perfection.** The rules governing perfection of security interests and agricultural liens are found in Part 3, Subpart 2 (Sections 9-308 through 9-316 [30-9A-308 through 30-9A-316]).

Deposit accounts; letter-of-credit rights. With certain exceptions, this Article [Title 30, chapter 9A] provides that a security interest in a deposit account or a letter-of-credit right may be perfected only by the secured party's acquiring "control" of the deposit account or letter-of-credit right. See Sections 9-312, 9-314 [30-9A-312 and 30-9A-314]. Under Section 9-104 [30-9A-104], a secured party has "control" of a deposit account when, with the consent of the debtor, the secured party obtains the depositary bank's agreement to act on the secured party's instructions (including when the secured party becomes the account holder) or when the secured party is itself the depositary bank. The control requirements are patterned on Section 8-106 [30-8-116], which specifies the requirements for control of investment property. Under Section 9-107 [30-9A-107], "control" of a letter-of-credit right occurs when the issuer or nominated person consents to an assignment of proceeds under Section 5-114 [30-5-134].

Electronic chattel paper. Section 9-102 [30-9A-102] includes a new defined term: "electronic chattel paper." Electronic chattel paper is a record or records consisting of information stored in an electronic medium (i.e., it is not written). Perfection of a security interest in electronic chattel paper may be by control or filing. See Sections 9-105 [30-9A-105] (sui generis definition of control of electronic chattel paper), 9-312 [30-9A-312] (perfection by filing), 9-314 [30-9A-314] (perfection by control).

Investment property. The perfection requirements for "investment property" (defined in Section 9-102 [30-9A-102]), including perfection by control under Section 9-106 [30-9A-106], remain substantially unchanged. However, a new provision in Section 9-314 [30-9A-314] is designed to ensure that a secured party retains control in "repledge" transactions that are typical in the securities markets.

Instruments, agricultural liens, and commercial tort claims. This Article [Title 30, chapter 9A] expands the types of collateral in which a security interest may be perfected by filing to include instruments. See Section 9-312 [30-9A-312]. Agricultural liens and security interests in commercial tort claims also are perfected by filing, under this Article [Title 30, chapter 9A]. See Sections 9-308, 9-310 [30-9A-308 and 30-9A-310].

Sales of payment intangibles and promissory notes. Although former Article 9 [Title 30, chapter 9, now repealed] covered the outright sale of accounts and chattel paper, sales of most other types of receivables also are financing transactions to which Article 9 [Title 30, chapter 9A] should apply. Accordingly, Section 9-102 [30-9A-102] expands the definition of "account" to include many types of receivables (including "health-care-insurance receivables," defined in Section 9-102 [30-9A-102]) that former Article 9 [Title 30, chapter 9, now repealed] classified as "general intangibles." It thereby subjects to Article 9's [Title 30, chapter 9A] filing system sales of more types of receivables than did former Article 9 [Title 30, chapter 9, now repealed]. Certain sales of payment intangibles-primarily bank loan participation transactions-should not be subject to the Article 9 [Title 30, chapter 9A] filing rules. These transactions fall in a residual category of collateral, "payment intangibles" (general intangibles under which the account debtor's principal obligation is monetary), the sale of which is exempt from the filing requirements of Article 9 [Title 30, chapter 9A]. See Sections 9-102, 9-109, 9-309 [30-9A-102, 30-9A-109, and 30-9A-309] (perfection upon attachment). The perfection rules for sales of promissory notes are the same as those for sales of payment intangibles.

Possessory security interests. Several provisions of this Article [Title 30, chapter 9A] address aspects of security interests involving a secured party or a third party who is in possession of the collateral. In particular, Section 9-313 [30-9A-313] resolves a number of uncertainties under former Section 9-305 [30-9A-305]. It provides that a security interest in collateral in the possession of a third party is perfected when the third party acknowledges in an authenticated record that it holds for the secured party's benefit. Section 9-313 [30-9A-313] also provides that a third party need not so acknowledge and that its acknowledgment does not impose any duties on it, unless it otherwise agrees. A special rule in Section 9-313 [30-9A-313] provides that if a secured party already is in possession of collateral, its security interest remains perfected by possession if it delivers the collateral to a third party and the collateral is accompanied by instructions to hold it for the secured party or to redeliver it to the secured party. Section 9-313 [30-9A-313] also clarifies the limited circumstances under which a security interest in goods covered by a certificate of title may be perfected by the secured party's taking possession.

Automatic perfection. Section 9-309 [30-9A-309] lists various types of security interests as to which no public-notice step is required for perfection (e.g., purchase-money security interests in consumer goods other than automobiles). This automatic perfection also extends to a transfer of a health-care-insurance receivable to a health-care provider. Those transfers normally will be made by natural persons who receive health-care services; there is little value in requiring filing for perfection in that context. Automatic perfection also applies to security interests created by sales of payment intangibles and promissory notes. Section 9-308 [30-9A-308] provides that a perfected security interest in collateral supported by a "supporting obligation" (such as an account supported by a guaranty) also is a perfected security interest in the supporting obligation, and that a perfected security interest in an obligation secured by a security interest or lien on property (e.g., a real-property mortgage) also is a perfected security interest in the security interest or lien.

e. **Priority; Special Rules for Banks and Deposit Accounts.** The rules governing priority of security interests and agricultural liens are found in Part 3, Subpart 3 (Sections 9-317 through 9-342 [30-9A-317 through 30-9A-342]). This Article [Title 30, chapter 9A] includes several new priority rules and some special rules relating to banks and deposit accounts (Sections 9-340 through 9-342 [30-9A-340 through 30-9A-342]).

Purchase-money security interests: General; consumer-goods transactions; inventory. Section 9-103 [30-9A-103] substantially rewrites the definition of purchase-money security interest (PMSI) (although the term is not formally "defined"). The substantive changes, however, apply only to non-consumer-goods transactions. (Consumer transactions and consumer-goods transactions are discussed below in Comment 4.j.) For non-consumer-goods transactions, Section 9-103 [30-9A-103] makes clear that a security interest in collateral may be (to some extent) both a PMSI as well as a non-PMSI, in accord with the "dual status" rule applied by some courts under former Article 9 [Title 30, chapter 9, now repealed] (thereby rejecting the "transformation" rule). The definition provides an even broader conception of a PMSI in inventory, yielding a result that accords with private agreements entered into in response to the uncertainty under former Article 9 [Title 30, chapter 9, now repealed]. It also treats consignments as purchase-money security interests in inventory. Section 9-324 [30-9A-324] revises the PMSI priority rules, but for the most part without material change in substance. Section 9-324 [30-9A-324] also clarifies the priority rules for competing PMSIs in the same collateral.

Purchase-money security interests in livestock; agricultural liens. Section 9-324 [30-9A-324] provides a special PMSI priority, similar to the inventory PMSI priority rule, for livestock. Section 9-322 [30-9A-322] (which contains the baseline first-to-file-or-perfect priority rule) also recognizes special non-Article 9 [non-Title 30, chapter 9A] priority rules for agricultural liens, which can override the baseline first-in-time rule.

Purchase-money security interests in software. Section 9-324 [30-9A-324] contains a new priority rule for a software purchase-money security interest. (Section 9-102 [30-9A-102] includes a definition of "software.") Under Section 9-103 [30-9A-103], a software PMSI includes a PMSI in software that is used in goods that are also subject to a PMSI. (Note also that the definition of "chattel paper" has been expanded to include records that evidence a monetary obligation and a security interest in specific goods and software used in the goods.)

Investment property. The priority rules for investment property are substantially similar to the priority rules found in former Section 9-115 [30-9-115, now repealed, see 30-9A-106, 30-9A-203, 30-9A-308, 30-9A-309, 30-9A-313, 30-9A-314, and 30-9A-328], which was added in conjunction with the 1994 revisions to UCC Article 8 [Title 30, chapter 8]. Under Section 9-328 [30-9A-328], if a secured party has control of investment property (Sections 8-106, 9-106 [30-8-116, 30-9A-106]), its security interest is senior to a security interest perfected in another manner (e.g., by filing). Also under Section 9-328 [30-9A-328], security interests perfected by control generally rank according to the time that control is obtained or, in the case of a security entitlement or a commodity contract carried in a commodity account, the time when the control arrangement is entered into. This is a change from former Section 9-115 [30-9-115, now repealed, see 30-9A-314], under which the security interests ranked equally. However, as between a securities intermediary's security interest in a security entitlement that it maintains for the debtor and a security interest held by another secured party, the securities intermediary's security interest is senior.

Deposit accounts. This Article's [Title 30, chapter 9A] priority rules applicable to deposit accounts are found in Section 9-327 [30-9A-327]. They are patterned on and are similar to those for investment property in former Section 9-115 [30-9-115, now repealed, see 30-9A-327] and Section 9-328 [30-9A-328] of this Article [Title 30, chapter 9A]. Under Section 9-327 [30-9A-327], if a secured party has control of a deposit account, its security interest is senior to a security interest perfected in another manner (i.e., as cash proceeds). Also under Section 9-327 [30-9A-327], security interests perfected by control rank according to the time that control is obtained, but as between a depositary bank's security interest and one held by another secured party, the depositary bank's security interest is senior. A corresponding rule in Section 9-340 [30-9A-340] makes a depositary bank's right of set-off generally senior to a security interest held by another secured party. However, if the other secured party becomes the depositary bank's customer with respect to the deposit account, then its security interest is senior to the depositary bank's security interest and right of set-off. Sections 9-327, 9-340 [30-9A-327 and 30-9A-340].

Letter-of-credit rights. The priority rules for security interests in letter-of-credit rights are found in Section 9-329 [30-9A-329]. They are somewhat analogous to those for deposit accounts. A security interest perfected by control has priority over one perfected in another manner (i.e., as a supporting obligation for the collateral in which a security interest is perfected). Security interests in a letter-of-credit right perfected by control rank according to the time that control is obtained. However, the rights of a transferee beneficiary or a nominated person are independent and superior to the extent provided in Section 5-114 [30-5-134]. See Section 9-109(c)(4) [30-9A-102(3)(d), now repealed, see 30-9A-102].

Chattel paper and instruments. Section 9-330 [30-9A-330] is the successor to former Section 9-308 [30-9-308, now repealed, see 30-9A-330]. As under former Section 9-308 [30-9-308, now repealed, see 30-9A-330], differing priority rules apply to purchasers of chattel paper who give new value and take possession (or, in the case of electronic chattel paper, obtain control) of the collateral depending on whether a conflicting security interest in the collateral is claimed merely as proceeds. The principal change relates to the role of knowledge and the effect of an indication of a previous assignment of the collateral. Section 9-330 [30-9A-330] also affords priority to purchasers of instruments who take possession in good faith and without knowledge that the purchase violates the rights of the competing secured party. In addition, to qualify for priority, purchasers of chattel paper, but not of instruments, must purchase in the ordinary course of business.

Proceeds. Section 9-322 [30-9A-322] contains new priority rules that clarify when a special priority of a security interest in collateral continues or does not continue with respect to proceeds of the collateral. Other refinements to the priority rules for proceeds are included in Sections 9-324 [30-9A-324] (purchase-money security interest priority) and 9-330 [30-9A-330] (priority of certain purchasers of chattel paper and instruments).

Miscellaneous priority provisions. This Article [Title 30, chapter 9A] also includes (i) clarifications of selected good-faith-purchase and similar issues (Sections 9-317, 9-331 [30-9A-317 and 30-9A-331]); (ii) new priority rules to deal with the "double debtor" problem arising when a debtor creates a security interest in collateral acquired by the debtor subject to a security interest created by another person (Section 9-325 [30-9A-325]); (iii) new priority rules to deal with the problems created when a change in corporate structure or the like results in a new entity that has become bound by the original debtor's after-acquired property agreement (Section 9-326 [30-9A-326]); (iv) a provision enabling most transferees of funds from a deposit account or money to take free of a security interest (Section 9-332 [30-9A-332]); (v) substantially rewritten and refined priority rules dealing with accessions and commingled goods (Sections 9-335, 9-336 [30-9A-335 and 30-9A-336]); (vi) revised priority rules for security interests in goods covered by a certificate of title (Section 9-337 [30-9A-337]); and (vii) provisions designed to ensure that security interests in deposit accounts will not extend to most transferees of funds on deposit or payees from deposit accounts and will not otherwise "clog" the payments system (Sections 9-341, 9-342 [30-9A-341 and 30-9A-342]).

Model provisions relating to production-money security interests. Appendix II to this Article [Title 30, chapter 9A] contains model definitions and priority rules relating to "production-money security interests" held by secured parties who give new value used in the production of crops. Because no consensus emerged on the wisdom of these provisions during the drafting process, the sponsors make no recommendation on whether these model provisions should be enacted.

f. **Proceeds.** Section 9-102 [30-9A-102] contains an expanded definition of "proceeds" of collateral which includes additional rights and property that arise out of collateral, such as distributions on account of collateral and claims arising out of the loss or nonconformity of, defects in, or damage to collateral. The term also includes collections on account of "supporting obligations," such as guarantees.

g. **Part 4 [Title 30, chapter 9A, part 4]: Additional Provisions Relating to Third-Party Rights.** New Part 4 [Title 30, chapter 9A, part 4] contains several provisions relating to the relationships between certain third parties and the parties to secured transactions. It contains new Sections 9-401 [30-9A-401] (replacing former Section 9-311) [30-9-311, now repealed, see

30-9A-401] (alienability of debtor's rights), 9-402 [30-9A-402] (replacing former Section 9-317 [30-9-317, now repealed, see 30-9A-402]) (secured party not obligated on debtor's contracts), 9-403 [30-9A-403] (replacing former Section 9-206) [30-9-206, now repealed, see 30-9A-403] (agreement not to assert defenses against assignee), 9-404, 9-405, and 9-406 [30-9A-404, 30-9A-405, and 30-9A-406] (replacing former Section 9-318 [30-9-318, now repealed, see 30-9A-404 through 30-9A-406]) (rights acquired by assignee, modification of assigned contract, discharge of account debtor, restrictions on assignment of account, chattel paper, promissory note, or payment intangible ineffective), 9-407 [30-9A-407] (replacing some provisions of former Section 2A-303 [30-2A-303]) (restrictions on creation or enforcement of security interest in leasehold interest or lessor's residual interest ineffective). It also contains new Sections 9-408 [30-9A-408] (restrictions on assignment of promissory notes, health-care-insurance receivables ineffective, and certain general intangibles ineffective) and 9-409 [30-9A-409] (restrictions on assignment of letter-of-credit rights ineffective), which are discussed above.

h. **Filing.** Part 5 (formerly Part 4 [Title 30, chapter 9, part 4, now repealed]) of Article 9 [Title 30, chapter 9A, part 5] has been substantially rewritten to simplify the statutory text and to deal with numerous problems of interpretation and implementation that have arisen over the years.

Medium-neutrality. This Article [Title 30, chapter 9A] is "medium-neutral"; that is, it makes clear that parties may file and otherwise communicate with a filing office by means of records communicated and stored in media other than on paper.

Identity of person who files a record; authorization. Part 5 [Title 30, chapter 9A, part 5] is largely indifferent as to the person who effects a filing. Instead, it addresses whose authorization is necessary for a person to file a record with a filing office. The filing scheme does not contemplate that the identity of a "filer" will be a part of the searchable records. This approach is consistent with, and a necessary aspect of, eliminating signatures or other evidence of authorization from the system (except to the extent that filing offices may choose to employ authentication procedures in connection with electronic communications). As long as the appropriate person authorizes the filing, or, in the case of a termination statement, the debtor is entitled to the termination, it is largely insignificant whether the secured party or another person files any given record.

Section 9-509 [30-9A-509] collects in one place most of the rules that determine when a record may be filed. In general, the debtor's authorization is required for the filing of an initial financing statement or an amendment that adds collateral. With one further exception, a secured party of record's authorization is required for the filing of other amendments. The exception arises if a secured party has failed to provide a termination statement that is required because there is no outstanding secured obligation or commitment to give value. In that situation, a debtor is authorized to file a termination statement indicating that it has been filed by the debtor.

Financing statement formal requisites. The formal requisites for a financing statement are set out in Section 9-502 [30-9A-502]. A financing statement must provide the name of the debtor and the secured party and an indication of the collateral that it covers. Sections 9-503 and 9-506 [30-9A-503 and 30-9A-506] address the sufficiency of a name provided on a financing statement and clarify when a debtor's name is correct and when an incorrect name is insufficient. Section 9-504 [30-9A-504] addresses the indication of collateral covered. Under Section 9-504 [30-9A-504], a super-generic description (e.g.,"all assets" or "all personal property") in a financing statement is a sufficient indication of the collateral. (Note, however, that a super-generic description is inadequate for purposes of a security agreement. See Sections 9-108, 9-203 [30-9A-108 and 30-9A-203].) To facilitate electronic filing, this Article [Title 30, chapter 9A] does not require that the debtor's signature or other authorization appear on a financing statement. Instead, it prohibits the filing of unauthorized financing statements and imposes liability upon those who violate the prohibition. See Sections 9-509, 9-626 [30-9A-509 and 30-9A-626].

Filing-office operations. Part 5 [Title 30, chapter 9A, part 5] contains several provisions governing filing operations. First, it prohibits the filing office from rejecting an initial financing statement or other record for a reason other than one of the few that are specified. See Sections 9-520, 9-516 [30-9A-520 and 30-9A-516]. Second, the filing office is obliged to link all subsequent records (e.g., assignments, continuation statements, etc.) to the initial financing statement to which they relate. See Section 9-519 [30-9A-519]. Third, the filing office may delete a financing statement and related records from the files no earlier than one year after lapse (lapse normally is five years after the filing date), and then only if a continuation statement has not been filed. See Sections 9-515, 9-519, 9-522 [30-9A-515, 30-9A-519, and 30-9A-522]. Thus, a financing statement and related records would be discovered by a search of the files even after the filing of a termination statement. This approach helps eliminate filing-office discretion and also eases problems associated with multiple secured parties and multiple partial assignments. Fourth, Part 5 [Title 30, chapter 9A, part 5] mandates performance standards for filing offices. See Sections 9-519, 9-520, 9-523 [30-9A-519, 30-9A-520, and 30-9A-523]. Fifth, it provides for the promulgation of filing-office rules to deal with details best left out of the statute and requires the filing office to submit periodic reports. See Sections 9-526, 9-527 [30-9A-526 and 30-9A-527].

Defaulting or missing secured parties and fraudulent filings. In some areas of the country, serious problems have arisen from fraudulent financing statements that are filed against public officials and other persons. This Article [Title 30, chapter 9A] addresses the fraud problem by providing the opportunity for a debtor to file a termination statement when a secured party wrongfully refuses or fails to provide a termination statement. See Section 9-509 [30-9A-509]. This opportunity also addresses the problem of secured parties that simply disappear through mergers or liquidations. In addition, Section 9-518 [30-9A-518] affords a statutory method by which a debtor who believes that a filed record is inaccurate or was wrongfully filed may indicate that fact in the files, albeit without affecting the efficacy, if any, of the challenged record.

Extended period of effectiveness for certain financing statements. Section 9-515 [30-9A-515] contains an exception to the usual rule that financing statements are effective for five years unless a continuation statement is filed to continue the effectiveness for another five years. Under that section, an initial financing statement filed in connection with a “public-finance transaction” or a “manufactured-home transaction” (terms defined in Section 9-102 [30-9A-102]) is effective for 30 years.

National form of financing statement and related forms. Section 9-521 [30-9A-521] provides for uniform, national written forms of financing statements and related written records that must be accepted by a filing office that accepts written records.

i. **Default and Enforcement.** Part 6 of Article 9 [Title 30, chapter 9A, part 6] extensively revises former Part 5 [Title 30, chapter 9, part 5, now repealed]. Provisions relating to enforcement of consumer-goods transactions and consumer transactions are discussed in Comment 4.j.

Debtor, secondary obligor; waiver. Section 9-602 [30-9A-602] clarifies the identity of persons who have rights and persons to whom a secured party owes specified duties under Part 6 [Title 30, chapter 9A, part 6]. Under that section, the rights and duties are enjoyed by and run to the “debtor,” defined in Section 9-102 [30-9A-102] to mean any person with a non-lien property interest in collateral, and to any “obligor.” However, with one exception (Section 9-616 [30-9A-616], as it relates to a consumer obligor), the rights and duties concerned affect non-debtor obligors only if they are “secondary obligors.” “Secondary obligor” is defined in Section 9-102 [30-9A-102] to include one who is secondarily obligated on the secured obligation, e.g., a guarantor, or one who has a right of recourse against the debtor or another obligor with respect to an obligation secured by collateral. However, under Section 9-628 [30-9A-628], the secured party is relieved from any duty or liability to any person unless the secured party knows that the person is a debtor or obligor. Resolving an issue on which courts disagreed under former Article 9 [Title 30, chapter 9, now repealed], this Article [Title 30, chapter 9A] generally prohibits waiver by a secondary obligor of its rights and a secured party’s duties under Part 6 [Title 30, chapter 9A, part 6]. See Section 9-602 [30-9A-602]. However, Section 9-624 [30-9A-624] permits a secondary obligor or debtor to waive the right to notification of disposition of collateral and, in a non-consumer transaction, the right to redeem collateral, if the secondary obligor or debtor agrees to do so after default.

Rights of collection and enforcement of collateral. Section 9-607 [30-9A-607] explains in greater detail than former 9-502 [30-9-502, now repealed, see 30-9A-607 and 30-9A-608] the rights of a secured party who seeks to collect or enforce collateral, including accounts, chattel paper, and payment intangibles. It also sets forth the enforcement rights of a depositary bank holding a security interest in a deposit account maintained with the depositary bank. Section 9-607 [30-9A-607] relates solely to the rights of a secured party vis-a-vis a debtor with respect to collections and enforcement. It does not affect the rights or duties of third parties, such as account debtors on collateral, which are addressed elsewhere (e.g., Section 9-406 [30-9A-406]). Section 9-608 [30-9A-608] clarifies the manner in which proceeds of collection or enforcement are to be applied.

Disposition of collateral: Warranties of title. Section 9-610 [30-9A-610] imposes on a secured party who disposes of collateral the warranties of title, quiet possession, and the like that are otherwise applicable under other law. It also provides rules for the exclusion or modification of those warranties.

Disposition of collateral: Notification, application of proceeds, surplus and deficiency, other effects. Section 9-611 [30-9A-611] requires a secured party to give notification of a disposition of collateral to other secured parties and lienholders who have filed financing statements against the debtor covering the collateral. (That duty was eliminated by the 1972 revisions to Article 9 [Title 30, chapter 9, now repealed].) However, that section relieves the secured party from that duty when the secured party undertakes a search of the records and a report of the results is unreasonably delayed. Section 9-613 [30-9A-613], which applies only to non-consumer transactions, specifies the contents of a sufficient notification of disposition and provides that a notification sent 10 days or more before the earliest time for disposition is sent within a reasonable time. Section 9-615 [30-9A-615] addresses the application of proceeds of disposition, the entitlement of a debtor to any surplus, and the liability of an obligor for any deficiency. Section 9-619 [30-9A-619] clarifies the effects of a disposition by a secured party, including the rights of transferees of the collateral.

Rights and duties of secondary obligor. Section 9-618 [30-9A-618] provides that a secondary obligor obtains the rights and assumes the duties of a secured party if the secondary obligor receives an assignment of a secured obligation, agrees to assume the secured party's rights and duties upon a transfer to it of collateral, or becomes subrogated to the rights of the secured party with respect to the collateral. The assumption, transfer, or subrogation is not a disposition of collateral under Section 9-610 [30-9A-610], but it does relieve the former secured party of further duties. Former Section 9-504(5) [30-9-504(5), now repealed, see 30-9A-618] did not address whether a secured party was relieved of its duties in this situation.

Transfer of record or legal title. Section 9-619 [30-9A-619] contains a new provision making clear that a transfer of record or legal title to a secured party is not of itself a disposition under Part 6 [Title 30, chapter 9A, part 6]. This rule applies regardless of the circumstances under which the transfer of title occurs.

Strict foreclosure. Section 9-620 [30-9A-620], unlike former Section 9-505 [30-9-505, now repealed, see 30-9A-620, 30-9A-621, and 30-9A-624], permits a secured party to accept collateral in partial satisfaction, as well as full satisfaction, of the obligations secured. This right of strict foreclosure extends to intangible as well as tangible property. Section 9-622 [30-9A-622] clarifies the effects of an acceptance of collateral on the rights of junior claimants. It rejects the approach taken by some courts-deeming a secured party to have constructively retained collateral in satisfaction of the secured obligations-in the case of a secured party's unreasonable delay in the disposition of collateral. Instead, unreasonable delay is relevant when determining whether a disposition under Section 9-610 [30-9A-610] is commercially reasonable.

Effect of noncompliance: "Rebuttable presumption" test. Section 9-626 [30-9A-626] adopts the "rebuttable presumption" test for the failure of a secured party to proceed in accordance with certain provisions of Part 6 [Title 30, chapter 9A, part 6]. (As discussed in Comment 4.j., the test does not necessarily apply to consumer transactions.) Under this approach, the deficiency claim of a noncomplying secured party is calculated by crediting the obligor with the greater of the actual net proceeds of a disposition and the amount of net proceeds that would have been realized if the disposition had been conducted in accordance with Part 6 [Title 30, chapter 9A, part 6] (e.g., in a commercially reasonable manner). For non-consumer transactions, Section 9-626 [30-9A-626] rejects the "absolute bar" test that some courts have imposed; that approach bars a noncomplying secured party from recovering any deficiency, regardless of the loss (if any) the debtor suffered as a consequence of the noncompliance.

"Low-price" dispositions: Calculation of deficiency and surplus. Section 9-615(f) [30-9A-615(6)] addresses the problem of procedurally regular dispositions that fetch a low price. Subsection (f) [subsection (6)] provides a special method for calculating a deficiency if the proceeds of a disposition of collateral to a secured party, a person related to the secured party, or a secondary obligor are "significantly below the range of proceeds that a complying disposition to a person other than the secured party, a person related to the secured party, or a secondary obligor would have brought." ("Person related to" is defined in Section 9-102 [30-9A-102].) In these situations there is reason to suspect that there may be inadequate incentives to obtain a better price. Consequently, instead of calculating a deficiency (or surplus) based on the actual net proceeds, the deficiency (or surplus) would be calculated based on the proceeds that would have been received in a disposition to a person other than the secured party, a person related to the secured party, or a secondary obligor.

j. **Consumer Goods, Consumer-Goods Transactions, and Consumer Transactions.** This Article [Title 30, chapter 9A] (including the accompanying conforming revisions (see Appendix I)) includes several special rules for "consumer goods," "consumer transactions," and "consumer-goods transactions." Each term is defined in Section 9-102 [30-9A-102].

(i) Revised Sections 2-502 and 2-716 [30-2-502 and 30-2-716] provide a buyer of consumer goods with enhanced rights to possession of the goods, thereby accelerating the opportunity to achieve "buyer in ordinary course of business" status under Section 1-201 [30-1-201].

(ii) Section 9-103(e) [30-9A-103(5)] (allocation of payments for determining extent of purchase-money status), (f) [30-9A-103(6)] (purchase-money status not affected by cross-collateralization, refinancing, restructuring, or the like), and (g) [30-9A-103(7)] (secured party has burden of establishing extent of purchase-money status) do not apply to consumer-goods transactions. Sections 9-103 [30-9A-103] also provides that the limitation of those provisions to transactions other than consumer-goods transactions leaves to the courts the proper rules for consumer-goods transactions and prohibits the courts from drawing inferences from that limitation.

(iii) Section 9-108 [30-9A-108] provides that in a consumer transaction a description of consumer goods, a security entitlement, securities account, or commodity account "only by [UCC-defined] type of collateral" is not a sufficient collateral description in a security agreement.

(iv) Sections 9-403 and 9-404 [30-9A-403 and 30-9A-404] make effective the Federal Trade Commission's anti-holder-in-due-course rule (when applicable), 16 C.F.R. Part 433, even in the absence of the required legend.

(v) The 10-day safe-harbor for notification of a disposition provided by Section 9-612 [30-9A-612] does not apply in a consumer transaction.

(vi) Section 9-613 [30-9A-613] (contents and form of notice of disposition) does not apply to a consumer-goods transaction.

(vii) Section 9-614 [30-9A-614] contains special requirements for the contents of a notification of disposition and a safe-harbor, "plain English" form of notification, for consumer-goods transactions.

(viii) Section 9-616 [30-9A-616] requires a secured party in a consumer-goods transaction to provide a debtor with a notification of how it calculated a deficiency at the time it first undertakes to collect a deficiency.

(ix) Section 9-620 [30-9A-620] prohibits partial strict foreclosure with respect to consumer goods collateral and, unless the debtor agrees to waive the requirement in an authenticated record after default, in certain cases requires the secured party to dispose of consumer goods collateral which has been repossessed.

(x) Section 9-626 [30-9A-626] ("rebuttable presumption" rule) does not apply to a consumer transaction. Section 9-626 [30-9A-626] also provides that its limitation to transactions other than consumer transactions leaves to the courts the proper rules for consumer transactions and prohibits the courts from drawing inferences from that limitation.

k. **Good Faith.** Section 9-102 [30-9A-102] contains a new definition of "good faith" that includes not only "honesty in fact" but also "the observance of reasonable commercial standards of fair dealing." The definition is similar to the ones adopted in connection with other, recently completed revisions of the UCC.

l. **Transition Provisions.** Part 7 (Sections 9-701 through 9-707 [Title 30, chapter 9A, part 7]) contains transition provisions. Transition from former Article 9 [Title 30, chapter 9, now repealed] to this Article [Title 30, chapter 9A] will be particularly challenging in view of its expanded scope, its modification of choice-of-law rules for perfection and priority, and its expansion of the methods of perfection.

m. **Conforming and Related Amendments to Other UCC Articles [chapters].** Appendix I contains several proposed revisions to the provisions and Comments of other UCC articles [chapters]. For the most part the revisions are explained in the Comments to the proposed revisions. Cross-references in other UCC articles [chapters] to sections of Article 9 [Title 30, chapter 9A] also have been revised.

Article 1 [Title 30, chapter 1]. Revised Section 1-201 [30-1-201] contains revisions to the definitions of "buyer in ordinary course of business," "purchaser," and "security interest."

Articles 2 and 2A [Title 30, chapters 2 and 2A. Sections 2-210, 2-326, 2-502, 2-716, 2A-303, and 2A-307 [30-2-210, 30-2-326, 30-2-502, 30-2-716, 30-2A-303, and 30-2A-307] have been revised to address the intersection between Articles 2 and 2A and Article 9 [Title 30, chapters 2 and 2A and chapter 9A].

Article 5 [Title 30, chapter 5]. New Section 5-118 [30-5-118] is patterned on Section 4-210 [30-4-210]. It provides for a security interest in documents presented under a letter of credit in favor of the issuer and a nominated person on the letter of credit.

Article 8 [Title 30, chapter 8]. Revisions to Section 8-106 [30-8-116], which deals with "control" of securities and security entitlements, conform it to Section 8-302 [sic] [30-8-331], which deals with "delivery." Revisions to Section 8-110 [30-8-120], which deals with a "securities intermediary's jurisdiction," conform it to the revised treatment of a "commodity intermediary's jurisdiction" in Section 9-305 [30-9A-305]. Sections 8-301 and 8-302 [30-8-331 and 30-8-332] have been revised for clarification. Section 8-510 [30-8-510] has been revised to conform it to the revised priority rules of Section 9-328 [30-9A-328]. Several Comments in Article 8 [Title 30, chapter 8] also have been revised.

30-9A-102. Definitions and index of definitions.

Official Comments

[*Corresponding U.C.C. Section:* Section 9-102, U.C.C.]

1. **Source.** All terms that are defined in Article 9 [Title 30, chapter 9A] and used in more than one section are consolidated in this section. Note that the definition of "security interest" is found in Section 1-201 [30-1-201], not in this Article [Title 30, chapter 9A], and has been revised. See Appendix I. Many of the definitions in this section are new; many others derive from those in former Section 9-105 [30-9-105, now repealed, see 30-9A-102]. The following Comments also indicate other sections of former Article 9 [Title 30, chapter 9, now repealed] that defined (or explained) terms.

2. **Parties to Secured Transactions.**

a. **"Debtor"; "Obligor"; "Secondary Obligor."** Determining whether a person was a "debtor" under former Section 9-105(1)(d) [30-9-105(1)(d), now repealed, see 30-9A-102(1)(bb)] required a close examination of the context in which the term was used. To reduce the need for this examination, this Article [Title 30, chapter 9A] redefines "debtor" and adds new defined terms, "secondary obligor" and "obligor." In the context of Part 6 [Title 30, chapter 9A, part 6] (default and enforcement), these definitions distinguish among three classes of persons: (i) those persons who may have a stake in the proper enforcement of a security interest by virtue of their non-lien property interest (typically, an ownership interest) in the collateral, (ii) those persons who may have a stake in the proper enforcement of the security interest because of their obligation to pay the secured debt, and (iii) those persons who have an obligation to pay the secured debt but have no stake in the proper enforcement of the security interest. Persons in the first class are debtors. Persons in the second class are secondary obligors if any portion of the obligation is secondary or if the obligor has a right of recourse against the debtor or another obligor with respect to an obligation secured by collateral. One must consult the law of suretyship to determine whether an obligation is secondary. The Restatement (3d), Suretyship and Guaranty § 1 (1996), contains a useful explanation of the concept. Obligors in the third class are neither debtors nor secondary obligors. With one exception (Section 9-616 [30-9A-616], as it relates to a consumer obligor), the rights and duties provided by Part 6 [Title 30, chapter 9A, part 6] affect non-debtor obligors only if they are "secondary obligors."

By including in the definition of "debtor" all persons with a property interest (other than a security interest in or other lien on collateral), the definition includes transferees of collateral, whether or not the secured party knows of the transfer or the transferee's identity. Exculpatory provisions in Part 6 [Title 30, chapter 9A, part 6] protect the secured party in that circumstance. See Sections 9-605 and 9-628 [30-9A-605 and 30-9A-628]. The definition renders unnecessary former Section 9-112 [30-9-112, now repealed, see 30-9A-202], which governed situations in which collateral was not owned by the debtor. The definition also includes a "consignee," as defined in this section, as well as a seller of accounts, chattel paper, payment intangibles, or promissory notes.

Secured parties and other lienholders are excluded from the definition of "debtor" because the interests of those parties normally derive from and encumber a debtor's interest. However, if in a separate secured transaction a secured party grants, as debtor, a security interest in its own interest (i.e., its security interest and any obligation that it secures), the secured party is a debtor in that transaction. This typically occurs when a secured party with a security interest in specific goods assigns chattel paper.

Consider the following examples:

Example 1: Behnfeldt borrows money and grants a security interest in her Miata to secure the debt. Behnfeldt is a debtor and an obligor.

Example 2: Behnfeldt borrows money and grants a security interest in her Miata to secure the debt. Bruno co-signs a negotiable note as maker. As before, Behnfeldt is the debtor and an obligor. As an accommodation party (see Section 3-419 [30-3-419]), Bruno is a secondary obligor. Bruno has this status even if the note states that her obligation is a primary obligation and that she waives all suretyship defenses.

Example 3: Behnfeldt borrows money on an unsecured basis. Bruno co-signs the note and grants a security interest in her Honda to secure her obligation. Inasmuch as Behnfeldt does not have a property interest in the Honda, Behnfeldt is not a debtor. Having granted the security interest, Bruno is the debtor. Because Behnfeldt is a principal obligor, she is not a secondary obligor. Whatever the outcome of enforcement of the security interest against the Honda or Bruno's secondary obligation, Bruno will look to Behnfeldt for her losses. The enforcement will not affect Behnfeldt's aggregate obligations.

When the principal obligor (borrower) and the secondary obligor (surety) each has granted a security interest in different collateral, the status of each is determined by the collateral involved.

Example 4: Behnfeldt borrows money and grants a security interest in her Miata to secure the debt. Bruno co-signs the note and grants a security interest in her Honda to secure her obligation. When the secured party enforces the security interest in Behnfeldt's Miata, Behnfeldt is the debtor, and Bruno is a secondary obligor. When the secured party enforces the security interest in the Honda, Bruno is the "debtor." As in Example 3, Behnfeldt is an obligor, but not a secondary obligor.

b. **"Secured Party."** The secured party is the person in whose favor the security interest has been created, as determined by reference to the security agreement. This definition controls, among other things, which person has the duties and potential liability that Part 6 [Title 30, chapter 9A, part 6] imposes upon a secured party. The definition of "secured party" also includes a "consignee," a person to which accounts, chattel paper, payment intangibles, or promissory notes have been sold, and the holder of an agricultural lien.

The definition of "secured party" clarifies the status of various types of representatives. Consider, for example, a multi-bank facility under which Bank A, Bank B, and Bank C are lenders and Bank A serves as the collateral agent. If the security interest is granted to the banks, then they are the secured parties. If the security interest is granted to Bank A as collateral agent, then Bank A is the secured party.

c. **Other Parties.** A "consumer obligor" is defined as the obligor in a consumer transaction. Definitions of "new debtor" and "original debtor" are used in the special rules found in Sections 9-326 and 9-508 [30-9A-326 and 30-9A-508].

3. **Definitions Relating to Creation of a Security Interest.**

a. **"Collateral."** As under former Section 9-105 [30-9-105, now repealed, see 30-9A-102(1)(l)], "collateral" is the property subject to a security interest and includes accounts and chattel paper that have been sold. It has been expanded in this Article [Title 30, chapter 9A]. The term now explicitly includes proceeds subject to a security interest. It also reflects the broadened scope of the Article [Title 30, chapter 9A]. It includes property subject to an agricultural lien as well as payment intangibles and promissory notes that have been sold.

b. **"Security Agreement."** The definition of "security agreement" is substantially the same as under former Section 9-105 [30-9-105, now repealed, see 30-9A-102(1)(uuu)]—an agreement that creates or provides for a security interest. However, the term frequently was used colloquially in former Article 9 [Title 30, chapter 9, now repealed] to refer to the document or writing that contained a debtor's security agreement. This Article [Title 30, chapter 9A] eliminates that usage, reserving the term for the more precise meaning specified in the definition.

Whether an agreement creates a security interest depends not on whether the parties intend that the law characterize the transaction as a security interest but rather on whether the transaction falls within the definition of "security interest" in Section 1-201 [30-1-201]. Thus, an agreement that the parties characterize as a "lease" of goods may be a "security agreement," notwithstanding the parties' stated intention that the law treat the transaction as a lease and not as a secured transaction.

4. **Goods-Related Definitions.**

a. **"Goods"; "Consumer Goods"; "Equipment"; "Farm Products"; "Farming Operation"; "Inventory."** The definition of "goods" is substantially the same as the definition in former Section 9-105 [30-9-105, now repealed, see 30-9A-102(1)(rr)]. This Article [Title 30, chapter 9A] also retains the four mutually-exclusive "types" of collateral that consist of goods: "consumer goods," "equipment," "farm products," and "inventory." The revisions are primarily for clarification.

The classes of goods are mutually exclusive. For example, the same property cannot simultaneously be both equipment and inventory. In borderline cases-a physician's car or a farmer's truck that might be either consumer goods or equipment-the principal use to which the property is put is determinative. Goods can fall into different classes at different times. For example, a radio may be inventory in the hands of a dealer and consumer goods in the hands of a consumer. As under former Article 9 [Title 30, chapter 9, now repealed], goods are "equipment" if they do not fall into another category.

The definition of "consumer goods" follows former Section 9-109 [30-9-109, now repealed, see 30-9A-102(1)(w)]. The classification turns on whether the debtor uses or bought the goods for use "primarily for personal, family, or household purposes."

Goods are inventory if they are leased by a lessor or held by a person for sale or lease. The revised definition of "inventory" makes clear that the term includes goods leased by the debtor to others as well as goods held for lease. (The same result should have obtained under the former definition.) Goods to be furnished or furnished under a service contract, raw materials, and work in process also are inventory. Implicit in the definition is the criterion that the sales or leases are or will be in the ordinary course of business. For example, machinery used in manufacturing is equipment, not inventory, even though it is the policy of the debtor to sell machinery when it becomes obsolete or worn. Inventory also includes goods that are consumed in a business (e.g., fuel used in operations). In general, goods used in a business are equipment if they are fixed assets or have, as identifiable units, a relatively long period of use, but are inventory, even though not held for sale or lease, if they are used up or consumed in a short period of time in producing a product or providing a service.

Goods are "farm products" if the debtor is engaged in farming operations with respect to the goods. Animals in a herd of livestock are covered whether the debtor acquires them by purchase or as a result of natural increase. Products of crops or livestock remain farm products as long as they have not been subjected to a manufacturing process. The terms "crops" and "livestock" are not defined. The new definition of "farming operations" is for clarification only.

Crops, livestock, and their products cease to be "farm products" when the debtor ceases to be engaged in farming operations with respect to them. If, for example, they come into the possession of a marketing agency for sale or distribution or of a manufacturer or processor as raw materials, they become inventory. Products of crops or livestock, even though they remain in the possession of a person engaged in farming operations, lose their status as farm products if they are subjected to a manufacturing process. What is and what is not a manufacturing operation is not specified in this Article [Title 30, chapter 9A]. At one end of the spectrum, some processes are so closely connected with farming-such as pasteurizing milk or boiling sap to produce maple syrup or sugar-that they would not constitute manufacturing. On the other hand an extensive canning operation would be manufacturing. Once farm products have been subjected to a manufacturing operation, they normally become inventory.

The revised definition of "farm products" clarifies the distinction between crops and standing timber and makes clear that aquatic goods produced in aquacultural operations may be either crops or livestock. Although aquatic goods that are vegetable in nature often would be crops and those that are animal would be livestock, this Article [Title 30, chapter 9A] leaves the courts free to classify the goods on a case-by-case basis. See Section 9-324 [30-9A-324], Comment 11.

b. **"Accession"; "Manufactured Home"; "Manufactured-Home Transaction."** Other specialized definitions of goods include "accession" (see the special priority and enforcement rules in Section 9-335 [30-9A-335]), and "manufactured home" (see Section 9-515 [30-9A-515], permitting a financing statement in a "manufactured-home transaction" to be effective for 30 years). The definition of "manufactured home" borrows from the federal Manufactured Housing Act, 42 U.S.C. § 5401 et seq., and is intended to have the same meaning.

c. **"As-Extracted Collateral."** Under this Article [Title 30, chapter 9A], oil, gas, and other minerals that have not been extracted from the ground are treated as real property, to which this Article [Title 30, chapter 9A] does not apply. Upon extraction, minerals become personal property (goods) and eligible to be collateral under this Article [Title 30, chapter 9A]. See the definition of "goods," which excludes "oil, gas, and other minerals before extraction." To take account of financing practices reflecting the shift from real to personal property, this Article [Title 30, chapter 9A] contains special rules for perfecting security interests in minerals which attach upon extraction and in accounts resulting from the sale of minerals at the wellhead or minehead. See, e.g., Sections 9-301(4) [30-9A-301(4)] (law governing perfection and priority); 9-501 [30-9A-501] (place of filing), 9-502 [30-9A-502] (contents of financing statement), 9-519 [30-9A-519] (indexing of records). The new term, "as-extracted collateral," refers to the minerals and related accounts to which the special rules apply. The term "at the wellhead" encompasses arrangements based on a sale of the produce at the moment that it issues from the ground and is measured, without technical distinctions as to whether title passes at the "Christmas tree" of a well, the far side of a gathering tank, or at some other point. The term "at . . . the minehead" is comparable.

The following examples explain the operation of these provisions.

Example 5: Debtor owns an interest in oil that is to be extracted. To secure Debtor's obligations to Lender, Debtor enters into an authenticated agreement granting Lender an interest in the oil.

Although Lender may acquire an interest in the oil under real-property law, Lender does not acquire a security interest under this Article [Title 30, chapter 9A] until the oil becomes personal property, i.e., until is extracted and becomes "goods" to which this Article [Title 30, chapter 9A] applies. Because Debtor had an interest in the oil before extraction and Lender's security interest attached to the oil as extracted, the oil is "as-extracted collateral."

Example 6: Debtor owns an interest in oil that is to be extracted and contracts to sell the oil to Buyer at the wellhead. In an authenticated agreement, Debtor agrees to sell to Lender the right to payment from Buyer. This right to payment is an account that constitutes "as-extracted collateral." If Lender then resells the account to Financer, Financer acquires a security interest. However, inasmuch as the debtor-seller in that transaction, Lender, had no interest in the oil before extraction, Financer's collateral (the account it owns) is not "as-extracted collateral."

Example 7: Under the facts of Example 6, before extraction, Buyer grants a security interest in the oil to Bank. Although Bank's security interest attaches when the oil is extracted, Bank's security interest is not in "as-extracted collateral," inasmuch as its debtor, Buyer, did not have an interest in the oil before extraction.

5. **Receivables-related Definitions.**

a. **"Account"; "Health-Care-Insurance Receivable"; "As-Extracted Collateral."** The definition of "account" has been expanded and reformulated. It is no longer limited to rights to payment relating to goods or services. Many categories of rights to payment that were classified as general intangibles under former Article 9 [Title 30, chapter 9, now repealed] are accounts under this Article [Title 30, chapter 9A]. Thus, if they are sold, a financing statement must be filed to perfect the buyer's interest in them. As used in the definition of "account," a right to payment "arising out of the use of a credit or charge card or information contained on or for use with the card" is the right of a card issuer to payment from its cardholder. A credit-card or charge-card transaction may give rise to other rights to payments; however, those other rights do not "arise out of the use" of the card or information contained on or for use with the card. Among the types of property that are expressly excluded from the definition of account is "a right to payment for money or funds advanced or sold." As defined in Section 1-201 [30-1-201], "money" is limited essentially to currency. As used in the exclusion from the definition of "account," however, "funds" is a broader concept (although the term is not defined). For example, when a bank-lender credits a borrower's deposit account for the amount of a loan, the bank's advance of funds is not a transaction giving rise to an account.

The definition of "health-care-insurance receivable" is new. It is a subset of the definition of "account." However, the rules generally applicable to account debtors on accounts do not apply to insurers obligated on health-care-insurance receivables. See Sections 9-404(e), 9-405(d), 9-406(i) [30-9A-404(5), 30-9A-405(4), and 30-9A-406(8)].

Note that certain accounts also are "as-extracted collateral." See Comment 4.c., Examples 6 and 7.

b. **"Chattel Paper"; "Electronic Chattel Paper"; "Tangible Chattel Paper."** "Chattel paper" consists of a monetary obligation together with a security interest in or a lease of specific goods if the obligation and security interest or lease are evidenced by "a record or records." The definition has been expanded from that found in former Article 9 [Title 30, chapter 9, now repealed] to include records that evidence a monetary obligation and a security interest in specific goods and software used in the goods, a security interest in specific goods and license of software used in the goods, or a lease of specific goods and license of software used in the goods. The expanded definition covers transactions in which the debtor's or lessee's monetary obligation includes amounts owed with respect to software used in the goods. The monetary obligation with respect to the software need not be owed under a license from the secured party or lessor, and the secured party or lessor need not be a party to the license transaction itself. Among the types of monetary obligations that are included in "chattel paper" are amounts that have been advanced by the secured party or lessor to enable the debtor or lessee to acquire or obtain financing for a license of the software used in the goods.

Charters of vessels are expressly excluded from the definition of chattel paper; they are accounts. The term "charter" as used in this section includes bareboat charters, time charters, successive voyage charters, contracts of affreightment, contracts of carriage, and all other arrangements for the use of vessels.

Under former Section 9-105 [30-9-105, now repealed, see 30-9A-102], only if the evidence of an obligation consisted of "a writing or writings" could an obligation qualify as chattel paper. In this Article [Title 30, chapter 9A], traditional, written chattel paper is included in the definition of "tangible chattel paper." "Electronic chattel paper" is chattel paper that is stored in an electronic medium instead of in tangible form. The concept of an electronic medium should be construed liberally to include electrical, digital, magnetic, optical, electromagnetic, or any other current or similar emerging technologies.

c. **"Instrument"; "Promissory Note."** The definition of "instrument" includes a negotiable instrument. As under former Section 9-105 [30-9-105, now repealed, see 30-9A-102], it also includes any other right to payment of a monetary obligation that is evidenced by a writing of a type that in ordinary course of business is transferred by delivery (and, if necessary, an indorsement or assignment). Except in the case of chattel paper, the fact that an instrument is secured by a security interest or encumbrance on property does not change the character of the instrument as such or convert the combination of the instrument and collateral into a separate classification of personal property. The definition makes clear that rights to payment arising out of credit-card transactions are not instruments. The definition of "promissory note" is new, necessitated by the inclusion of sales of promissory notes within the scope of Article 9 [Title 30, chapter 9A]. It explicitly excludes obligations arising out of "orders" to pay (e.g., checks) as opposed to "promises" to pay. See Section 3-104 [30-3-104].

d. **"General Intangible"; "Payment Intangible."** "General intangible" is the residual category of personal property, including things in action, that is not included in the other defined types of collateral. Examples are various categories of intellectual property and the right to payment of a loan of funds that is not evidenced by chattel paper or an instrument. The definition has been revised to exclude commercial tort claims, deposit accounts, and letter-of-credit rights. Each of the three is a separate type of collateral. One important consequence of this exclusion is that tortfeasors (commercial tort claims), banks (deposit accounts), and persons obligated on letters of credit (letter-of-credit rights) are not "account debtors" having the rights and obligations set forth in Sections 9-404, 9-405, and 9-406 [30-9A-404, 30-9A-405, and 30-9A-406]. In particular, tortfeasors, banks, and persons obligated on letters of credit are not obligated to pay an assignee (secured party) upon receipt of the notification described in Section 9-404(a) [30-9A-404(1)]. See Comment 5.h. Another important consequence relates to the adequacy of the description in the security agreement. See Section 9-108 [30-9A-108].

"Payment intangible" is a subset of the definition of "general intangible." The sale of a payment intangible is subject to this Article [Title 30, chapter 9A]. See Section 9-109(a)(3) [30-9A-109(1)(c)]. Virtually any intangible right could give rise to a right to payment of money once one hypothesizes, for example, that the account debtor is in breach of its obligation. The term "payment intangible," however, embraces only those general intangibles "under which the account debtor's principal obligation is a monetary obligation." (Emphasis added.) A debtor's right to payment from another person of amounts received by the other person on the debtor's behalf, including the right of a merchant in a credit-card, debit-card, prepaid-card, or other payment-card transaction to payment of amounts received by its bank from the card system in settlement of the transaction, is a "payment intangible." (In contrast, the right of a credit-card issuer to payment arising out of the use of a credit card is an "account.")

In classifying intangible collateral, a court should begin by identifying the particular rights that have been assigned. The account debtor (promisor) under a particular contract may owe several types of monetary obligations as well as other, nonmonetary obligations. If the promisee's right to payment of money is assigned separately, the right is an account or payment intangible, depending on how the account debtor's obligation arose. When all the promisee's rights are assigned together, an account, a payment intangible, and a general intangible all may be involved, depending on the nature of the rights.

A right to the payment of money is frequently buttressed by ancillary rights, such as rights arising from a purchase agreement, note, or mortgage requiring insurance on the collateral or forbidding removal of the collateral, rights arising from covenants to preserve the creditworthiness of the promisor, and the lessor's rights with respect to leased goods that arise upon the lessee's default (see Section 2A-523 [30-2A-523]). This Article [Title 30, chapter 9A] does not treat these ancillary rights separately from the rights to payment to which they relate. For example, attachment and perfection of an assignment of a right to payment of a monetary obligation, whether it be an account or payment intangible, also carries these ancillary rights. Thus, an assignment of the lessor's right to payment under a lease also transfers the lessor's rights with respect to the leased goods under Section 2A-523 [30-2A-523]. If, taken together, the lessor's rights to payment and with respect to the leased goods are evidenced by chattel paper, then, contrary to *In re Commercial Money Center, Inc.*, 350 B.R. 465 (Bankr. App. 9th Cir. 2006), an assignment of the lessor's right to payment constitutes an assignment of the chattel paper. Although an agreement excluding the lessor's rights with respect to the leased goods from an assignment of the lessor's right to payment may be effective between the parties, the agreement does not affect the characterization of the collateral to the prejudice of creditors of, and purchasers from, the assignor.

Every "payment intangible" is also a "general intangible." Likewise, "software" is a "general intangible" for purposes of this Article [Title 30, chapter 9A]. See Comment 25. Accordingly, except as otherwise provided, statutory provisions applicable to general intangibles apply to payment intangibles and software.

e. **"Letter-of-Credit Right."** The term "letter-of-credit right" embraces the rights to payment and performance under a letter of credit (defined in Section 5-102 [30-5-122]). However, it does not include a beneficiary's right to demand payment or performance. Transfer of those rights to a transferee beneficiary is governed by Article 5 [Title 30, chapter 5]. See Sections 9-107 [30-9A-107], Comment 4, and 9-329 [30-9A-329], Comments 3 and 4.

f. **"Supporting Obligation."** This new term covers the most common types of credit enhancements-suretyship obligations (including guarantees) and letter-of-credit rights that support one of the types of collateral specified in the definition. As explained in Comment 2.a., suretyship law determines whether an obligation is "secondary" for purposes of this definition. Section 9-109 [30-9A-109] generally excludes from this Article [Title 30, chapter 9A] transfers of interests in insurance policies. However, the regulation of a secondary obligation as an insurance product does not necessarily mean that it is a "policy of insurance" for purposes of the exclusion in Section 9-109 [30-9A-109]. Thus, this Article [Title 30, chapter 9A] may cover a secondary obligation (as a supporting obligation), even if the obligation is issued by a regulated insurance company and the obligation is subject to regulation as an "insurance" product.

This Article [Title 30, chapter 9A] contains rules explicitly governing attachment, perfection, and priority of security interests in supporting obligations. See Sections 9-203, 9-308, 9-310, and 9-322 [30-9A-203, 30-9A-308, 30-9A-310, and 30-9A-322]. These provisions reflect the principle that a supporting obligation is an incident of the collateral it supports.

Collections of or other distributions under a supporting obligation are "proceeds" of the supported collateral as well as "proceeds" of the supporting obligation itself. See Section 9-102 [30-9A-102] (defining "proceeds") and Comment 13.b. As such, the collections and distributions are subject to the priority rules applicable to proceeds generally. See Section 9-322 [30-9A-322]. However, under the special rule governing security interests in a letter-of-credit right, a secured party's failure to obtain control (Section 9-107 [30-9A-107]) of a letter-of-credit right supporting collateral may leave its security interest exposed to a priming interest of a party who does take control. See Section 9-329 [30-9A-329] (security interest in a letter-of-credit right perfected by control has priority over a conflicting security interest).

g. **"Commercial Tort Claim."** This term is new. A tort claim may serve as original collateral under this Article [Title 30, chapter 9A] only if it is a "commercial tort claim." See Section 9-109(d) [30-9A-109(4)]. Although security interests in commercial tort claims are within its scope, this Article [Title 30, chapter 9A] does not override other applicable law restricting the assignability of a tort claim. See Section 9-401 [30-9A-401]. A security interest in a tort claim also may exist under this Article [Title 30, chapter 9A] if the claim is proceeds of other collateral.

h. **"Account Debtor."** An "account debtor" is a person obligated on an account, chattel paper, or general intangible. The account debtor's obligation often is a monetary obligation; however, this is not always the case. For example, if a franchisee uses its rights under a franchise agreement (a general intangible) as collateral, then the franchisor is an "account debtor." As a general matter, Article 3 [Title 30, chapter 3], and not Article 9 [Title 30, chapter 9A], governs obligations on negotiable instruments. Accordingly, the definition of "account debtor" excludes obligors on negotiable instruments constituting part of chattel paper. The principal effect of this change from the definition in former Article 9 [Title 30, chapter 9, now repealed] is that the rules in Sections 9-403, 9-404, 9-405, and 9-406 [30-9A-403, 30-9A-404, 30-9A-405, and 30-9A-406], dealing with the rights of an assignee and duties of an account debtor, do not apply to an assignment of chattel paper in which the obligation to pay is evidenced by a negotiable instrument. (Section 9-406(d) [30-9A-406(4)], however, does apply to promissory notes, including negotiable promissory notes.) Rather, the assignee's rights are governed by Article 3 [Title 30, chapter 3]. Similarly, the duties of an obligor on a nonnegotiable instrument are governed by non-Article 9 [non-Title 30, chapter 9A] law unless the nonnegotiable instrument is a part of chattel paper, in which case the obligor is an account debtor.

i. **Receivables Under Government Entitlement Programs.** This Article [Title 30, chapter 9A] does not contain a defined term that encompasses specifically rights to payment or performance under the many and varied government entitlement programs. Depending on the nature of a right under a program, it could be an account, a payment intangible, a general intangible other than a payment intangible, or another type of collateral. The right also might be proceeds of collateral (e.g., crops).

6. **Investment-Property-Related Definitions: "Commodity Account"; "Commodity Contract"; "Commodity Customer"; "Commodity Intermediary"; "Investment Property."** These definitions are substantially the same as the corresponding definitions in former Section 9-115 [30-9-115, now repealed, see 30-9A-102]. "Investment property" includes securities, both certificated and uncertificated, securities accounts, security entitlements, commodity accounts, and commodity contracts. The term investment property includes a "securities account" in order to facilitate transactions in which a debtor wishes to create a security interest in all of the investment positions held through a particular account rather than in particular positions carried in the account. Former Section 9-115 [30-9-115, now repealed, see 30-9A-102] was added in conjunction with Revised Article 8 [Title 30, chapter 8] and contained a variety of rules applicable to security interests in investment property. These rules have been relocated to the appropriate sections of Article 9 [Title 30, chapter 9A]. See, e.g., Sections 9-203 [30-9A-203] (attachment), 9-314 [30-9A-314] (perfection by control), 9-328 [30-9A-328] (priority).

The terms "security," "security entitlement," and related terms are defined in Section 8-102 [30-8-112], and the term "securities account" is defined in Section 8-501 [30-8-501]. The terms "commodity account," "commodity contract," "commodity customer," and "commodity intermediary" are defined in this section. Commodity contracts are not "securities" or "financial assets" under Article 8 [Title 30, chapter 8]. See Section 8-103(f) [30-8-113(5)]. Thus, the relationship between commodity intermediaries and commodity customers is not governed by the indirect-holding-system rules of Part 5 of Article 8 [Title 30, chapter 8, part 5]. For securities, Article 9 [Title 30, chapter 9A] contains rules on security interests, and Article 8 [Title 30, chapter 8] contains rules on the rights of transferees, including secured parties, on such matters as the rights of a transferee if the transfer was itself wrongful and gives rise to an adverse claim. For commodity contracts, Article 9 [Title 30, chapter 9A] establishes rules on security interests, but questions of the sort dealt with in Article 8 [Title 30, chapter 8] for securities are left to other law.

The indirect-holding-system rules of Article 8 [Title 30, chapter 8] are sufficiently flexible to be applied to new developments in the securities and financial markets, where that is appropriate. Accordingly, the definition of "commodity contract" is narrowly drafted to ensure that it does not operate as an obstacle to the application of the Article 8 [Title 30, chapter 8] indirect-holding-system rules to new products. The term "commodity contract" covers those contracts that are traded on or subject to the rules of a designated contract market and foreign commodity contracts that are carried on the books of American commodity intermediaries. The effect of this definition is that the category of commodity contracts that are excluded from Article 8 [Title 30, chapter 8] but governed by Article 9 [Title 30, chapter 9A] is essentially the same as the category of contracts that fall within the exclusive regulatory jurisdiction of the federal Commodity Futures Trading Commission.

Commodity contracts are different from securities or other financial assets. A person who enters into a commodity futures contract is not buying an asset having a certain value and holding it in anticipation of increase in value. Rather the person is entering into a contract to buy or sell a commodity at set price for delivery at a future time. That contract may become advantageous or disadvantageous as the price of the commodity fluctuates during the term of the contract. The rules of the commodity exchanges require that the contracts be marked to market on a daily basis; that is, the customer pays or receives any increment attributable to that day's price change. Because commodity customers may incur obligations on their contracts, they are required to provide collateral at the outset, known as "original margin," and may be required to provide additional amounts, known as "variation margin," during the term of the contract.

The most likely setting in which a person would want to take a security interest in a commodity contract is where a lender who is advancing funds to finance an inventory of a physical commodity requires the borrower to enter into a commodity contract as a hedge against the risk of decline in the value of the commodity. The lender will want to take a security interest in both the commodity itself and the hedging commodity contract. Typically, such arrangements are structured as security interests in the entire commodity account in which the borrower carries the hedging contracts, rather than in individual contracts.

One important effect of including commodity contracts and commodity accounts in Article 9 [Title 30, chapter 9A] is to provide a clearer legal structure for the analysis of the rights of commodity clearing organizations against their participants and futures commission merchants against their customers. The rules and agreements of commodity clearing organizations generally provide that the clearing organization has the right to liquidate any participant's positions in order to satisfy obligations of the participant to the clearing corporation. Similarly, agreements between futures commission merchants and their customers generally provide that the futures commission merchant has the right to liquidate a customer's positions in order to satisfy obligations of the customer to the futures commission merchant.

The main property that a commodity intermediary holds as collateral for the obligations that the commodity customer may incur under its commodity contracts is not other commodity contracts carried by the customer but the other property that the customer has posted as margin. Typically, this property will be securities. The commodity intermediary's security interest in such securities is governed by the rules of this Article [Title 30, chapter 9A] on security interests in securities, not the rules on security interests in commodity contracts or commodity accounts.

Although there are significant analytic and regulatory differences between commodities and securities, the development of commodity contracts on financial products in the past few decades has resulted in a system in which the commodity markets and securities markets are closely linked. The rules on security interests in commodity contracts and commodity accounts provide a structure that may be essential in times of stress in the financial markets. Suppose, for example that a firm has a position in a securities market that is hedged by a position in a commodity market, so that payments that the firm is obligated to make with respect to the securities position will be covered by the receipt of funds from the commodity position. Depending upon the settlement cycles of the different markets, it is possible that the firm could find itself in a position where it is obligated to make the payment with respect to the securities position before it receives the matching funds from the commodity position. If cross-margining arrangements have not been developed between the two markets, the firm may need to borrow funds temporarily to make the earlier payment. The rules on security interests in investment property would facilitate the use of positions in one market as collateral for loans needed to cover obligations in the other market.

7. **Consumer-Related Definitions: "Consumer Debtor"; "Consumer Goods"; "Consumer-goods transaction"; "Consumer Obligor"; "Consumer Transaction."** The definition of "consumer goods" (discussed above) is substantially the same as the definition in former Section 9-109 [30-9-109, now repealed, see 30-9A-102]. The definitions of "consumer debtor," "consumer obligor," "consumer-goods transaction," and "consumer transaction" have been added in connection with various new (and old) consumer-related provisions and to designate certain provisions that are inapplicable in consumer transactions.

"Consumer-goods transaction" is a subset of "consumer transaction." Under each definition, both the obligation secured and the collateral must have a personal, family, or household purpose. However, "mixed" business and personal transactions also may be characterized as a consumer-goods transaction or consumer transaction. Subparagraph (A) [subsection (1)(x)(i)] of the definition of consumer-goods transactions and clause (i) [subsection (1)(z)(i)] of the definition of consumer transaction are primary purposes tests. Under these tests, it is necessary to determine the primary purpose of the obligation or obligations secured. Subparagraph (B) and clause (iii) [subsections (1)(x)(ii) and (1)(z)(iii)] of these definitions are satisfied if any of the collateral is consumer goods, in the case of a consumer-goods transaction, or "is held or acquired primarily for personal, family, or household purposes," in the case of a consumer transaction. The fact that some of the obligations secured or some of the collateral for the obligation does not satisfy the tests (e.g., some of the collateral is acquired for a business purpose) does not prevent a transaction from being a "consumer transaction" or "consumer-goods transaction."

8. **Filing-Related Definitions: "Continuation Statement"; "File Number"; "Filing Office"; "Filing-office Rule"; "Financing Statement"; "Fixture Filing"; "Manufactured-Home Transaction"; "New Debtor"; "Original Debtor"; "Public-Finance Transaction"; "Termination Statement"; "Transmitting Utility."** These definitions are used exclusively or primarily in the filing-related provisions in Part 5 [Title 30, chapter 9A, part 5]. Most are self-explanatory and are discussed in the Comments to Part 5 [Title 30, chapter 9A, part 5]. A financing statement filed in a manufactured-home transaction or a public-finance transaction may remain effective for 30 years instead of the 5 years applicable to other financing statements. See Section 9-515(b) [30-9A-515(2)]. The definitions relating to medium neutrality also are significant for the filing provisions. See Comment 9.

The definition of "transmitting utility" has been revised to embrace the business of transmitting communications generally to take account of new and future types of communications technology. The term designates a special class of debtors for whom separate filing rules are provided in Part 5 [Title 30, chapter 9A, part 5], thereby obviating the many local fixture filings that would be necessary under the rules of Section 9-501 [30-9A-501] for a far-flung public-utility debtor. A transmitting utility will not necessarily be regulated by or operating as such in a jurisdiction where fixtures are located. For example, a utility might own transmission lines in a jurisdiction, although the utility generates no power and has no customers in the jurisdiction.

9. Definitions Relating to Medium Neutrality.

a. **"Record."** In many, but not all, instances, the term "record" replaces the term "writing" and "written." A "record" includes information that is in intangible form (e.g., electronically stored) as well as tangible form (e.g., written on paper). Given the rapid development and commercial adoption of modern communication and storage technologies, requirements that documents or communications be "written," "in writing," or otherwise in tangible form do not necessarily reflect or aid commercial practices.

A "record" need not be permanent or indestructible, but the term does not include any oral or other communication that is not stored or preserved by any means. The information must be stored on paper or in some other medium. Information that has not been retained other than through human memory does not qualify as a record. Examples of current technologies commercially used to communicate or store information include, but are not limited to, magnetic media, optical discs, digital voice messaging systems, electronic mail, audio tapes, and photographic media, as well as paper. "Record" is an inclusive term that includes all of these methods of storing or communicating information. Any "writing" is a record. A record may be authenticated. See Comment 9.b. A record may be created without the knowledge or intent of a particular person.

Like the terms "written" or "in writing," the term "record" does not establish the purposes, permitted uses, or legal effect that a record may have under any particular provision of law. Whatever is filed in the Article 9 [Title 30, chapter 9A] filing system, including financing statements, continuation statements, and termination statements, whether transmitted in tangible or intangible form, would fall within the definition. However, in some instances, statutes or filing-office rules may require that a paper record be filed. In such cases, even if this Article [Title 30, chapter 9A] permits the filing of an electronic record, compliance with those statutes or rules is necessary. Similarly, a filer must comply with a statute or rule that requires a particular type of encoding or formatting for an electronic record.

This Article [Title 30, chapter 9A] sometimes uses the terms "for record," "of record," "record or legal title," and "record owner." Some of these are terms traditionally used in real-property law. The definition of "record" in this Article [Title 30, chapter 9A] now explicitly excepts these usages from the defined term. Also, this Article [Title 30, chapter 9A] refers to a record that is filed or recorded in real-property recording systems to record a mortgage as a "record of a mortgage." This usage recognizes that the defined term "mortgage" means an interest in real property; it does not mean the record that evidences, or is filed or recorded with respect to, the mortgage.

b. **"Authenticate"; "Communicate"; "Send."** The terms "authenticate" and "authenticated" generally replace "sign" and "signed." "Authenticated" replaces and broadens the definition of "signed," in Section 1-201 [30-1-201], to encompass authentication of all records, not just writings. (References to authentication of, e.g., an agreement, demand, or notification mean, of course, authentication of a record containing an agreement, demand, or notification.) The terms "communicate" and "send" also contemplate the possibility of communication by nonwritten media. These definitions include the act of transmitting both tangible and intangible records. The definition of "send" replaces, for purposes of this Article [Title 30, chapter 9A], the corresponding term in Section 1-201 [30-1-201]. The reference to "usual means of communication" in that definition contemplates an inquiry into the appropriateness of the method of transmission used in the particular circumstances involved.

10. Scope-Related Definitions.

a. **Expanded Scope of Article [Title 30, chapter 9A]: "Agricultural Lien"; "Consignment"; "Payment Intangible"; "Promissory Note."** These new definitions reflect the expanded scope of Article 9 [Title 30, chapter 9A], as provided in Section 9-109(a) [30-9A-109(1)].

b. **Reduced Scope of Exclusions: "Governmental Unit"; "Health-Care-Insurance Receivable"; "Commercial Tort Claims."** These new definitions reflect the reduced scope of the exclusions, provided in Section 9-109(c) and (d) [30-9A-109(3) and (4)], of transfers by governmental debtors and assignments of interests in insurance policies and commercial tort claims.

11. Choice-of-Law-Related Definitions: "Certificate of Title"; "Governmental Unit"; "Jurisdiction of Organization"; "Public Organic Record"; "Registered Organization"; "State." These new definitions reflect the changes in the law governing perfection and priority of security interests and agricultural liens provided in Part 3, Subpart 1 [30-9A-301 through 30-9A-307].

Statutes often require applicants for a certificate of title to identify all security interests on the application and require the issuing agency to indicate the identified security interests on the certificate. Some of these statutes provide that priority over the rights of a lien creditor (i.e., perfection of a security interest) in goods covered by the certificate occurs upon indication of the security interest on the certificate; that is, they provide for the indication of the security interest on the certificate as a "condition" of perfection. Other statutes contemplate that perfection is achieved upon the occurrence of another act, e.g., delivery of the application to the issuing agency, that "results" in the indication of the security interest on the certificate. A certificate governed by either type of statute can qualify as a "certificate of title" under this Article [Title 30, chapter 9A]. The statute providing for the indication of a security interest need not expressly state the connection between the indication and perfection. For example, a certificate issued pursuant to a statute that requires applicants to identify security interests, requires the issuing agency to indicate the identified security interests on the certificate, but is silent concerning the legal consequences of the indication would be a "certificate of title" if, under a judicial interpretation of the statute, perfection of a security interest is a legal consequence of the indication. Likewise, a certificate would be a "certificate of title" if another statute provides, expressly or as interpreted, the requisite connection between the indication and perfection.

The first sentence of the definition of "certificate of title" includes certificates consisting of tangible records, of electronic records, and of combinations of tangible and electronic records.

In many States, a certificate of title covering goods that are encumbered by a security interest is delivered to the secured party by the issuing authority. To eliminate the need for the issuance of a paper certificate under these circumstances, several States have revised their certificate-of-title statutes to permit or require a State agency to maintain an electronic record that evidences ownership of the goods and in which a security interest in the goods may be noted. The second sentence of the definition provides that such a record is a "certificate of title" if it is in fact maintained as an alternative to the issuance of a paper certificate of title, regardless of whether the certificate-of-title statute provides that the record is a certificate of title and even if the statute does not expressly state that the record is maintained instead of issuing a paper certificate.

Not every organization that may provide information about itself in the public records is a "registered organization." For example, a general partnership is not a "registered organization," even if it files a statement of partnership authority under Section 303 of the Uniform Partnership Act (1994) or an assumed name ("dba") certificate. This is because such a partnership is not formed or organized by the filing of a record with, or the issuance of a record by, a State or the United States. In contrast, corporations, limited liability companies, and limited partnerships ordinarily are "registered organizations."

Not every record concerning a registered organization that is filed with, or issued by, a State or the United States is a "public organic record." For example, a certificate of good standing issued with respect to a corporation or a published index of domestic corporations would not be a "public organic record" because its issuance or publication does not form or organize the corporations named.

When collateral is held in a trust, one must look to non-UCC law to determine whether the trust is a "registered organization." Non-UCC law typically distinguishes between statutory trusts and common-law trusts. A statutory trust is formed by the filing of a record, commonly referred to as a certificate of trust, in a public office pursuant to a statute. See, e.g., Uniform Statutory Trust Entity Act § 201 (2009); Delaware Statutory Trust Act, Del. Code Ann. tit. 12, § 3801 et seq. A statutory trust is a juridical entity, separate from its trustee and beneficial owners, that may sue and be sued, own property, and transact business in its own name. Inasmuch as a statutory trust is a "legal or commercial entity," it qualifies as a "person other than an individual," and therefore as an "organization," under Section 1-201 [30-1-201]. A statutory trust that is formed by the filing of a record in a public office is a "registered organization," and the filed record is a "public organic record" of the statutory trust, if the filed record is available to the public for inspection. (The requirement that a record be "available to the public for inspection" is satisfied if a copy of the relevant record is available for public inspection.)

Unlike a statutory trust, a common-law trust—whether its purpose is donative or commercial—arises from private action without the filing of a record in a public office. See Uniform Trust Code § 401 (2000); Restatement (Third) of Trusts § 10 (2003). Moreover, under traditional law, a common-law trust is not itself a juridical entity and therefore must sue and be sued, own property, and transact business in the name of the trustee acting in the capacity of trustee. A common-law trust that is a "business trust," i.e., that has a business or commercial purpose, is an "organization" under Section 1-201 [30-1-201]. However, such a trust would not be a "registered organization" if, as is typically the case, the filing of a public record is not needed to form it.

In some states, however, the trustee of a common-law trust that has a commercial or business purpose is required by statute to file a record in a public office following the trust's formation. See, e.g., Mass. Gen. Laws Ch. 182, § 2; Fla. Stat. Ann. § 609.02. A business trust that is required to file its organic record in a public office is a "registered organization" under the second sentence of the definition if the filed record is available to the public for inspection. Any organic record required to be filed, and filed, with respect to a common-law business trust after the trust is formed is a "public organic record" of the trust. Some statutes require a trust or other organization to file, after formation or organization, a record other than an organic record. See, e.g., N.Y. Gen Assn's Law § 18 (requiring associations doing business within New York to file a certificate designating the secretary of state as an agent upon whom process may be served). This requirement does not render the organization a "registered organization" under the second sentence of the definition, and the record is not a "public organic record."

12. **Deposit-Account-Related Definitions: "Deposit Account"; "Bank."** The revised definition of "deposit account" incorporates the definition of "bank," which is new. The definition derives from the definitions of "bank" in Sections 4-105(1) and 4A-105(a)(2) [30-4-105(1) and 30-4A-105(1)(b)], which focus on whether the organization is "engaged in the business of banking."

Deposit accounts evidenced by Article 9 [Title 30, chapter 9A] "instruments" are excluded from the term "deposit account." In contrast, former Section 9-105 [30-9-105, now repealed, see 30-9A-102] excluded from the former definition "an account evidenced by a certificate of deposit." The revised definition clarifies the proper treatment of nonnegotiable or uncertificated certificates of deposit. Under the definition, an uncertificated certificate of deposit would be a deposit account (assuming there is no writing evidencing the bank's obligation to pay) whereas a nonnegotiable certificate of deposit would be a deposit account only if it is not an "instrument" as defined in this section (a question that turns on whether the nonnegotiable certificate of deposit is "of a type that in ordinary course of business is transferred by delivery with any necessary indorsement or assignment.")

A deposit account evidenced by an instrument is subject to the rules applicable to instruments generally. As a consequence, a security interest in such an instrument cannot be perfected by "control" (see Section 9-104 [30-9A-104]), and the special priority rules applicable to deposit accounts (see Sections 9-327 and 9-340 [30-9A-327 and 30-9A-340]) do not apply.

The term "deposit account" does not include "investment property," such as securities and security entitlements. Thus, the term also does not include shares in a money-market mutual fund, even if the shares are redeemable by check.

13. **Proceeds-Related Definitions: "Cash Proceeds"; "Noncash Proceeds"; "Proceeds."** The revised definition of "proceeds" expands the definition beyond that contained in former Section 9-306 [30-9-306, now repealed, see 30-9A-102] and resolves ambiguities in the former section.

a. **Distributions on Account of Collateral.** The phrase "whatever is collected on, or distributed on account of, collateral," in subparagraph (B) [subsection (1)(lll)(ii)], is broad enough to cover cash or stock dividends distributed on account of securities or other investment property that is original collateral. Compare former Section 9-306 [30-9-306, now repealed, see 30-9A-102] ("Any payments or distributions made with respect to investment property collateral are proceeds."). This section rejects the holding of Hastie v. FDIC, 2 F.3d 1042 (10th Cir. 1993) (postpetition cash dividends on stock subject to a prepetition pledge are not "proceeds" under Bankruptcy Code Section 552(b)), to the extent the holding relies on the Article 9 [Title 30, chapter 9A] definition of "proceeds."

b. **Distributions on Account of Supporting Obligations.** Under subparagraph (B) [subsection (1)(lll)(ii)], collections on and distributions on account of collateral consisting of various credit-support arrangements ("supporting obligations," as defined in Section 9-102 [30-9A-102]) also are proceeds. Consequently, they are afforded treatment identical to proceeds collected from or distributed by the obligor on the underlying (supported) right to payment or other collateral. Proceeds of supporting obligations also are proceeds of the underlying rights to payment or other collateral.

c. **Proceeds of Proceeds.** The definition of "proceeds" no longer provides that proceeds of proceeds are themselves proceeds. That idea is expressed in the revised definition of "collateral" in Section 9-102 [30-9A-102]. No change in meaning is intended.

d. **Proceeds Received by Person Who Did Not Create Security Interest.** When collateral is sold subject to a security interest and the buyer then resells the collateral, a question arose under former Article 9 [Title 30, chapter 9, now repealed] concerning whether the "debtor" had "received" what the buyer received on resale and, therefore, whether those receipts were "proceeds" under former Section 9-306(2) [30-9-306(2), now repealed, see 30-9A-315]. This Article [Title 30, chapter 9A] contains no requirement that property be "received" by the debtor for the property to qualify as proceeds. It is necessary only that the property be traceable, directly or indirectly, to the original collateral.

e. **Cash Proceeds and Noncash Proceeds.** The definition of "cash proceeds" is substantially the same as the corresponding definition in former Section 9-306 [30-9-306, now repealed, see 30-9A-315]. The phrase "and the like" covers property that is functionally equivalent to "money, checks, or deposit accounts," such as some money-market accounts that are securities or part of securities entitlements. Proceeds other than cash proceeds are noncash proceeds.

14. **Consignment-Related Definitions: "Consignee"; "Consignment"; "Consignor."** The definition of "consignment" excludes, in subparagraphs (B) and (C) [subsections (1)(t)(ii) and (1)(t)(iii)], transactions for which filing would be inappropriate or of insufficient benefit to justify the costs. A consignment excluded from the application of this Article [Title 30, chapter 9A] by one of those subparagraphs may still be a true consignment; however, it is governed by non-Article 9 [non-Title 30, chapter 9A] law. The definition also excludes, in subparagraph (D) [subsection (1)(t)(iv)], what have been called "consignments intended for security." These "consignments" are not bailments but secured transactions. Accordingly, all of Article 9 [Title 30, chapter 9A] applies to them. See Sections 1-201(b)(35), 9-109(a)(1) [30-1-201(2)(jj), 30-9A-109(1)(a)]. The "consignor" is the person who delivers goods to the "consignee" in a consignment.

The definition of "consignment" requires that the goods be delivered "to a merchant for the purpose of sale." If the goods are delivered for another purpose as well, such as milling or processing, the transaction is a consignment nonetheless because a purpose of the delivery is "sale." On the other hand, if a merchant-processor-bailee will not be selling the goods itself but will be delivering to buyers to which the owner-bailor agreed to sell the goods, the transaction would not be a consignment.

15. **"Accounting."** This definition describes the record and information that a debtor is entitled to request under Section 9-210 [30-9A-210].

16. **"Document."** The definition of "document" incorporates both tangible and electronic documents of title. See Section 1-201(b)(16) and Comment 16 [30-1-201(2)(q) and Comment 16 (comment to subsection (2)(q)].

17. **"Encumbrance"; "Mortgage."** The definitions of "encumbrance" and "mortgage" are unchanged in substance from the corresponding definitions in former Section 9-105 [30-9-105, now repealed, see 30-9A-102]. They are used primarily in the special real-property-related priority and other provisions relating to crops, fixtures, and accessions.

18. **"Fixtures."** This definition is unchanged in substance from the corresponding definition in former Section 9-313 [30-9-313, now repealed, see 30-9A-102]. See Section 9-334 [30-9A-334] (priority of security interests in fixtures and crops).

19. **"Good Faith."** This Article [Title 30, chapter 9A] expands the definition of "good faith" to include "the observance of reasonable commercial standards of fair dealing." The definition in this section applies when the term is used in this Article [Title 30, chapter 9A], and the same concept applies in the context of this Article [Title 30, chapter 9A] for purposes of the obligation of good faith imposed by Section 1-203 [30-1-203]. See subsection (c) [subsection 3].

20. **"Lien Creditor"** This definition is unchanged in substance from the corresponding definition in former Section 9-301 [30-9-301, now repealed, see 30-9A-102].

21. **"New Value."** This Article [Title 30, chapter 9A] deletes former Section 9-108 [30-9-108, now repealed, see 30-9A-102]. Its broad formulation of new value, which embraced the taking of after-acquired collateral for a pre-existing claim, was unnecessary, counterintuitive, and ineffective for its original purpose of sheltering after-acquired collateral from attack as a voidable preference in bankruptcy. The new definition derives from Bankruptcy Code Section 547(a). The term is used with respect to temporary perfection of security interests in instruments, certificated securities, or negotiable documents under Section 9-312(e) [30-9A-312(5)] and with respect to chattel paper priority in Section 9-330 [30-9A-330].

22. **"Person Related To."** Section 9-615 [30-9A-615] provides a special method for calculating a deficiency or surplus when "the secured party, a person related to the secured party, or a secondary obligor" acquires the collateral at a foreclosure disposition. Separate definitions of the term are provided with respect to an individual secured party and with respect to a secured

party that is an organization. The definitions are patterned on the corresponding definition in Section 1.301(32) of the Uniform Consumer Credit Code (1974).

23. **"Proposal."** This definition describes a record that is sufficient to propose to retain collateral in full or partial satisfaction of a secured obligation. See Sections 9-620, 9-621, 9-622 [30-9A-620, 30-9A-621, and 30-9A-622].

24. **"Pursuant to Commitment."** This definition is unchanged in substance from the corresponding definition in former Section 9-105 [30-9-105, now repealed, see 30-9A-102]. It is used in connection with special priority rules applicable to future advances. See Section 9-323 [30-9A-323].

25. **"Software."** The definition of "software" is used in connection with the priority rules applicable to purchase-money security interests. See Sections 9-103, 9-324 [30-9A-103 and 30-9A-324]. Software, like a payment intangible, is a type of general intangible for purposes of this Article [Title 30, chapter 9A].

26. **Terminology: "Assignment" and "Transfer."** In numerous provisions, this Article [Title 30, chapter 9A] refers to the "assignment" or the "transfer" of property interests. These terms and their derivatives are not defined. This Article [Title 30, chapter 9A] generally follows common usage by using the terms "assignment" and "assign" to refer to transfers of rights to payment, claims, and liens and other security interests. It generally uses the term "transfer" to refer to other transfers of interests in property. Except when used in connection with a letter-of-credit transaction (see Section 9-107 [30-9A-107], Comment 4), no significance should be placed on the use of one term or the other. Depending on the context, each term may refer to the assignment or transfer of an outright ownership interest or to the assignment or transfer of a limited interest, such as a security interest.

Compiler's Comments

2013 Amendment: Chapter 75 in definition of authenticate in (ii) substituted "with present intent to adopt or accept a record, to attach to or logically associate with the record an electronic sound, symbol, or process" for "execute or adopt a symbol, or encrypt a record in whole or in part, with present intent to:

(A) identify the authenticating party; and

(B) adopt, accept, or establish the authenticity of a record or term"; in definition of certificate of title inserted last sentence regarding another record maintained as an alternative to a certificate of title; in definition of jurisdiction of organization inserted "formed or"; inserted definition of public organic record; in definition of registered organization in first sentence inserted "formed or" and substituted "by the filing of a public organic record with, the issuance of a public organic record by, or the enactment of legislation by the state or the United States" for "and as to which the state or the United States is required to maintain a public record showing the organization to have been organized", and inserted last sentence regarding a business trust; and made minor changes in style. Amendment effective July 1, 2013.

Saving Clause: Section 26, Ch. 75, L. 2013, provided: "(1) Except as otherwise provided in [sections 19 through 25] [Title 30, chapter 9A, part 8], this chapter applies to a transaction or lien within its scope, even if the transaction or lien was entered into or created before [the effective of this act] [July 1, 2013].

(2) This chapter does not affect an action, case, or proceeding commenced before [the effective date of this act] [July 1, 2013]."

2005 Amendment: Chapter 575 in (2) in list inserted reference to control. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

2001 Amendment: Chapter 179 in definition of chattel paper in (1) near beginning of first sentence after "obligation and a security interest in" substituted "specific goods, a security interest in" for "or a lease of specific goods or of" and at end inserted "a security interest in specific goods and license of software used in the goods, a lease of specific goods, or a lease of specific goods and license of software used in the goods" and inserted second sentence defining monetary obligation, inserted (ii)(A)(II) excluding records that evidence a right to payment out of use of credit card from definition of chattel paper, and in (ii)(B) after "evidenced" substituted "by records that include an instrument" for "both by a security agreement or lease and by an instrument"; in definition of original debtor inserted exception clause; in definition of proceeds inserted exception clause; and made minor changes in style. Amendment effective July 1, 2001.

Administrative Rules

ARM 42.12.205 Requirements when liquor license subject to lien.
ARM 44.5.301 Definitions and requirements for annual report online filing.
ARM 44.6.302 Nonstandard inquiry.

Case Notes

CASES DECIDED AFTER 1999 REVISION

IRS Form 1099-C — Not Discharge of Debt — Creditor Still Able to Collect: The Supreme Court adopted the majority position regarding the purpose of the Form 1099-C and held that the issuance of an IRS Form 1099-C is not prima facie evidence of a creditor's intent to discharge a debt; rather, it is a means of satisfying the agency's reporting requirements and does not, in and of itself, prevent a creditor from seeking collection of a debt. Flathead Bank of Bigfork v. Masonry by Muller, Inc., 2016 MT 269, 385 Mont. 214, 383 P.3d 215.

CASES DECIDED PRIOR TO 1999 REVISION

Parol Evidence Held Inadmissible to Prove Representative Capacity of Maker of Note — Definition of Debtor — Unambiguous Terms Notwithstanding Security Agreement — Statute Not Retroactive — Former Statute Inapplicable: By use of a note and security agreement, Carelli sold 38 elk to Hall who, as Stireses' partner, operated the Elk Valley Game Ranch (Game Ranch). Later, Carelli brought an action against Stireses, alleging that Stireses were also liable on the debt because Hall had orally told Carelli at the time of the sale that the elk were being purchased for the Game Ranch. The Supreme Court held that Hall's oral statements to Carelli were inadmissible on the issue of Stireses' liability on the note for three reasons: (1) The note was clear and unambiguous in that Hall's representative capacity did not appear on the note, Hall was the "debtor" as defined in the security agreement, and a reference to the Game Ranch in the security agreement did not make the note ambiguous so as to require explanation by parol evidence. (2) The Supreme Court held that a 1991 amendment to 30-3-403 regarding the capacity in which a person signs an instrument, if applied in this case, would cause a difference in the liability of the parties. Therefore, the amendment is substantive. Because there was no expression of legislative intent that the 1991 version be applied retroactively, the 1985 version of 30-3-403 and not the 1991 version applies, and parol evidence is not relevant to that 1985 version. (3) The facts of the case did not fall within the terms of the 1985 version of 30-3-403. Carelli v. Hall, 279 M 202, 926 P2d 756, 53 St. Rep. 1116 (1996).

Generally Worded After-Acquired Property Security Interest: Security interest covered all goods used in rental business, including but not limited to machinery, equipment, and inventory held for sale or rent "existing or hereafter acquired". Lower court's conclusion that a general description of items covered was insufficient and that trailers, hoppers, mixer, and loader used by renters to make, haul, and pour cement were not covered was erroneous. Further, the conclusion that there could be no security interest because those items were not financed by the holder of the security interest was also erroneous. Taylor Rental Corp. v. Ted Godwin Leasing, Inc., 209 M 124, 681 P2d 691, 41 St. Rep. 594 (1984).

When Limitation of Remedies Permissible — Equipment Sales — Factors: In a case stemming from an accident involving a hay baler, one issue on appeal was the limitation of remedies. Although limitation of damages for personal injuries in the case of consumer goods is prima facie unconscionable under 30-2-719, farm equipment is defined as "equipment". The limitation of remedy provisions could as a matter of law be found unconscionable. Accordingly, the court ordered an evidentiary hearing on the remedy limitations. Factors under 30-2-302 were to be considered at the hearing. Schlenz v. John Deere Co., 511 F. Supp. 224, 38 St. Rep. 579 (D.C. Mont. 1981).

30-9A-103. Purchase-money security interest — application of payments — burden of establishing purchase-money security interest.

Official Comments

1. **Source.** Former Section 9-107 [30-9-107, now repealed].
2. **Scope of This Section.** Under Section 9-309(1) [30-9A-309(1)], a purchase-money security interest in consumer goods is perfected when it attaches. Sections 9-317 and 9-324

[30-9A-317 and 30-9A-324] provide special priority rules for purchase-money security interests in a variety of contexts. This section explains when a security interest enjoys purchase-money status.

3. **"Purchase-Money Collateral"; "Purchase-Money Obligation"; "Purchase-Money Security Interest."** Subsection (a) [subsection (1)] defines "purchase-money collateral" and "purchase-money obligation." These terms are essential to the description of what constitutes a purchase-money security interest under subsection (b) [subsection (2)]. As used in subsection (a)(2) [subsection (1)(b)], the definition of "purchase-money obligation," the "price" of collateral or the "value given to enable" includes obligations for expenses incurred in connection with acquiring rights in the collateral, sales taxes, duties, finance charges, interest, freight charges, costs of storage in transit, demurrage, administrative charges, expenses of collection and enforcement, attorney's fees, and other similar obligations.

The concept of "purchase-money security interest" requires a close nexus between the acquisition of collateral and the secured obligation. Thus, a security interest does not qualify as a purchase-money security interest if a debtor acquires property on unsecured credit and subsequently creates the security interest to secure the purchase price.

4. **Cross-Collateralization of Purchase-Money Security Interests in Inventory.** Subsection (b)(2) [subsection (2)(b)] deals with the problem of cross-collateralized purchase-money security interests in inventory. Consider a simple example:

Example: Seller (S) sells an item of inventory (Item-1) to Debtor (D), retaining a security interest in Item-1 to secure Item-1's price and all other obligations, existing and future, of D to S. S then sells another item of inventory to D (Item-2), again retaining a security interest in Item-2 to secure Item-2's price as well as all other obligations of D to S. D then pays to S Item-1's price. D then sells Item-2 to a buyer in ordinary course of business, who takes Item-2 free of S's security interest. Under subsection (b)(2) [subsection (2)(b)], S's security interest in Item-1 securing Item-2's unpaid price would be a purchase-money security interest. This is so because S has a purchase-money security interest in Item-1, Item-1 secures the price of (a "purchase-money obligation incurred with respect to") Item-2 ("other inventory"), and Item-2 itself was subject to a purchase-money security interest. Note that, to the extent Item-1 secures the price of Item-2, S's security interest in Item-1 would not be a purchase-money security interest under subsection (b)(1) [subsection (2)(a)]. The security interest in Item-1 is a purchase-money security interest under subsection (b)(1) [subsection (2)(a)] only to the extent that Item-1 is "purchase-money collateral," i.e., only to the extent that Item-1 "secures a purchase-money obligation incurred with respect to that collateral" (i.e., Item-1). See subsection (a)(1) [subsection (1)(a)].

5. **Purchase-Money Security Interests in Goods and Software.** Subsections (b) and (c) [subsections (2) and (3)] limit purchase-money security interests to security interests in goods, including fixtures, and software. Otherwise, no change in meaning from former Section 9-107 [30-9-107, now repealed] is intended. The second sentence of former Section 9-115(5)(f) [30-9-115(5)(f), now repealed, see 30-9A-328] made the purchase-money priority rule (former Section 9-312(4) [30-9-312(4), now repealed, see 30-9A-324]) inapplicable to investment property. This section's limitation makes that provision unnecessary.

Subsection (c) [subsection (3)] describes the limited circumstances under which a security interest in goods may be accompanied by a purchase-money security interest in software. The software must be acquired by the debtor in a transaction integrated with the transaction in which the debtor acquired the goods, and the debtor must acquire the software for the principal purpose of using the software in the goods. "Software" is defined in Section 9-102 [30-9A-102].

6. **Consignments.** Under former Section 9-114 [30-9-114, now repealed], the priority of the consignor's interest is similar to that of a purchase-money security interest. Subsection (d) [subsection (4)] achieves this result more directly, by defining the interest of a "consignor," defined in Section 9-102 [30-9A-102], to be a purchase-money security interest in inventory for purposes of this Article [Title 30, chapter 9A]. This drafting convention obviates any need to set forth special priority rules applicable to the interest of a consignor. Rather, the priority of the consignor's interest as against the rights of lien creditors of the consignee, competing secured parties, and purchasers of the goods from the consignee can be determined by reference to the priority rules generally applicable to inventory, such as Sections 9-317, 9-320, 9-322, and 9-324 [30-9A-317, 30-9A-320, 30-9A-322, and 30-9A-324]. For other purposes, including the rights and duties of the consignor and consignee as between themselves, the consignor would remain the owner of goods under a bailment arrangement with the consignee. See Section 9-319 [30-9A-319).

7. **Provisions Applicable Only to Non-Consumer-Goods Transactions.**

a. **"Dual-Status" Rule.** For transactions other than consumer-goods transactions, this Article [Title 30, chapter 9A] approves what some cases have called the "dual-status" rule, under which a security interest may be a purchase-money security interest to some extent and a non-purchase-money security interest to some extent. (Concerning consumer-goods transactions, see subsection (h) [subsection (8)] and Comment 8.) Some courts have found this rule to be explicit or implicit in the words "to the extent," found in former Section 9-107 [30-9-107, now repealed] and continued in subsections (b)(1) and (b)(2) [subsections (2)(a) and (2)(b)]. The rule is made explicit in subsection (e) [subsection (5)]. For non-consumer-goods transactions, this Article [Title 30, chapter 9A] rejects the "transformation" rule adopted by some cases, under which any cross-collateralization, refinancing, or the like destroys the purchase-money status entirely.

Consider, for example, what happens when a $10,000 loan secured by a purchase-money security interest is refinanced by the original lender, and, as part of the transaction, the debtor borrows an additional $2,000 secured by the collateral. Subsection (f) [subsection (6)] resolves any doubt that the security interest remains a purchase-money security interest. Under subsection (b) [subsection (2)], however, it enjoys purchase-money status only to the extent of $10,000.

b. **Allocation of Payments.** Continuing with the example, if the debtor makes a $1,000 payment on the $12,000 obligation, then one must determine the extent to which the security interest remains a purchase-money security interest-$9,000 or $10,000. Subsection (e)(1) [subsection (5)(a)] expresses the overriding principle, applicable in cases other than consumer-goods transactions, for determining the extent to which a security interest is a purchase-money security interest under these circumstances: freedom of contract, as limited by principle of reasonableness. An unconscionable method of application, for example, is not a reasonable one and so would not be given effect under subsection (e)(1) [subsection (5)(a)]. In the absence of agreement, subsection (e)(2) [subsection (5)(b)] permits the obligor to determine how payments should be allocated. If the obligor fails to manifest its intention, obligations that are not secured will be paid first. (As used in this Article [Title 30, chapter 9A], the concept of "obligations that are not secured" means obligations for which the debtor has not created a security interest. This concept is different from and should not be confused with the concept of an "unsecured claim" as it appears in Bankruptcy Code Section 506(a).) The obligor may prefer this approach, because unsecured debt is likely to carry a higher interest rate than secured debt. A creditor who would prefer to be secured rather than unsecured also would prefer this approach.

After the unsecured debt is paid, payments are to be applied first toward the obligations secured by purchase-money security interests. In the event that there is more than one such obligation, payments first received are to be applied to obligations first incurred. See subsection (e)(3) [subsection (5)(c)]. Once these obligations are paid, there are no purchase-money security interests and no additional allocation rules are needed.

Subsection (f) [subsection (6)] buttresses the dual-status rule by making it clear that (in a transaction other than a consumer-goods transaction) cross-collateralization and renewals, refinancings, and restructurings do not cause a purchase-money security interest to lose its status as such. The statutory terms "renewed," "refinanced," and "restructured" are not defined. Whether the terms encompass a particular transaction depends upon whether, under the particular facts, the purchase-money character of the security interest fairly can be said to survive. Each term contemplates that an identifiable portion of the purchase-money obligation could be traced to the new obligation resulting from a renewal, refinancing, or restructuring.

c. **Burden of Proof.** As is the case when the extent of a security interest is in issue, under subsection (g) [subsection (7)] the secured party claiming a purchase-money security interest in a transaction other than a consumer-goods transaction has the burden of establishing whether the security interest retains its purchase-money status. This is so whether the determination is to be made following a renewal, refinancing, or restructuring or otherwise.

8. **Consumer-Goods Transactions; Characterization Under Other Law.** Under subsection (h) [subsection (8)], the limitation of subsections (e), (f), and (g) [subsections (5), (6), and (7)] to transactions other than consumer-goods transactions leaves to the court the determination of the proper rules in consumer-goods transactions. Subsection (h) [subsection (8)] also instructs the court not to draw any inference from this limitation as to the proper rules for consumer-goods transactions and leaves the court free to continue to apply established approaches to those transactions.

This section addresses only whether a security interest is a "purchase-money security interest" under this Article [Title 30, chapter 9A], primarily for purposes of perfection and priority. See, e.g., Sections 9-317, 9-324 [30-9A-317 and 30-9A-324]. In particular, its adoption of the dual-status rule, allocation of payments rules, and burden of proof standards for non-consumer-goods transactions is not intended to affect or influence characterizations under other statutes. Whether a security interest is a "purchase-money security interest" under other law is determined by that law. For example, decisions under Bankruptcy Code Section 522(f) have applied both the dual-status and the transformation rules. The Bankruptcy Code does not expressly adopt the state law definition of "purchase-money security interest." Where federal law does not defer to this Article [Title 30, chapter 9A], this Article [Title 30, chapter 9A] does not, and could not, determine a question of federal law.

Case Notes

CASES DECIDED PRIOR TO 1999 REVISION

Good Faith Filing — Effective Against Persons With Knowledge: In a case decided before the 1985 amendments to 30-9-401 (now repealed, see 30-9A-501), a bank that filed its security agreement in livestock in the wrong county did not have a perfected security interest in the livestock but did take precedence over another secured party because the filing was made in good faith and the other secured party had actual knowledge of the security interest. First Nat'l Bank of Glasgow v. First Sec. Bank of Mont., 222 M 118, 721 P2d 1270, 43 St. Rep. 1105 (1986).

30-9A-104. Control of deposit account.

Official Comments

1. **Source.** New; derived from Section 8-106 [30-8-116].

2. **Why "Control" Matters.** This section explains the concept of "control" of a deposit account. "Control" under this section may serve two functions. First, "control . . . pursuant to the debtor's agreement" may substitute for an authenticated security agreement as an element of attachment. See Section 9-203(b)(3)(D) [30-9A-203(2)(c)(iv)]. Second, when a deposit account is taken as original collateral, the only method of perfection is obtaining control under this section. See Section 9-312(b)(1) [30-9A-312(2)(a)].

3. **Requirements for "Control."** This section derives from Section 8-106 [30-8-116] of Revised Article 8 [Title 30, chapter 8], which defines "control" of securities and certain other investment property. Under subsection (a)(1) [subsection (1)(a)], the bank with which the deposit account is maintained has control. The effect of this provision is to afford the bank automatic perfection. No other form of public notice is necessary; all actual and potential creditors of the debtor are always on notice that the bank with which the debtor's deposit account is maintained may assert a claim against the deposit account.

Example: D maintains a deposit account with Bank A. To secure a loan from Banks X, Y, and Z, D creates a security interest in the deposit account in favor of Bank A, as agent for Banks X, Y, and Z. Because Bank A is a "secured party" as defined in Section 9-102 [30-9A-102], the security interest is perfected by control under subsection (a)(1) [subsection (1)(b)].

Under subsection (a)(2) [subsection (1)(b)], a secured party may obtain control by obtaining the bank's authenticated agreement that it will comply with the secured party's instructions without further consent by the debtor. The analogous provision in Section 8-106 [30-8-116] does not require that the agreement be authenticated. An agreement to comply with the secured party's instructions suffices for "control" of a deposit account under this section even if the bank's agreement is subject to specified conditions, e.g., that the secured party's instructions are accompanied by a certification that the debtor is in default. (Of course, if the condition is the debtor's further consent, the statute explicitly provides that the agreement would not confer control.) See revised Section 8-106 [30-8-116], Comment 7.

Under subsection (a)(3) [subsection (1)(c)], a secured party may obtain control by becoming the bank's "customer," as defined in Section 4-104 [30-4-104]. As the customer, the secured party would enjoy the right (but not necessarily the exclusive right) to withdraw funds from, or close, the deposit account. See Sections 4-401(a), 4-403(a) [30-4-401(1), 30-4-403(1)].

As is the case with possession under Section 9-313 [30-9A-313], in determining whether a particular person has control under subsection (a) [subsection (1)], the principles of agency apply. See Section 1-103 [30-1-103] and Restatement (3d), Agency § 8.12, Comment b.

Although the arrangements giving rise to control may themselves prevent, or may enable the secured party at its discretion to prevent, the debtor from reaching the funds on deposit, subsection (b) [subsection (2)] makes clear that the debtor's ability to reach the funds is not inconsistent with "control."

Perfection by control is not available for bank accounts evidenced by an instrument (e.g., certain certificates of deposit), which by definition are "instruments" and not "deposit accounts." See Section 9-102 [30-9A-102] (defining "deposit account" and "instrument").

Compiler's Comments

2001 Amendment: Chapter 179 near end of (1)(b) substituted "deposit account" for "account". Amendment effective July 1, 2001.

30-9A-105. Control of electronic chattel paper.

Official Comments

1. **Source.** New.

2. **"Control" of Electronic Chattel Paper.** This Article [Title 30, chapter 9A] covers security interests in "electronic chattel paper," a new term defined in Section 9-102 [30-9A-102]. This section governs how "control" of electronic chattel paper may be obtained. Subsection (a) [subsection (1)], which derives from Section 16 of the Uniform Electronic Transactions Act, sets forth the general test for control. Subsection (b) [subsection (2)] sets forth a safe harbor test that, if satisfied, establishes control under the general test in subsection (a) [subsection (1)].

A secured party's control of electronic chattel paper (i) may substitute for an authenticated security agreement for purposes of attachment under Section 9-203 [30-9A-203], (ii) is a method of perfection under Section 9-314 [30-9A-314], and (iii) is a condition for obtaining special, non-temporal priority under Section 9-330 [30-9A-330]. Because electronic chattel paper cannot be transferred, assigned, or possessed in the same manner as tangible chattel paper, a special definition of control is necessary. In descriptive terms, this section provides that control of electronic chattel paper is the functional equivalent of possession of "tangible chattel paper" (a term also defined in Section 9-102 [30-9A-102]).

3. **Development of Control Systems.** This Article [Title 30, chapter 9A] leaves to the marketplace the development of systems and procedures, through a combination of suitable technologies and business practices, for dealing with control of electronic chattel paper in a commercial context. Systems that evolve for control of electronic chattel paper may or may not involve a third party custodian of the relevant records. As under UETA, a system must be shown to reliably establish that the secured party is the assignee of the chattel paper. Reliability is a high standard and encompasses the general principles of uniqueness, identifiability, and unalterability found in subsection (b) [subsection (2)] without setting forth specific guidelines as to how these principles must be achieved. However, the standards applied to determine whether a party is in control of electronic chattel paper should not be more stringent than the standards now applied to determine whether a party is in possession of tangible chattel paper. For example, just as a secured party does not lose possession of tangible chattel paper merely by virtue of the possibility that a person acting on its behalf could wrongfully redeliver the chattel paper to the debtor, so control of electronic chattel paper would not be defeated by the possibility that the secured party's interest could be subverted by the wrongful conduct of a person (such as a custodian) acting on its behalf.

This section and the concept of control of electronic chattel paper are not based on the same concepts as are control of deposit accounts (Section 9-104 [30-9A-104]), security entitlements, a type of investment property (Section 9-106 [30-9A-106]), and letter-of-credit rights (Section 9-107 [30-9A-107]). The rules for control of those types of collateral are based on existing market practices and legal and regulatory regimes for institutions such as banks and securities intermediaries. Analogous practices for electronic chattel paper are developing nonetheless. The flexible approach adopted by this section, moreover, should not impede the development of these practices and, eventually, legal and regulatory regimes, which may become analogous to those for, e.g., investment property.

4. **"Authoritative Copy" of Electronic Chattel Paper.** One requirement for establishing control under subsection (b) [subsection (1)] is that a particular copy be an "authoritative copy. " Although other copies may exist, they must be distinguished from the authoritative copy. This may be achieved, for example, through the methods of authentication that are used or by business practices involving the marking of any additional copies. When tangible chattel paper is converted to electronic chattel paper, in order to establish that a copy of the electronic chattel paper is the authoritative copy it may be necessary to show that the tangible chattel paper no longer exists or has been permanently marked to indicate that it is not the authoritative copy.

Compiler's Comments

2013 Amendment: Chapter 75 in (1) after "electronic chattel paper if" inserted provision regarding a system for evidencing a transfer of interests; in (2) inserted "A system satisfies subsection (1) if"; in (2)(d) and (2)(f) substituted reference to amendment for reference to revision; in (2)(f) after "unauthorized" deleted "revision"; and made minor changes in style. Amendment effective July 1, 2013.

Saving Clause: Section 26, Ch. 75, L. 2013, provided: "(1) Except as otherwise provided in [sections 19 through 25] [Title 30, chapter 9A, part 8], this chapter applies to a transaction or lien within its scope, even if the transaction or lien was entered into or created before [the effective of this act] [July 1, 2013].

(2) This chapter does not affect an action, case, or proceeding commenced before [the effective date of this act] [July 1, 2013]."

30-9A-106. Control of investment property.

Official Comments

1. **Source.** Former Section 9-115(e) [30-9-115(1)(e), now repealed, see 30-9A-106].

2. **"Control" Under Article 8 [Title 30, chapter 8].** For an explanation of "control" of securities and certain other investment property, see Section 8-106 [30-8-116], Comments 4 and 7.

3. **"Control" of Commodity Contracts.** This section, as did former Section 9-115(1)(e) [30-9-115(1)(e), now repealed, see 30-9A-106], contains provisions relating to control of commodity contracts which are analogous to those in Section 8-106 [30-8-116] for other types of investment property.

4. **Securities Accounts and Commodity Accounts.** For drafting convenience, control with respect to a securities account or commodity account is defined in terms of obtaining control over the security entitlements or commodity contracts. Of course, an agreement that provides that (without further consent of the debtor) the securities intermediary or commodity intermediary will honor instructions from the secured party concerning a securities account or commodity account described as such is sufficient. Such an agreement necessarily implies that the intermediary will honor instructions concerning all security entitlements or commodity contracts carried in the account and thus affords the secured party control of all the security entitlements or commodity contracts.

30-9A-107. Control of letter-of-credit right.

Official Comments

1. **Source.** New.

2. **"Control" of Letter-of-Credit Right.** Whether a secured party has control of a letter-of-credit right may determine the secured party's priority as against competing secured parties. See Section 9-329 [30-9A-329]. This section provides that a secured party acquires control of a letter-of-credit right by receiving an assignment if the secured party obtains the consent of the issuer or any nominated person, such as a confirmer or negotiating bank, under Section 5-114 [30-5-134] or other applicable law or practice. Because both issuers and nominated persons may give or be obligated to give value under a letter of credit, this section contemplates that a secured party obtains control of a letter-of-credit right with respect to the issuer or a particular nominated person only to the extent that the issuer or that nominated person consents to the assignment. For example, if a secured party obtains control to the extent of an issuer's obligation but fails to obtain the consent of a nominated person, the secured party does not have control to the extent that the nominated person gives value. In many cases the person or persons who will give value under a letter of credit will be clear from its terms. In other cases, prudence may suggest obtaining consent from more than one person. The details of the consenting issuer's or nominated person's duties to pay or otherwise render performance to the secured party are left to the agreement of the parties.

3. **"Proceeds of a Letter of Credit."** Section 5-114 [30-5-134] follows traditional banking terminology by referring to a letter of credit beneficiary's assignment of its right to receive payment thereunder as an assignment of the "proceeds of a letter of credit." However, as the seller of goods can assign its right to receive payment (an "account") before it has been earned by delivering the goods to the buyer, so the beneficiary of a letter of credit can assign its contingent right to payment before the letter of credit has been honored. See Section 5-114(b) [30-5-134(2)]. If the assignment creates a security interest, the security interest can be perfected at the time it is created. An assignment of, including the creation of a security interest in, a letter-of-credit right is an assignment of a present interest.

4. **"Transfer" vs. "Assignment."** Letter-of-credit law and practice distinguish the "transfer" of a letter of credit from an "assignment." Under a transfer, the transferee itself becomes the beneficiary and acquires the right to draw. Whether a new, substitute credit is issued or the

issuer advises the transferee of its status as such, the transfer constitutes a novation under which the transferee is the new, substituted beneficiary (but only to the extent of the transfer, in the case of a partial transfer).

Section 5-114(e) [30-5-134(5)] provides that the rights of a transferee beneficiary or nominated person are independent of the beneficiary's assignment of the proceeds of a letter of credit and are superior to the assignee's right to the proceeds. For this reason, transfer does not appear in this Article [Title 30, chapter 9A] as a means of control or perfection. Section 9-109(c)(4) [30-9A-109(3)(d)] recognizes the independent and superior rights of a transferee beneficiary under Section 5-114(e) [30-5-134(5)]; this Article [Title 30, chapter 9A] does not apply to the rights of a transferee beneficiary or nominated person to the extent that those rights are independent and superior under Section 5-114 [30-5-134].

5. **Supporting Obligation: Automatic Attachment and Perfection.** A letter-of-credit right is a type of "supporting obligation," as defined in Section 9-102 [30-9A-102]. Under Sections 9-203 and 9-308 [30-9A-203 and 30-9A-308], a security interest in a letter-of-credit right automatically attaches and is automatically perfected if the security interest in the supported obligation is a perfected security interest. However, unless the secured party has control of the letter-of-credit right or itself becomes a transferee beneficiary, it cannot obtain any rights against the issuer or a nominated person under Article 5 [Title 30, chapter 5]. Consequently, as a practical matter, the secured party's rights would be limited to its ability to locate and identify proceeds distributed by the issuer or nominated person under the letter of credit.

30-9A-108. Sufficiency of description.

Official Comments

1. **Source.** Former Sections 9-110, 9-115(3) [30-9-110, 30-9-115(3), both now repealed].

2. **General Rules.** Subsection (a) [subsection (1)] retains substantially the same formulation as former Section 9-110 [30-9-110, now repealed]. Subsection (b) [subsection (2)] expands upon subsection (a) [subsection (1)] by indicating a variety of ways in which a description might reasonably identify collateral. Whereas a provision similar to subsection (b) [subsection (2)] was applicable only to investment property under former Section 9-115(3) [30-9-115(3), now repealed], subsection (b) [subsection (2)] applies to all types of collateral, subject to the limitation in subsection (d) [subsection (4)]. Subsection (b) [subsection (2)] is subject to subsection (c) [subsection (3)], which follows prevailing case law and adopts the view that an "all assets" or "all personal property" description for purposes of a security agreement is not sufficient. Note, however, that under Section 9-504 [30-9A-504], a financing statement sufficiently indicates the collateral if it "covers all assets or all personal property."

The purpose of requiring a description of collateral in a security agreement under Section 9-203 [30-9A-203] is evidentiary. The test of sufficiency of a description under this section, as under former Section 9-110 [30-9-110, now repealed], is that the description do the job assigned to it: make possible the identification of the collateral described. This section rejects any requirement that a description is insufficient unless it is exact and detailed (the so-called "serial number" test).

3. **After-Acquired Collateral.** Much litigation has arisen over whether a description in a security agreement is sufficient to include after-acquired collateral if the agreement does not explicitly so provide. This question is one of contract interpretation and is not susceptible to a statutory rule (other than a rule to the effect that it is a question of contract interpretation). Accordingly, this section contains no reference to descriptions of after-acquired collateral.

4. **Investment Property.** Under subsection (d) [subsection (4)], the use of the wrong Article 8 [Title 30, chapter 8] terminology does not render a description invalid (e.g., a security agreement intended to cover a debtor's "security entitlements" is sufficient if it refers to the debtor's "securities"). Note also that given the broad definition of "securities account" in Section 8-501 [30-8-501], a security interest in a securities account also includes all other rights of the debtor against the securities intermediary arising out of the securities account. For example, a security interest in a securities account would include credit balances due to the debtor from the securities intermediary, whether or not they are proceeds of a security entitlement. Moreover, describing collateral as a securities account is a simple way of describing all of the security entitlements carried in the account.

5. **Consumer Investment Property; Commercial Tort Claims.** Subsection (e) [subsection (5)] requires greater specificity of description in order to prevent debtors from inadvertently encumbering certain property. Subsection (e) [subsection (5)] requires that a description by defined "type" of collateral alone of a commercial tort claim or, in a consumer transaction, of a

security entitlement, securities account, or commodity account, is not sufficient. For example, "all existing and after-acquired investment property" or "all existing and after-acquired security entitlements," without more, would be insufficient in a consumer transaction to describe a security entitlement, securities account, or commodity account. The reference to "only by type" in subsection (e) [subsection (5)] means that a description is sufficient if it satisfies subsection (a) [subsection (1)] and contains a descriptive component beyond the "type" alone. Moreover, if the collateral consists of a securities account or commodity account, a description of the account is sufficient to cover all existing and future security entitlements or commodity contracts carried in the account. See Section 9-203(h), (i) [30-9A-203(8) and (9)].

Under Section 9-204 [30-9A-204], an after-acquired collateral clause in a security agreement will not reach future commercial tort claims. It follows that when an effective security agreement covering a commercial tort claim is entered into the claim already will exist. Subsection (e) [subsection (5)] does not require a description to be specific. For example, a description such as "all tort claims arising out of the explosion of debtor's factory" would suffice, even if the exact amount of the claim, the theory on which it may be based, and the identity of the tortfeasor(s) are not described. (Indeed, those facts may not be known at the time.)

Case Notes

CASES DECIDED PRIOR TO 1999 REVISION

Statement of Location in Security Agreement — Limiting Factor: A security agreement in livestock and their progeny which contained an after-acquired property clause and which described the livestock as being located "20 miles East of Jordan on premises owned by: James J. Murnion" is limited to livestock located on the described premises. This security agreement did not give the secured party a prior perfected security interest in the debtor's cattle that were purchased with a later loan from another bank and pastured in another location. First Nat'l Bank of Glasgow v. First Sec. Bank of Mont., 222 M 118, 721 P2d 1270, 43 St. Rep. 1105 (1986).

Generally Worded After-Acquired Property Security Interest: Security interest covered all goods used in rental business, including but not limited to machinery, equipment, and inventory held for sale or rent "existing or hereafter acquired". Lower court's conclusion that a general description of items covered was insufficient and that trailers, hoppers, mixer, and loader used by renters to make, haul, and pour cement were not covered was erroneous. Further, the conclusion that there could be no security interest because those items were not financed by the holder of the security interest was also erroneous. Taylor Rental Corp. v. Ted Godwin Leasing, Inc., 209 M 124, 681 P2d 691, 41 St. Rep. 594 (1984).

30-9A-109. Scope.

Official Comments

1. **Source.** Former Sections 9-102, 9-104 [30-9-102, 30-9-104, both now repealed].

2. **Basic Scope Provision.** Subsection (a)(1) [subsection (1)(a)] derives from former Section 9-102(1) and (2) [30-9-102(1) and (2), now repealed]. These subsections have been combined and shortened. No change in meaning is intended. Under subsection (a)(1) [subsection (1)(a)], all consensual security interests in personal property and fixtures are covered by this Article [Title 30, chapter 9A], except for transactions excluded by subsections (c) and (d) [subsections (3) and (4)]. As to which transactions give rise to a "security interest," the definition of that term in Section 1-201 [30-1-201] must be consulted. When a security interest is created, this Article [Title 30, chapter 9A] applies regardless of the form of the transaction or the name that parties have given to it. Likewise, the subjective intention of the parties with respect to the legal characterization of their transaction is irrelevant to whether this Article applies, as it was to the application of former Article 9 [Title 30, chapter 9, now repealed] under the proper interpretation of former Section 9-102 [30-9-102, now repealed].

3. **Agricultural Liens.** Subsection (a)(2) [subsection (1)(b)] is new. It expands the scope of this Article [Title 30, chapter 9A] to cover agricultural liens, as defined in Section 9-102 [30-9A-102].

4. **Sales of Accounts, Chattel Paper, Payment Intangibles, Promissory Notes, and Other Receivables.** Under subsection (a)(3) [subsection (1)(c)], as under former Section 9-102 [30-9-102, now repealed], this Article [Title 30, chapter 9A] applies to sales of accounts and chattel paper. This approach generally has been successful in avoiding difficult problems of distinguishing between transactions in which a receivable secures an obligation and those in which the receivable has been sold outright. In many commercial financing transactions the distinction is blurred.

Subsection (a)(3) [subsection (1)(c)] expands the scope of this Article [Title 30, chapter 9A] by including the sale of a "payment intangible" (defined in Section 9-102 [30-9A-102] as "a general intangible under which the account debtor's principal obligation is a monetary obligation") and a "promissory note" (also defined in Section 9-102 [30-9A-102]). To a considerable extent, this Article [Title 30, chapter 9A] affords these transactions treatment identical to that given sales of accounts and chattel paper. In some respects, however, sales of payment intangibles and promissory notes are treated differently from sales of other receivables. See, e.g., Sections 9-309 [30-9A-309] (automatic perfection upon attachment), 9-408 [30-9A-408] (effect of restrictions on assignment). By virtue of the expanded definition of "account" (defined in Section 9-102 [30-9A-102]), this Article [Title 30, chapter 9A] now covers sales of (and other security interests in) "health-care-insurance receivables" (also defined in Section 9-102 [30-9A-102]). Although this Article [Title 30, chapter 9A] occasionally distinguishes between outright sales of receivables and sales that secure an obligation, neither this Article [Title 30, chapter 9A] nor the definition of "security interest" (Section 1-201(37) [30-1-201(37)]) delineates how a particular transaction is to be classified. That issue is left to the courts.

5. **Transfer of Ownership in Sales of Receivables.** A "sale" of an account, chattel paper, a promissory note, or a payment intangible includes a sale of a right in the receivable, such as a sale of a participation interest. The term also includes the sale of an enforcement right. For example, a "[p]erson entitled to enforce" a negotiable promissory note (Section 3-301 [30-3-301]) may sell its ownership rights in the instrument. See Section 3-203 [30-3-203], Comment 1 ("Ownership rights in instruments may be determined by principles of the law of property, independent of Article 3 [Title 30, chapter 3], which do not depend upon whether the instrument was transferred under Section 3-203 [30-3-203]."). Also, the right under Section 3-309 [30-3-309] to enforce a lost, destroyed, or stolen negotiable promissory note may be sold to a purchaser who could enforce that right by causing the seller to provide the proof required under that section. This Article [Title 30, chapter 9A] rejects decisions reaching a contrary result, e.g., Dennis Joslin Co. v. Robinson Broadcasting, 977 F. Supp. 491 (D.D.C. 1997).

Nothing in this section or any other provision of Article 9 [Title 30, chapter 9A] prevents the transfer of full and complete ownership of an account, chattel paper, an instrument, or a payment intangible in a transaction of sale. However, as mentioned in Comment 4, neither this Article [Title 30, chapter 9A] nor the definition of "security interest" in Section 1-201 [30-1-201] provides rules for distinguishing sales transactions from those that create a security interest securing an obligation. This Article [Title 30, chapter 9A] applies to both types of transactions. The principal effect of this coverage is to apply this Article's [Title 30, chapter 9A] perfection and priority rules to these sales transactions. Use of terminology such as "security interest," "debtor," and "collateral" is merely a drafting convention adopted to reach this end, and its use has no relevance to distinguishing sales from other transactions. See PEB Commentary No. 14.

Following a debtor's outright sale and transfer of ownership of a receivable, the debtor-seller retains no legal or equitable rights in the receivable that has been sold. See Section 9-318(a) [30-9A-318(1)]. This is so whether or not the buyer's security interest is perfected. (A security interest arising from the sale of a promissory note or payment intangible is perfected upon attachment without further action. See Section 9-309 [30-9A-309].) However, if the buyer's interest in accounts or chattel paper is unperfected, a subsequent lien creditor, perfected secured party, or qualified buyer can reach the sold receivable and achieve priority over (or take free of) the buyer's unperfected security interest under Section 9-317 [30-9A-317]. This is so not because the seller of a receivable retains rights in the property sold; it does not. Nor is this so because the seller of a receivable is a "debtor" and the buyer of a receivable is a "secured party" under this Article [Title 30, chapter 9A] (they are). It is so for the simple reason that Sections 9-318(b), 9-317, and 9-322 [30-9A-318(2), 30-9A-317, and 30-9A-322] make it so, as did former Sections 9-301 and 9-312 [30-9-301 and 30-9-312, both now repealed, see 30-9A-317, 30-9A-322, 30-9A-323, and 30-9A-324]. Because the buyer's security interest is unperfected, for purposes of determining the rights of creditors of and purchasers for value from the debtor-seller, under Section 9-318(b) [30-9A-318(2)] the debtor-seller is deemed to have the rights and title it sold. Section 9-317 [30-9A-317] subjects the buyer's unperfected interest in accounts and chattel paper to that of the debtor-seller's lien creditor and other persons who qualify under that section.

6. **Consignments.** Subsection (a)(4) [subsection (1)(d)] is new. This Article [Title 30, chapter 9A] applies to every "consignment." The term, defined in Section 9-102 [30-9A-102], includes many but not all "true" consignments (i.e., bailments for the purpose of sale). If a transaction is a "sale or return," as defined in revised Section 2-326 [30-2-326], it is not a "consignment." In a "sale or return" transaction, the buyer becomes the owner of the goods, and the seller may obtain

an enforceable security interest in the goods only by satisfying the requirements of Section 9-203 [30-9A-203].

Under common law, creditors of a bailee were unable to reach the interest of the bailor (in the case of a consignment, the consignor-owner). Like former Section 2-326 [30-2-326] and former Article 9 [Title 30, chapter 9, now repealed], this Article [Title 30, chapter 9A] changes the common-law result; however, it does so in a different manner. For purposes of determining the rights and interests of third-party creditors of, and purchasers of the goods from, the consignee, but not for other purposes, such as remedies of the consignor, the consignee is deemed to acquire under this Article [Title 30, chapter 9A] whatever rights and title the consignor had or had power to transfer. See Section 9-319 [30-9A-319]. The interest of a consignor is defined to be a security interest under revised Section 1-201(37) [30-1-201(37)], more specifically, a purchase-money security interest in the consignee's inventory. See Section 9-103(d) [30-9A-103(4)]. Thus, the rules pertaining to lien creditors, buyers, and attachment, perfection, and priority of competing security interests apply to consigned goods. The relationship between the consignor and consignee is left to other law. Consignors also have no duties under Part 6 [Title 30, chapter 9A, part 6]. See Section 9-601(g) [30-9A-601(7)].

Sometimes parties characterize transactions that secure an obligation (other than the bailee's obligation to returned bailed goods) as "consignments." These transactions are not "consignments" as contemplated by Section 9-109(a)(4) [30-9A-109(1)(d)]. See Section 9-102 [30-9A-102]. This Article [Title 30, chapter 9A] applies also to these transactions, by virtue of Section 9-109(a)(1) [30-9A-109(1)(a)]. They create a security interest within the meaning of the first sentence of Section 1-201(37) [30-1-201(37)].

This Article [Title 30, chapter 9A] does not apply to bailments for sale that fall outside the definition of "consignment" in Section 9-102 [30-9A-102] and that do not create a security interest that secures an obligation.

7. **Security Interest in Obligation Secured by Non-Article 9 [non-Title 30, chapter 9A] Transaction.** Subsection (b) [subsection (2)] is unchanged in substance from former Section 9-102(3) [30-9-102(3), now repealed]. The following example provides an illustration.

Example 1: O borrows $10,000 from M and secures its repayment obligation, evidenced by a promissory note, by granting to M a mortgage on O's land. This Article [Title 30, chapter 9A] does not apply to the creation of the real-property mortgage. However, if M sells the promissory note to X or gives a security interest in the note to secure M's own obligation to X, this Article [Title 30, chapter 9A] applies to the security interest thereby created in favor of X. The security interest in the promissory note is covered by this Article [Title 30, chapter 9A] even though the note is secured by a real-property mortgage. Also, X's security interest in the note gives X an attached security interest in the mortgage lien that secures the note and, if the security interest in the note is perfected, the security interest in the mortgage lien likewise is perfected. See Sections 9-203, 9-308 [30-9A-203 and 30-9A-308]. It also follows from subsection (b) [subsection (2)] that an attempt to obtain or perfect a security interest in a secured obligation by complying with non-Article 9 [non-Title 30, chapter 9A] law, as by an assignment of record of a real-property mortgage, would be ineffective. Finally, it is implicit from subsection (b) [subsection (2)] that one cannot obtain a security interest in a lien, such as a mortgage on real property, that is not also coupled with an equally effective security interest in the secured obligation. This Article [Title 30, chapter 9A] rejects cases such as In re Maryville Savings & Loan Corp., 743 F.2d 413 (6th Cir. 1984), clarified on reconsideration, 760 F.2d 119 (1985).

8. **Federal Preemption.** Former Section 9-104(a) [30-9-104(1), now repealed] excluded from Article 9 [Title 30, chapter 9, now repealed] "a security interest subject to any statute of the United States, to the extent that such statute governs the rights of parties to and third parties affected by transactions in particular types of property." Some (erroneously) read the former section to suggest that Article 9 [Title 30, chapter 9, now repealed] sometimes deferred to federal law even when federal law did not preempt Article 9 [Title 30, chapter 9, now repealed]. Subsection (c)(1) [subsection (3)(a)] recognizes explicitly that this Article [Title 30, chapter 9A] defers to federal law only when and to the extent that it must-i.e., when federal law preempts it.

9. **Governmental Debtors.** Former Section 9-104(e) [30-9-104(5), now repealed] excluded transfers by governmental debtors. It has been revised and replaced by the exclusions in new paragraphs (2) and (3) of subsection (c) [subsections (3)(b) and (3)(c)]. These paragraphs reflect the view that Article 9 [Title 30, chapter 9A] should apply to security interests created by a State, foreign country, or a "governmental unit" (defined in Section 9-102 [30-9A-102]) of either except to the extent that another statute governs the issue in question. Under paragraph (2) [subsection (3)(b)], this Article [Title 30, chapter 9A] defers to all statutes of the forum State. (A forum cannot

determine whether it should consult the choice-of-law rules in the forum's UCC unless it first determines that its UCC applies to the transaction before it.) Paragraph (3) [subsection (3)(c)] defers to statutes of another State or a foreign country only to the extent that those statutes contain rules applicable specifically to security interests created by the governmental unit in question.

Example 2: A New Jersey state commission creates a security interest in favor of a New York bank. The validity of the security interest is litigated in New York. The relevant security agreement provides that it is governed by New York law. To the extent that a New Jersey statute contains rules peculiar to creation of security interests by governmental units generally, to creation of security interests by state commissions, or to creation of security interests by this particular state commission, then that law will govern. On the other hand, to the extent that New Jersey law provides that security interests created by governmental units, state commissions, or this state commission are governed by the law generally applicable to secured transactions (i.e., New Jersey's Article 9), then New York's Article 9 will govern.

Example 3: An airline that is an instrumentality of a foreign country creates a security interest in favor of a New York bank. The analysis used in the previous example would apply here. That is, if the matter is litigated in New York, New York law would govern except to the extent that the foreign country enacted a statute applicable to security interests created by governmental units generally or by the airline specifically.

The fact that New York law applies does not necessarily mean that perfection is accomplished by filing in New York. Rather, it means that the court should apply New York's Article 9, including its choice-of-law provisions. Under New York's Section 9-301, perfection is governed by the law of the jurisdiction in which the debtor is located. Section 9-307 [30-9A-307] determines the debtor's location for choice-of-law purposes.

If a transaction does not bear an appropriate relation to the forum State, then that State's Article 9 will not apply, regardless of whether the transaction would be excluded by paragraph (3) [subsection (3)(c)].

Example 4: A Belgian governmental unit grants a security interest in its equipment to a Swiss secured party. The equipment is located in Belgium. A dispute arises and, for some reason, an action is brought in a New Mexico state court. Inasmuch as the transaction bears no "appropriate relation" to New Mexico, New Mexico's UCC, including its Article 9, is inapplicable. See Section 1-105(1) [30-1-105(1), now repealed]. New Mexico's Section 9-109(c) on excluded transactions should not come into play. Even if the parties agreed that New Mexico law would govern, the parties' agreement would not be effective because the transaction does not bear a "reasonable relation" to New Mexico. See Section 1-105(1) [30-1-105(1), now repealed].

Conversely, Article 9 [Title 30, chapter 9A] will come into play only if the litigation arises in a UCC jurisdiction or if a foreign choice-of-law rule leads a foreign court to apply the law of a UCC jurisdiction. For example, if issues concerning a security interest granted by a foreign airline to a New York bank are litigated overseas, the court may be bound to apply the law of the debtor's jurisdiction and not New York's Article 9.

10. **Certain Statutory and Common-Law Liens; Interests in Real Property.** With few exceptions (nonconsensual agricultural liens being one), this Article [Title 30, chapter 9A] applies only to consensual security interests in personal property. Following former Section 9-104(b) and (j) [30-9-104(2) and (10), now repealed], paragraphs (1) and (11) of subsection (d) [subsections (4)(a) and (4)(k)] exclude landlord's liens and leases and most other interests in or liens on real property. These exclusions generally reiterate the limitations on coverage (i.e., "by contract," "in personal property and fixtures") made explicit in subsection (a)(1) [subsection (1)(a)]. Similarly, most jurisdictions provide special liens to suppliers of many types of services and materials, either by statute or by common law. With the exception of agricultural liens, it is not necessary for this Article [Title 30, chapter 9A] to provide general codification of this lien structure, which is determined in large part by local conditions and which is far removed from ordinary commercial financing. As under former Section 9-104(c) [30-9-104(3), now repealed], subsection (d)(2) [subsection (4)(b)] excludes these suppliers' liens (other than agricultural liens) from this Article [Title 30, chapter 9A]. However, Section 9-333 [30-9A-333)] provides a rule for determining priorities between certain possessory suppliers' liens and security interests covered by this Article [Title 30, chapter 9A].

11. **Wage and Similar Claims.** As under former Section 9-104(d) [30-9-104(4), now repealed], subsection (d)(3) [subsection (4)(c)] excludes assignments of claims for wages and the like from this Article [Title 30, chapter 9A]. These assignments present important social issues that other law addresses. The Federal Trade Commission has ruled that, with some exceptions,

the taking of an assignment of wages or other earnings is an unfair act or practice under the Federal Trade Commission Act. See 16 C.F.R. Part 444. State statutes also may regulate such assignments.

12. **Certain Sales and Assignments of Receivables; Judgments.** In general this Article [Title 30, chapter 9A] covers security interests in (including sales of) accounts, chattel paper, payment intangibles, and promissory notes. Paragraphs (4), (5), (6), and (7) of subsection (d) [subsections (4)(d), (4)(e), (4)(f), and (4)(g)] exclude from the Article [Title 30, chapter 9A] certain sales and assignments of receivables that, by their nature, do not concern commercial financing transactions. These paragraphs add to the exclusions in former Section 9-104(f) [30-9-104(6), now repealed] analogous sales and assignments of payment intangibles and promissory notes. For similar reasons, subsection (d)(9) [subsection (4)(i)] retains the exclusion of assignments of judgments under former Section 9-104(h) [30-9-104(8), now repealed] (other than judgments taken on a right to payment that itself was collateral under this Article [Title 30, chapter 9A]).

13. **Insurance.** Subsection (d)(8) [subsection (4)(h)] narrows somewhat the broad exclusion of interests in insurance policies under former Section 9-104(g) [30-9-104(7), now repealed]. This Article [Title 30, chapter 9A] now covers assignments by or to a health-care provider of "health-care-insurance receivables" (defined in Section 9-102 [30-9A-102]).

14. **Set-Off.** Subsection (d)(10) [subsection (4)(j)] adds two exceptions to the general exclusion of set-off rights from Article 9 [Title 30, chapter 9A] under former Section 9-104(i) [30-9-104(9), now repealed]. The first takes account of new Section 9-340 [30-9A-340], which regulates the effectiveness of a set-off against a deposit account that stands as collateral. The second recognizes Section 9-404 [30-9A-404], which affords the obligor on an account, chattel paper, or general intangible the right to raise claims and defenses against an assignee (secured party).

15. **Tort Claims.** Subsection (d)(12) [subsection (4)(l)] narrows somewhat the broad exclusion of transfers of tort claims under former Section 9-104(k) [30-9-104(11), now repealed]. This Article [Title 30, chapter 9A] now applies to assignments of "commercial tort claims" (defined in Section 9-102 [30-9A-102]) as well as to security interests in tort claims that constitute proceeds of other collateral (e.g., a right to payment for negligent destruction of the debtor's inventory). Note that once a claim arising in tort has been settled and reduced to a contractual obligation to pay (as in, but not limited to, a structured settlement) the right to payment becomes a payment intangible and ceases to be a claim arising in tort.

This Article [Title 30, chapter 9A] contains two special rules governing creation of a security interest in tort claims. First, a description of collateral in a security agreement as "all tort claims" is insufficient to meet the requirement for attachment. See Section 9-108(e) [30-9A-108(5)]. Second, no security interest attaches under an after-acquired property clause to a tort claim. See Section 9-204(b) [30-9A-204(2)]. In addition, this Article [Title 30, chapter 9A] does not determine whom the tortfeasor must pay to discharge its obligation. Inasmuch as a tortfeasor is not an "account debtor," the rules governing waiver of defenses and discharge of an obligation by an obligor (Sections 9-403, 9-404, 9-405, and 9-406) [30-9A-403, 30-9A-404, 30-9A-405, and 30-9A-406] are inapplicable to tort-claim collateral.

16. **Deposit Accounts.** Except in consumer transactions, deposit accounts may be taken as original collateral under this Article [Title 30, chapter 9A]. Under former Section 9-104(l) [30-9-104(12), now repealed], deposit accounts were excluded as original collateral, leaving security interests in deposit accounts to be governed by the common law. The common law is nonuniform, often difficult to discover and comprehend, and frequently costly to implement. As a consequence, debtors who wished to use deposit accounts as collateral sometimes were precluded from doing so as a practical matter. By excluding deposit accounts from the Article's [Title 30, chapter 9A] scope as original collateral in consumer transactions, subsection (d)(13) [subsection (4)(m)] leaves those transactions to law other than this Article [Title 30, chapter 9A]. However, in both consumer and non-consumer transactions, sections 9-315 and 9-322 [30-9A-315 and 30-9A-322] apply to deposit accounts as proceeds and with respect to priorities in proceeds.

This Article [Title 30, chapter 9A] contains several safeguards to protect debtors against inadvertently encumbering deposit accounts and to reduce the likelihood that a secured party will realize a windfall from a debtor's deposit accounts. For example, because "deposit account" is a separate type of collateral, a security agreement covering general intangibles will not adequately describe deposit accounts. Rather, a security agreement must reasonably identify the deposit accounts that are the subject of a security interest, e.g., by using the term "deposit accounts." See Section 9-108 [30-9A-108]. To perfect a security interest in a deposit account as original collateral, a secured party (other than the bank with which the deposit account is maintained) must obtain "control" of the account either by obtaining the bank's authenticated agreement or by becoming the bank's customer with respect to the deposit account. See Sections 9-312(b)(1), 9-104 [30-9A-312(2)(a) and 30-9A-104]. Either of these steps requires the debtor's consent.

This Article [Title 30, chapter 9A] also contains new rules that determine which State's law governs perfection and priority of a security interest in a deposit account (Section 9-304 [30-9A-304]), priority of conflicting security interests in and set-off rights against a deposit account (Sections 9-327, 9-340 [30-9A-327 and 30-9A-340]), the rights of transferees of funds from an encumbered deposit account (Section 9-332 [30-9A-332]), the obligations of the bank (Section 9-341 [30-9A-341]), enforcement of security interests in a deposit account (Section 9-607(c) [30-9A-607(3)]), and the duty of a secured party to terminate control of a deposit account (Section 9-208(b) [30-9A-208(2)]).

Compiler's Comments

2005 Amendment: Chapter 416 in (4)(o) near end after "chapter 51, 71" deleted "72". Amendment effective July 1, 2005.

Severability: Section 42, Ch. 416, L. 2005, was a severability clause.

Effective Date — Applicability: Section 43, Ch. 416, L. 2005, provided: "[This act] is effective July 1, 2005, and applies to occupational diseases that occur on or after July 1, 2005."

2001 Amendments — Composite Section: Chapter 179 inserted (4)(m) concerning governmental transfers; and made minor changes in style. Amendment effective July 1, 2001.

Chapter 214 inserted (4)(o) providing chapter does not apply to assignment of payments made under Title 39, chapter 51, 71, 72, or 73; and made minor changes in style. Amendment effective July 1, 2001.

Severability: Section 25, Ch. 214, L. 2001, was a severability clause.

Case Notes

CASES DECIDED PRIOR TO 1999 REVISION

Inadequate Notice of Assignment — Escrow Agent Not Liable for Failure to Disburse Funds to Party With No Escrow Rights: Brandts invested in a condominium development corporation, loaning $20,000 to the corporation president. The promissory note exchanged for the loan provided that Brandts would be repaid with interest upon sale of a condominium to a family trust. Sande acted as escrow agent for the closing of the real estate sale and purchase transaction. The corporation president had instructed the title company to repay Brandts upon closing, but later rescinded that instruction, so funds from the purchase of the condominium were disbursed to the corporation and to various creditors instead of to Brandts. When the corporation was later sold, Brandts signed an agreement releasing and discharging their claims against the corporation. Nearly 2 years later, Brandts sued Sande and the title company for negligently and wrongfully applying $20,000 from the escrow account. The District Court summarily dismissed the suit and ordered sanctions against Brandts for filing a frivolous complaint. The court determined that there was neither a valid assignment nor legal notice of an assignment of Brandts' interest in the funds from the closing, so Sande owed no legal duty to Brandts. However, Brandts never asserted an irrevocable interest in the closing proceeds either prior to or during the time that the funds were in Sande's possession, nor did they execute a written assignment to ensure that the repayment instruction would not be rescinded. Under Montana law, an escrow agent or other account debtor must have adequate notice of an assignment before an assignee can hold the agent liable for wrongful payment. The promissory note did not reasonably identify the rights assigned and was thus ineffective. Brandts did not dispute that they were not a party to the escrow agreement, and because Sande had no notice of an assignment of the closing proceeds, he was not liable under an assignment theory. Sande simply fulfilled his fiduciary duty by strictly following the instructions of the principles to the escrow account, which did not assign any funds to Brandts. Summary dismissal was affirmed on grounds that Sande owed no legal duty to Brandts. Brandt v. Sande, 2000 MT 98, 299 M 256, 1 P3d 929, 57 St. Rep. 400 (2000), distinguishing Merchants & Miners Nat'l Bank v. Barnes, 18 M 335, 45 P 218 (1896).

30-9A-110. Security interests arising under chapter 2 or 2A.

Official Comments

1. **Source.** Former Section 9-113 [30-9-113, now repealed].
2. **Background.** Former Section 9-113 [30-9-113, now repealed], from which this section derives, referred generally to security interests "arising solely under the Article on Sales (Article 2 [Title 30, chapter 2]) or the Article on Leases (Article 2A [Title 30, chapter 2A])." Views differed as to the precise scope of that section. In contrast, Section 9-110 [30-9A-110] specifies the security interests to which it applies.

3. **Security Interests Under Articles 2 and 2A [Title 30, chapters 2 and 2A].** Section 2-505 [30-2-505] explains how a seller of goods may reserve a security interest in them. Section 2-401 [30-2-401] indicates that a reservation of title by the seller of goods, despite delivery to the buyer, is limited to reservation of a security interest. As did former Article 9 [Title 30, chapter 9, now repealed], this Article [Title 30, chapter 9A] governs a security interest arising solely under one of those sections; however, until the buyer obtains possession of the goods, the security interest is enforceable even in the absence of a security agreement, filing is not necessary to perfect the security interest, and the seller-secured party's rights on the buyer's default are governed by Article 2 [Title 30, chapter 2].

Sections 2-711(3) and 2A-508(5) [30-2-711(3) and 30-2A-508(5)] create a security interest in favor of a buyer or lessee in possession of goods that were rightfully rejected or as to which acceptance was justifiably revoked. As did former Article 9 [Title 30, chapter 9, now repealed], this Article [Title 30, chapter 9A] governs a security interest arising solely under one of those sections; however, until the seller or lessor obtains possession of the goods, the security interest is enforceable even in the absence of a security agreement, filing is not necessary to perfect the security interest, and the secured party's (buyer's or lessee's) rights on the debtor's (seller's or lessor's) default are governed by Article 2 or 2A [Title 30, chapter 2 or 2A], as the case may be.

4. **Priority.** This section adds to former Section 9-113 [30-9-113, now repealed] a priority rule. Until the debtor obtains possession of the goods, a security interest arising under one of the specified sections of Article 2 or 2A [Title 30, chapter 2 or 2A] has priority over conflicting security interests created by the debtor. Thus, a security interest arising under Section 2-401 or 2-505 [30-2-401 or 30-2-505] has priority over a conflicting security interest in the buyer's after-acquired goods, even if the goods in question are inventory. Arguably, the same result would obtain under Section 9-322 [30-9A-322], but even if it would not, a purchase-money-like priority is appropriate. Similarly, a security interest under Section 2-711(3) or 2A-508(5) [30-2-711(3) or 30-2A-508(5)] has priority over security interests claimed by the seller's or lessor's secured lender. This result is appropriate, inasmuch as the payments giving rise to the debt secured by the Article 2 or 2A [Title 30, chapter 2 or 2A] security interest are likely to be included among the lender's proceeds.

Example: Seller owns equipment subject to a security interest created by Seller in favor of Lender. Buyer pays for the equipment, accepts the goods, and then justifiably revokes acceptance. As long as Seller does not recover possession of the equipment, Buyer's security interest under Section 2-711(3) [30-2-711(3)] is senior to that of Lender.

In the event that a security interest referred to in this section conflicts with a security interest that is created by a person other than the debtor, Section 9-325 [30-9A-325] applies. Thus, if Lender's security interest in the example was created not by Seller but by the person from whom Seller acquired the goods, Section 9-325 [30-9A-325] would govern.

5. **Relationship to Other Rights and Remedies Under Articles 2 and 2A [Title 30, chapters 2 and 2A].** This Article [Title 30, chapter 9A] does not specifically address the conflict between (i) a security interest created by a buyer or lessee and (ii) the seller's or lessor's right to withhold delivery under Section 2-702(1), 2-703(a), or 2A-525 [30-2-702(1), 30-2-703(1), or 30-2A-525], the seller's or lessor's right to stop delivery under Section 2-705 or 2A-526 [30-2-705 or 30-2A-526], or the seller's right to reclaim under Section 2-507(2) or 2-702(2) [30-2-507(2) or 30-2-702(2)]. These conflicts are governed by the first sentence of Section 2-403(1) [30-2-403(1)], under which the buyer's secured party obtains no greater rights in the goods than the buyer had or had power to convey, or Section 2A-307(1) [30-2A-307(1)], under which creditors of the lessee take subject to the lease contract.

Part 2

Effectiveness of Security Agreement — Attachment of Security Interest — Rights of Parties to Security Agreement

Part Compiler's Comments

Saving Clause: Section 169, Ch. 305, L. 1999, provided: "(1) Except as otherwise provided in [sections 164 through 169] [sections 162 through 167—30-9A-703 through 30-9A-706, 30-9A-708, and 30-9A-709], [this act] applies to a transaction or lien within its scope, even if the transaction or lien was entered into or created before [this act] takes effect.

(2) Except as otherwise provided in subsection (3) and [sections 164 through 169] [sections 162 through 167—30-9A-703 through 30-9A-706, 30-9A-708, and 30-9A-709]:

(a) transactions and liens that were not governed by [former chapter 9, now repealed] were validly entered into or created before [this act] takes effect and would be subject to [this act] if they had been entered into or created after [this act] takes effect, and the rights, duties, and interests flowing from those transactions and liens remain valid after [this act] takes effect; and

(b) the transactions and liens may be terminated, completed, consummated, or enforced as required or permitted by [this act] or by the law that otherwise would apply if [this act] did not take effect.

(3) [This act] does not affect an action, case, or proceeding commenced before [this act] takes effect."

30-9A-201. General effectiveness of security agreement.

Official Comments

1. **Source.** Former Sections 9-201, 9-203(4) [30-9-201, 30-9-203(4), both now repealed].

2. **Effectiveness of Security Agreement.** Subsection (a) [subsection (1)] provides that a security agreement is generally effective. With certain exceptions, a security agreement is effective between the debtor and secured party and is likewise effective against third parties. Note that "security agreement" is used here (and elsewhere in this Article [Title 30, chapter 9A]) as it is defined in Section 9-102 [30-9A-102]: "an agreement that creates or provides for a security interest." It follows that subsection (a) [subsection (1)] does not provide that every term or provision contained in a record that contains a security agreement or that is so labeled is effective. Properly read, former Section 9-201 [30-9-201, now repealed] was to the same effect. Exceptions to the general rule of subsection (a) [subsection (1)] arise where there is an overriding provision in this Article [Title 30, chapter 9A] or any other Article [chapter] of the UCC. For example, Section 9-317 [30-9A-317] subordinates unperfected security interests to lien creditors and certain buyers, and several provisions in Part 3 [Title 30, chapter 9A, part 3] subordinate some security interests to other security interests and interests of purchasers.

3. **Law, Statutes, and Regulations Applicable to Certain Transactions.** Subsection (b) [subsection (2)] makes clear that certain transactions, although subject to this Article [Title 30, chapter 9A], also are subject to other applicable laws relating to consumers or specified in that subsection. Subsection (c) [subsection (3)] provides that the other law is controlling in the event of a conflict, and that a violation of other law does not ipso facto constitute a violation of this Article [Title 30, chapter 9A]. Subsection (d) [subsection (4)] provides that this Article [Title 30, chapter 9A] does not validate violations under or extend the application of the other applicable laws.

Case Notes

DECISIONS UNDER UNIFORM TRUST RECEIPTS ACT

Validity of Trust Receipt Transactions: One of the purposes of the Uniform Trust Receipts Act, sections 65-201 through 65-219, R.C.M. 1947 (since repealed), is to make bipartite trust receipt transactions as valid as tripartite trust transactions. Keating v. Univ. Underwriters Ins. Co., 133 M 89, 320 P2d 351 (1958).

30-9A-202. Title to collateral immaterial.

Official Comments

1. **Source.** Former Section 9-202 [30-9-202, now repealed].

2. **Title Immaterial.** The rights and duties of parties to a secured transaction and affected third parties are provided in this Article [Title 30, chapter 9A] without reference to the location of "title" to the collateral. For example, the characteristics of a security interest that secures the purchase price of goods are the same whether the secured party appears to have retained title or the debtor appears to have obtained title and then conveyed title or a lien to the secured party.

3. **When Title Matters.**

a. **Under this Article [Title 30, chapter 9A].** This section explicitly acknowledges two circumstances in which the effect of certain Article 9 [Title 30, chapter 9A] provisions turns on ownership (title). First, in some respects sales of accounts, chattel paper, payment intangibles, and promissory notes receive special treatment. See, e.g., Sections 9-207(a), 9-210(b), 9-615(e) [30-9A-207(1), 30-9A-210(2), and 30-9A-615(5)]. Buyers of receivables under former Article 9 [Title 30, chapter 9, now repealed] were treated specially, as well. See, e.g., former Section 9-502(2) [30-9-502(2), now repealed, see 30-9A-608]. Second, the remedies of a consignor under a true consignment and, for the most part, the remedies of a buyer of accounts, chattel paper, payment intangibles, or promissory notes are determined by other law and not by Part 6 [Title 30, chapter 9A, part 6]. See Section 9-601(g) [30-9A-601(7)].

b. **Under Other Law.** This Article [Title 30, chapter 9A] does not determine which line of interpretation (e.g., title theory or lien theory, retained title or conveyed title) should be followed in cases in which the applicability of another rule of law depends upon who has title. If, for example, a revenue law imposes a tax on the "legal" owner of goods or if a corporation law makes a vote of the stockholders prerequisite to a corporation "giving" a security interest but not if it acquires property "subject" to a security interest, this Article [Title 30, chapter 9A] does not attempt to define whether the secured party is a "legal" owner or whether the transaction "gives" a security interest for the purpose of such laws. Other rules of law or the agreement of the parties determines the location and source of title for those purposes.

30-9A-203. Attachment and enforcement of security interest — proceeds — supporting obligations — formal requisites.

Official Comments

[*Corresponding U.C.C Section:* Section 9-203, U.C.C.]

1. **Source.** Former Sections 9-203, 9-115(2), (6) [30-9-203, 30-9-115(2), (6), both now repealed, see 30-9A-308, 30-9A-313, and this section].

2. **Creation, Attachment, and Enforceability.** Subsection (a) [subsection (1)] states the general rule that a security interest attaches to collateral only when it becomes enforceable against the debtor. Subsection (b) [subsection (2)] specifies the circumstances under which a security interest becomes enforceable. Subsection (b) [subsection (2)] states three basic prerequisites to the existence of a security interest: value (paragraph (1) [subsection (2)(a)]), rights or power to transfer rights in collateral (paragraph (2) [subsection (2)(b)]), and agreement plus satisfaction of an evidentiary requirement (paragraph (3) [subsection (2)(c)]). When all of these elements exist, a security interest becomes enforceable between the parties and attaches under subsection (a) [subsection (1)]. Subsection (c) [subsection (3)] identifies certain exceptions to the general rule of subsection (b) [subsection (2)].

3. **Security Agreement; Authentication.** Under subsection (b)(3) [subsection (2)(c)], enforceability requires the debtor's security agreement and compliance with an evidentiary requirement in the nature of a Statute of Frauds. Paragraph (3)(A) [subsection (2)(c)(i)] represents the most basic of the evidentiary alternatives, under which the debtor must authenticate a security agreement that provides a description of the collateral. Under Section 9-102 [30-9A-102], a "security agreement" is "an agreement that creates or provides for a security interest." Neither that definition nor the requirement of paragraph (3)(A) [subsection (2)(c)(i)] rejects the deeply rooted doctrine that a bill of sale, although absolute in form, may be shown in fact to have been given as security. Under this Article [Title 30, chapter 9A], as under prior law, a debtor may show by parol evidence that a transfer purporting to be absolute was in fact for security. Similarly, a self-styled "lease" may serve as a security agreement if the agreement creates a security interest. See Section 1-203 [30-1-201(2)(jj)] (distinguishing security interest from lease).

4. **Possession, Delivery, or Control Pursuant to Security Agreement.** The other alternatives in subsection (b)(3) [subsection (2)(c)] dispense with the requirement of an authenticated security agreement and provide alternative evidentiary tests. Under paragraph (3)(B) [subsection (2)(c)(ii)], the secured party's possession substitutes for the debtor's authentication under paragraph (3)(A) [subsection (2)(c)(i)] if the secured party's possession is "pursuant to the debtor's security agreement." That phrase refers to the debtor's agreement to the secured party's possession for the purpose of creating a security interest. The phrase should not be confused with the phrase "debtor has authenticated a security agreement," used in paragraph (3)(A) [subsection (2)(c)(i)], which contemplates the debtor's authentication of a record. In the unlikely event that possession is obtained without the debtor's agreement, possession would not suffice as a substitute for an authenticated security agreement. However, once the security interest has become enforceable and has attached, it is not impaired by the fact that the secured party's possession is maintained without the agreement of a subsequent debtor (e.g., a transferee). Possession as contemplated by Section 9-313 [30-9A-313] is possession for purposes of subsection (b)(3)(B) [subsection (2)(c)(ii)], even though it may not constitute possession "pursuant to the debtor's agreement" and consequently might not serve as a substitute for an authenticated security agreement under subsection (b)(3)(A) [subsection (2)(c)(i)]. Subsection (b)(3)(C) [subsection (2)(c)(iii)] provides that delivery of a certificated security to the secured party under Section 8-301 [30-8-331] pursuant to the debtor's security agreement is sufficient as a substitute for an authenticated security agreement. Similarly, under subsection (b)(3)(D) [subsection (2)(c)(iv)], control of investment property, a deposit account, electronic chattel paper, a letter-of-credit right, or electronic documents satisfies the evidentiary test if control is pursuant to the debtor's security agreement.

5. **Collateral Covered by Other Statute or Treaty.** One evidentiary purpose of the formal requisites stated in subsection (b) [subsection (2)] is to minimize the possibility of future disputes

as to the terms of a security agreement (e.g., as to the property that stands as collateral for the obligation secured). One should distinguish the evidentiary functions of the formal requisites of attachment and enforceability (such as the requirement that a security agreement contain a description of the collateral) from the more limited goals of "notice filing" for financing statements under Part 5 [Title 30, chapter 9A, part 5], explained in Section 9-502 [30-9A-502], Comment 2. When perfection is achieved by compliance with the requirements of a statute or treaty described in Section 9-311(a) [30-9A-311(1)], such as a federal recording act or a certificate-of-title statute, the manner of describing the collateral in a registry imposed by the statute or treaty may or may not be adequate for purposes of this section and Section 9-108 [30-9A-108]. However, the description contained in the security agreement, not the description in a public registry or on a certificate of title, controls for purposes of this section.

6. **Debtor's Rights; Debtor's Power to Transfer Rights.** Subsection (b)(2) [subsection (2)(b)] conditions attachment on the debtor's having "rights in the collateral or the power to transfer rights in the collateral to a secured party." A debtor's limited rights in collateral, short of full ownership, are sufficient for a security interest to attach. However, in accordance with basic personal property conveyancing principles, the baseline rule is that a security interest attaches only to whatever rights a debtor may have, broad or limited as those rights may be.

Certain exceptions to the baseline rule enable a debtor to transfer, and a security interest to attach to, greater rights than the debtor has. See Part 3, Subpart 3 [30-9A-317 through 30-9A-339] (priority rules). The phrase, "or the power to transfer rights in the collateral to a secured party," accommodates those exceptions. In some cases, a debtor may have power to transfer another person's rights only to a class of transferees that excludes secured parties. See, e.g., Section 2-403(2) [30-2-403(2)] (giving certain merchants power to transfer an entruster's rights to a buyer in ordinary course of business). Under those circumstances, the debtor would not have the power to create a security interest in the other person's rights, and the condition in subsection (b)(2) [subsection (2)(B)] would not be satisfied.

7. **New Debtors.** Subsection (e) [subsection (5)] makes clear that the enforceability requirements of subsection (b)(3) [subsection (2)(c)] are met when a new debtor becomes bound under an original debtor's security agreement. If a new debtor becomes bound as debtor by a security agreement entered into by another person, the security agreement satisfies the requirement of subsection (b)(3) [subsection (2)(c)] as to the existing and after-acquired property of the new debtor to the extent the property is described in the agreement.

Subsection (d) [subsection (4)] explains when a new debtor becomes bound. Persons who become bound under paragraph (2) [subsection (4)(b)] are limited to those who both become primarily liable for the original debtor's obligations and succeed to (or acquire) its assets. Thus, the paragraph [subsection] excludes sureties and other secondary obligors as well as persons who become obligated through veil piercing and other non-successorship doctrines. In many cases, paragraph (2) [subsection (4)(b)] will exclude successors to the assets and liabilities of a division of a debtor. See also Section 9-508 [30-9A-508], Comment 3.

8. **Supporting Obligations.** Under subsection (f) [subsection (6)], a security interest in a "supporting obligation" (defined in Section 9-102 [30-9A-102]) automatically follows from a security interest in the underlying, supported collateral. This result was implicit under former Article 9 [Title 30, chapter 9, now repealed]. Implicit in subsection (f) [subsection (6)] is the principle that the secured party's interest in a supporting obligation extends to the supporting obligation only to the extent that it supports the collateral in which the secured party has a security interest. Complex issues may arise, however, if a supporting obligation supports many separate obligations of a particular account debtor and if the supported obligations are separately assigned as security to several secured parties. The problems may be exacerbated if a supporting obligation is limited to an aggregate amount that is less than the aggregate amount of the obligations it supports. This Article [Title 30, chapter 9A] does not contain provisions dealing with competing claims to a limited supporting obligation. As under former Article 9 [Title 30, chapter 9, now repealed], the law of suretyship and the agreements of the parties will control.

9. **Collateral Follows Right to Payment or Performance.** Subsection (g) [subsection (7)] codifies the common-law rule that a transfer of an obligation secured by a security interest or other lien on personal or real property also transfers the security interest or lien. See Restatement (3d), Property (Mortgages) § 5.4(a) (1997). See also Section 9-308(e) [30-9A-308(5)] (analogous rule for perfection).

10. **Investment Property.** Subsections (h) and (i) [subsections (8) and (9)] make clear that attachment of a security interest in a securities account or commodity account is also attachment in security entitlements or commodity contracts carried in the accounts.

Compiler's Comments

2005 Amendment: Chapter 575 in (2)(c)(iv) near middle inserted "or electronic document" and near end inserted "30-7-107". Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

Case Notes

CASES DECIDED AFTER 1999 REVISION

Secured Party Entitled to Book of Business — Contracts Analyzed — Secured Interest Survived Termination of Prior Business — Insurance Company Liable for Conversion for Taking Book of Business From Secured Party: The defendant, an exclusive insurance agent for the plaintiff insurance company, sold her business to another agent and retained an economic interest as a secured creditor in the book of business. The purchasing agent was approved by the insurance company, but the insurance company terminated the relationship when the purchasing agent falsified an insurance claim. The insurance company then parked the book of business at another insurance agency and filed a complaint in interpleader to determine the rights of the parties to a contractual termination payment that was elected by the purchasing agent. In District Court, the defendant argued that she had a right to the termination payment, ongoing commissions generated by the policies, an economic interest in the agency book of business, and proceeds under 30-9A-315, while the insurance company argued that under 30-9A-203, the security interest terminated when the insurance company made the termination payment. The District Court held that the defendant retained no security interest in the book of business sold to the purchasing agent. On appeal, the Supreme Court reversed the District Court after analyzing the terms of the contracts between the parties. The court held that the defendant's position in holding an economic interest in the book of business, having the right as a secured creditor to possess the book of business upon default of the purchasing agent, and the insurance company's unauthorized control over the book of business by excluding it from the defendant after the purchasing agent's default satisfied the liability elements of conversion. Allstate Ins. Co. v. Posnien, Inc., 2015 MT 162, 379 Mont. 398, 352 P.3d 1.

CASES DECIDED PRIOR TO 1999 REVISION

Generally Worded After-Acquired Property Security Interest: Security interest covered all goods used in rental business, including but not limited to machinery, equipment, and inventory held for sale or rent "existing or hereafter acquired". Lower court's conclusion that a general description of items covered was insufficient and that trailers, hoppers, mixer, and loader used by renters to make, haul, and pour cement were not covered was erroneous. Further, the conclusion that there could be no security interest because those items were not financed by the holder of the security interest was also erroneous. Taylor Rental Corp. v. Ted Godwin Leasing, Inc., 209 M 124, 681 P2d 691, 41 St. Rep. 594 (1984).

Novation of Lease — New Lessee's Obligation Not Affected by His Ownership Rights: Franchisor took possession of franchise after franchisee indicated a desire to sell the franchise. To make the franchise more attractive to prospective purchasers, franchisor agreed with Godwin, who had leased equipment to the franchise, to make the rental payments on the equipment if Godwin would forgo repossession of the equipment. In a proceeding involving right to possession of the equipment and recovery of rental payments, although franchisor claimed a right under the Uniform Commercial Code to possession of the equipment under its security agreement with franchisee, the lower court correctly found franchisor liable for rent. That franchisor may have been entitled to possession did not preclude it from making a binding agreement with Godwin to take over franchisee's rental payments. Taylor Rental Corp. v. Ted Godwin Leasing, Inc., 209 M 124, 681 P2d 691, 41 St. Rep. 594 (1984).

Foreclosure by Secured Party Who Is Also Escrow Agent: Plaintiff bought a photography business and executed a promissory note with defendant. As collateral he assigned stock in the business. Plaintiff sold the business to Wolfe. Wolfe was to make payments to defendant to discharge his obligations, and these payments were to be directly applied to plaintiff's obligation under the promissory note. Defendant was escrow agent. Plaintiff later signed a financing statement granting defendant a security interest in the stock held in escrow. The defendant filed the security agreement. Wolfe became delinquent in his payments, and defendant notified plaintiff his payments were therefore delinquent. A later letter was sent by certified mail to the same address advising plaintiff the stock would be sold and applied to plaintiff's past-due loan. At the sale Wolfe bought the stock for the amount due on plaintiff's note. Plaintiff claimed defendant had breached its fiduciary duty by foreclosing on the stock. The security interest became binding (attached) before the parties entered the escrow agreement. The security interest continued in the collateral notwithstanding the sale to Wolfe. Upon default defendant acted within its statutory rights to foreclose on the collateral to satisfy plaintiff's obligation. The escrow arrangement did not prevent defendant as a secured party from exercising its rights to foreclose on collateral on which the debtor defaulted. Dulan v. Mont. Nat'l Bank of Roundup, 203 M 177, 661 P2d 28, 40 St. Rep. 376 (1983), followed in Weldon v. First Citizens Bank of Billings, 259 M 305, 856 P2d 225, 50 St. Rep. 807 (1993).

CASES DECIDED UNDER UNIFORM TRUST RECEIPTS ACT

Object of Trust Receipt Transactions: A cardinal object of trust receipt transactions is to enable the borrower to sell the goods in order to pay the lender, but the transactions never have for their object the vesting of ownership in the dealer. Keating v. Univ. Underwriters Ins. Co., 133 M 89, 320 P2d 351 (1958).

Type of Trust Receipt Transactions: When the financier advances funds for the purchase of the chattel, purchases it and receives title to it from the manufacturer, and delivers possession to the dealer, who gives his trust receipt to the financier, it is a tripartite or true orthodox trust receipt transaction, and where the dealer has title and gives his receipt to the financier it is a bipartite trust receipt transaction. Keating v. Univ. Underwriters Ins. Co., 133 M 89, 320 P2d 351 (1958).

30-9A-204. After acquired property — future advances.

Official Comments

1. **Source.** Former Section 9-204 [30-9-204, now repealed].

2. **After-Acquired Property; Continuing General Lien.** Subsection (a) [subsection (1)] makes clear that a security interest arising by virtue of an after-acquired property clause is no less valid than a security interest in collateral in which the debtor has rights at the time value is given. A security interest in after-acquired property is not merely an "equitable" interest; no further action by the secured party-such as a supplemental agreement covering the new collateral-is required. This section adopts the principle of a "continuing general lien" or "floating lien." It validates a security interest in the debtor's existing and (upon acquisition) future assets, even though the debtor has liberty to use or dispose of collateral without being required to account for proceeds or substitute new collateral. See Section 9-205 [30-9A-205]. Subsection (a) [subsection (1)], together with subsection (c) [subsection (3)], also validates "cross-collateral" clauses under which collateral acquired at any time secures advances whenever made.

3. **After-Acquired Consumer Goods.** Subsection (b)(1) [subsection (2)(a)] makes ineffective an after-acquired property clause covering consumer goods (defined in Section 9-109 [30-9A-109]), except as accessions (see Section 9-335 [30-9A-335]), acquired more than ten days after the secured party gives value. Subsection (b)(1) [subsection (2)(a)] is unchanged in substance from the corresponding provision in former Section 9-204(2) [30-9-204(2), now repealed].

4. **Commercial Tort Claims.** Subsection (b)(2) [subsection (2)(b)] provides that an after-acquired property clause in a security agreement does not reach future commercial tort claims. In order for a security interest in a tort claim to attach, the claim must be in existence when the security agreement is authenticated. In addition, the security agreement must describe the tort claim with greater specificity than simply "all tort claims." See Section 9-108(e) [30-9A-108(5)].

5. **Future Advances; Obligations Secured.** Under subsection (c) [subsection (3)] collateral may secure future as well as past or present advances if the security agreement so provides. This is in line with the policy of this Article [Title 30, chapter 9A] toward security interests in after-acquired property under subsection (a) [subsection (1)]. Indeed, the parties are free to agree that a security interest secures any obligation whatsoever. Determining the obligations secured by collateral is solely a matter of construing the parties' agreement under applicable law. This Article [Title 30, chapter 9A] rejects the holdings of cases decided under former Article 9 [Title 30, chapter 9, now repealed] that applied other tests, such as whether a future advance or other subsequently incurred obligation was of the same or a similar type or class as earlier advances and obligations secured by the collateral.

6. **Sales of Receivables.** Subsections (a) and (c) [subsections (1) and (3)] expressly validate after-acquired property and future advance clauses not only when the transaction is for security purposes but also when the transaction is the sale of accounts, chattel paper, payment intangibles, or promissory notes.. This result was implicit under former Article 9 [Title 30, chapter 9, now repealed].

7. **Financing Statements.** The effect of after-acquired property and future advance clauses as components of a security agreement should not be confused with the requirements applicable to financing statements under this Article's [Title 30, chapter 9A] system of perfection by notice filing. The references to after-acquired property clauses and future advance clauses in this section are limited to security agreements. There is no need to refer to after-acquired property or future advances or other obligations secured in a financing statement. See Section 9-502 [30-9A-502], Comment 2.

Case Notes

CASES DECIDED PRIOR TO 1999 REVISION

Generally Worded After-Acquired Property Security Interest: Security interest covered all goods used in rental business, including but not limited to machinery, equipment, and inventory held for sale or rent "existing or hereafter acquired". Lower court's conclusion that a general description of items covered was insufficient and that trailers, hoppers, mixer, and loader used by renters to make, haul, and pour cement were not covered was erroneous. Further, the conclusion that there could be no security interest because those items were not financed by the holder of the security interest was also erroneous. Taylor Rental Corp. v. Ted Godwin Leasing, Inc., 209 M 124, 681 P2d 691, 41 St. Rep. 594 (1984).

Joint Tenancy Auto Title — Effect on Default: Prior to the 1983 amendment to 30-9-204 (now repealed, see this section), when defendant borrowed from plaintiff on auto collateral registered in his "and/or" another's name, the plaintiff bank was entitled to sell the auto upon defendant's default and receive one-half of the proceeds even though the bank's security interest was unperfected at the time of defendant's fraudulent assignment of his interest to his sister without value. The joint tenancy interest of the defendant was severed upon his default, and the bank became tenant in common with the holder of the remaining interest in the auto. First Westside Nat'l Bank v. Llera, 176 M 481, 580 P2d 100 (1978).

30-9A-205. Use or disposition of collateral permissible.

Official Comments

1. **Source.** Former Section 9-205 [30-9-205, now repealed].

2. **Validity of Unrestricted "Floating Lien."** This Article [Title 30, chapter 9A] expressly validates the "floating lien" on shifting collateral. See Sections 9-201, 9-204 [30-9A-201 and 30-9A-204] and Comment 2. This section provides that a security interest is not invalid or fraudulent by reason of the debtor's liberty to dispose of the collateral without being required to account to the secured party for proceeds or substitute new collateral. As did former Section 9-205 [30-9-205, now repealed], this section repeals the rule of Benedict v. Ratner, 268 U.S. 353 (1925), and other cases which held such arrangements void as a matter of law because the debtor was given unfettered dominion or control over collateral. The Benedict rule did not effectively discourage or eliminate security transactions in inventory and receivables. Instead, it forced financing arrangements to be self-liquidating. Although this section repeals Benedict, the filing and other perfection requirements (see Part 3, Subpart 2 [30-9A-308 through 30-9A-316], and Part 5 [Title 30, chapter 9A, part 5]) provide for public notice that overcomes any potential misleading effects of a debtor's use and control of collateral. Moreover, nothing in this section prevents the debtor and secured party from agreeing to procedures by which the secured party polices or monitors collateral or to restrictions on the debtor's dominion. However, this Article [Title 30, chapter 9A] leaves these matters to agreement based on business considerations, not on legal requirements.

3. **Possessory Security Interests.** Subsection (b) [subsection (2)] makes clear that this section does not relax the requirements for perfection by possession under Section 9-315 [30-9A-315]. If a secured party allows the debtor access to and control over collateral its security interest may be or become unperfected.

4. **Permissible Freedom for Debtor to Enforce Collateral.** Former Section 9-205 [30-9-205, now repealed] referred to a debtor's "liberty . . to collect or compromise accounts or chattel paper." This section recognizes the broader rights of a debtor to "enforce," as well as to "collect" and "compromise" collateral. This section's reference to collecting, compromising, and

enforcing "collateral" instead of "accounts or chattel paper" contemplates the many other types of collateral that a debtor may wish to "collect, compromise, or enforce": e.g., deposit accounts, documents, general intangibles, instruments, investment property, and letter-of-credit rights.

30-9A-206. Security interest arising in purchase or delivery of financial asset.

Official Comments

1. **Source.** Former 9-116 [30-9-116, now repealed].

2. **Codification of "Broker's Lien."** Depending upon a securities intermediary's arrangements with its entitlement holders, the securities intermediary may treat the entitlement holder as entitled to financial assets before the entitlement holder has actually made payment for them. For example, many brokers permit retail customers to pay for financial assets by check. The broker may not receive final payment of the check until several days after the broker has credited the customer's securities account for the financial assets. Thus, the customer will have acquired a security entitlement prior to payment. Subsection (a) [subsection (1)] provides that, in such circumstances, the securities intermediary has a security interest in the entitlement holder's security entitlement. Under subsection (b) [subsection (2)] the security interest secures the customer's obligation to pay for the financial asset in question. Subsections (a) and (b) [subsections (1) and (2)] codify and adapt to the indirect holding system the so-called "broker's lien," which has long been recognized. See Restatement, Security § 12.

3. **Financial Assets Delivered Against Payment.** Subsection (c) [subsection (3)] creates a security interest in favor of persons who deliver certificated securities or other financial assets in physical form, such as money market instruments, if the agreed payment is not received. In some arrangements for settlement of transactions in physical financial assets, the seller's securities custodian will deliver physical certificates to the buyer's securities custodian and receive a time-stamped delivery receipt. The buyer's securities custodian will examine the certificate to ensure that it is in good order, and that the delivery matches a trade in which the buyer has instructed the seller to deliver to that custodian. If all is in order, the receiving custodian will settle with the delivering custodian through whatever funds settlement system has been agreed upon or is used by custom and usage in that market. The understanding of the trade, however, is that the delivery is conditioned upon payment, so that if payment is not made for any reason, the security will be returned to the deliverer. Subsection (c) [subsection (3)] clarifies the rights of persons making deliveries in such circumstances. It provides the person making delivery with a security interest in the securities or other financial assets; under subsection (d) [subsection (4)], the security interest secures the seller's right to receive payment for the delivery. Section 8-301 [30-8-331] specifies when delivery of a certificated security occurs; that section should be applied as well to other financial assets as well for purposes of this section.

4. **Automatic Attachment and Perfection.** Subsections (a) and (c) [subsections (1) and (3)] refer to attachment of a security interest. Attachment under this section has the same incidents (enforceability, right to proceeds, etc.) as attachment under Section 9-203 [30-9A-203]. This section overrides the general attachment rules in Section 9-203 [30-9A-203]. See Section 9-203(c) [30-9A-203(3)]. A securities intermediary's security interest under subsection (a) [subsection (1)] is perfected by control without further action. See Section 8-106 [30-8-116] (control); 9-314 [30-9A-314] (perfection). Security interests arising under subsection (c) [subsection (3)] are automatically perfected. See Section 9-309(9) [30-9A-309(9)].

30-9A-207. Rights and duties of secured party having possession or control of collateral.

Official Comments

1. **Source.** Former Section 9-207 [30-9-207, now repealed].

2. **Duty of Care for Collateral in Secured Party's Possession.** Like former section 9-207 [30-9-207, now repealed], subsection (a) [subsection (1)] imposes a duty of care, similar to that imposed on a pledgee at common law, on a secured party in possession of collateral. See Restatement, Security §§ 17, 18. In many cases a secured party in possession of collateral may satisfy this duty by notifying the debtor of action that should be taken and allowing the debtor to take the action itself. If the secured party itself takes action, its reasonable expenses may be added to the secured obligation. The revised definitions of "collateral," "debtor," and "secured party" in Section 9-102 [30-9A-102] make this section applicable to collateral subject to an agricultural lien if the collateral is in the lienholder's possession. Under Section 1-102 [30-1-102] the duty to exercise reasonable care may not be disclaimed by agreement, although under that section the parties remain free to determine by agreement standards that are not manifestly unreasonable as to what constitutes reasonable care. Unless otherwise agreed, for a secured party in possession of

chattel paper or an instrument, reasonable care includes the preservation of rights against prior parties. The secured party's right to have instruments or documents indorsed or transferred to it or its order is dealt with in the relevant sections of Articles 3, 7, and 8 [Title 30, chapters 3, 7, and 8]. See Sections 3-203(c), 7-506, 8-304(d) [30-3-203(3), 30-7-506, 30-8-115].

3. **Specific Rules When Secured Party in Possession or Control of Collateral.** Subsections (b) and (c) [subsections (2) and (3)] provide rules following common-law precedents which apply unless the parties otherwise agree. The rules in subsection (b) [subsection (2)] apply to typical issues that may arise while a secured party is in possession of collateral, including expenses, insurance, and taxes, risk of loss or damage, identifiable and fungible collateral, and use or operation of collateral. Subsection (c) [subsection (3)] contains rules that apply in certain circumstances that may arise when a secured party is in either possession or control of collateral. These circumstances include the secured party's receiving proceeds from the collateral and the secured party's creation of a security interest in the collateral.

4. **Applicability Following Default.** This section applies when the secured party has possession of collateral either before or after default. See Sections 9-601(b), 9-609 [30-9A-601(2) and 30-9A-609]. Subsection (b)(4)(C) [subsection (2)(d)(iii)] limits agreements concerning the use or operation of collateral to collateral other than consumer goods. Under Section 9-602(1) [30-9A-602(1)], a debtor cannot waive or vary that limitation.

5. **"Repledges" and Right of Redemption.** Subsection (c)(3) [subsection (3)(c)] eliminates the qualification in former Section 9-207 [30-9-207, now repealed] to the effect that the terms of a "repledge" may not "impair" a debtor's "right to redeem" collateral. The change is primarily for clarification. There is no basis on which to draw from subsection (c)(3) [subsection (3)(c)] any inference concerning the debtor's right to redeem the collateral. The debtor enjoys that right under Section 9-621 [30-9A-621]; this section need not address it. For example, if the collateral is a negotiable note that the secured party (SP-1) repledges to SP-2, nothing in this section suggests that the debtor (D) does not retain the right to redeem the note upon payment to SP-1 of all obligations secured by the note. But, as explained below, the debtor's unimpaired right to redeem as against the debtor's original secured party nevertheless may not be enforceable as against the new secured party.

In resolving questions that arise from the creation of a security interest by SP-1, one must take care to distinguish D's rights against SP-1 from D's rights against SP-2. Once D discharges the secured obligation, D becomes entitled to the note; SP-1 has no legal basis upon which to withhold it. If, as a practical matter, SP-1 is unable to return the note because SP-2 holds it as collateral for SP-1's unpaid debt, then SP-1 is liable to D under the law of conversion.

Whether SP-2 would be liable to D depends on the relative priority of SP-2's security interest and D's interest. By permitting SP-1 to create a security interest in the collateral (repledge), subsection (c)(3) [subsection (3)(c)] provides a statutory power for SP-1 to give SP-2 a security interest (subject, of course, to any agreement by SP-1 not to give a security interest). In the vast majority of cases where repledge rights are significant, the security interest of the second secured party, SP-2 in the example, will be senior to the debtor's interest. By virtue of the debtor's consent or applicable legal rules, SP-2 typically would cut off D's rights in investment property or be immune from D's claims. See Sections 9-331, 3-306 [30-9A-331 and 30-9A-306] (holder in due course), 8-303 [30-8-332] (protected purchaser), 8-502 [30-8-502] (acquisition of a security entitlement), 8-503(e) [30-8-503(5)] (action by entitlement holder). Moreover, the expectations and business practices in some markets, such as the securities markets, are such that D's consent to SP-2's taking free of D's rights inheres in D's creation of SP-1's security interest which gives rise to SP-1's power under this section. In these situations, D would have no right to recover the collateral or recover damages from SP-2. Nevertheless, D would have a damage claim against SP-1 if SP-1 had given a security interest to SP-2 in breach of its agreement with D. Moreover, if SP-2's security interest secures an amount that is less than the amount secured by SP-1's security interest (granted by D), then D's exercise of its right to redeem would provide value sufficient to discharge SP-1's obligations to SP-2.

For the most part this section does not change the law under former Section 9-207 [30-9-207, now repealed], although eliminating the reference to the debtor's right of redemption may alter the secured party's right to repledge in one respect. Former Section 9-207 [30-9-207, now repealed] could have been read to limit the secured party's statutory right to repledge collateral to repledge transactions in which the collateral did not secure a greater obligation than that of the original debtor. Inasmuch as this is a matter normally dealt with by agreement between the debtor and secured party, any change would appear to have little practical effect.

6. **"Repledges" of Investment Property.** The following example will aid the discussion of "repledges" of investment property.

Example. Debtor grants Alpha Bank a security interest in a security entitlement that includes 1000 shares of XYZ Co. stock that Debtor holds through an account with Able & Co. Alpha does not have an account with Able. Alpha uses Beta Bank as its securities custodian. Debtor instructs Able to transfer the shares to Beta, for the account of Alpha, and Able does so. Beta then credits Alpha's account. Alpha has control of the security entitlement for the 1000 shares under Section 8-106(d) [30-8-116(4)]. (These are the facts of Example 2, Section 8-106 [30-8-116], Comment 4.) Although, as between Debtor and Alpha, Debtor may have become the beneficial owner of the new securities entitlement with Beta, Beta has agreed to act on Alpha's entitlement orders because, as between Beta and Alpha, Alpha has become the entitlement holder.

Next, Alpha grants Gamma Bank a security interest in the security entitlement with Beta that includes the 1000 shares of XYZ Co. stock. In order to afford Gamma control of the entitlement, Alpha instructs Beta to transfer the stock to Gamma's custodian, Delta Bank, which credits Gamma's account for 1000 shares. At this point Gamma holds its securities entitlement for its benefit as well as that of its debtor, Alpha. Alpha's derivative rights also are for the benefit of Debtor.

In many, probably most, situations and at any particular point in time, it will be impossible for Debtor or Alpha to "trace" Alpha's "repledge" to any particular securities entitlement or financial asset of Gamma or anyone else. Debtor would retain, of course, a right to redeem the collateral from Alpha upon satisfaction of the secured obligation. However, in the absence of a traceable interest, Debtor would retain only a personal claim against Alpha in the event Alpha failed to restore the security entitlement to Debtor. Moreover, even in the unlikely event that Debtor could trace a property interest, in the context of the financial markets, normally the operation of this section, Debtor's explicit agreement to permit Alpha to create a senior security interest, or legal rules permitting Gamma to cut off Debtor's rights or become immune from Debtor's claims would effectively subordinate Debtor's interest to the holder of a security interest created by Alpha. And, under the shelter principle, all subsequent transferees would obtain interests to which Debtor's interest also would be subordinate.

7. **Buyers of Chattel Paper and Other Receivables; Consignors.** This section has been revised to reflect the fact that a seller of accounts, chattel paper, payment intangibles, or promissory notes retains no interest in the collateral and so is not disadvantaged by the secured party's noncompliance with the requirements of this section. Accordingly, subsection (d) [subsection (4)] provides that subsection (a) [subsection (1)] applies only to security interests that secure an obligation and to sales of receivables in which the buyer has recourse against the debtor. (Of course, a buyer of accounts or payment intangibles could not have "possession" of original collateral, but might have possession of proceeds, such as promissory notes or checks.) The meaning of "recourse" in this respect is limited to recourse arising out of the account debtor's failure to pay or other default.

Subsection (d) [subsection (4)] makes subsections (b) and (c) [subsections (2) and (3)] inapplicable to buyers of accounts, chattel paper, payment intangibles, or promissory notes and consignors. Of course, there is no reason to believe that a buyer of receivables or a consignor could not, for example, create a security interest or otherwise transfer an interest in the collateral, regardless of who has possession of the collateral. However, this section leaves the rights of those owners to law other than Article 9 [Title 30, chapter 9A].

Compiler's Comments

2005 Amendment: Chapter 575 in (3) near end inserted "30-7-107"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-9A-208. Additional duties of secured party having control of collateral.

Official Comments

[*Corresponding U.C.C Section:* Section 9-208, U.C.C.]

1. **Source.** New.
2. Scope and Purpose. This section imposes duties on a secured party who has control of a deposit account, electronic chattel paper, investment property, a letter-of-credit right, or electronic documents of title. The duty to terminate the secured party's control is analogous to the duty to file a termination statement, imposed by Section 9-513 [30-9A-513]. Under subsection (a) [subsection (1)], it applies only when there is no outstanding secured obligation and the secured party is not committed to give value. The requirements of this section can be varied by agreement under Section 1-102(3) [sic] [30-1-102(3), 2003 MCA]. For example, a debtor could by contract agree that the secured party may comply with subsection (b) [subsection (2)] by releasing control more than 10 days after demand. Also, duties under this section should not be read to conflict with the terms of the collateral itself. For example, if the collateral is a time deposit account, subsection (b)(2) [subsection (2)(b)] should not require a secured party with control to make an early withdrawal of the funds (assuming that were possible) in order to pay them over to the debtor or put them in an account in the debtor's name.
3. **Remedy for Failure to Relinquish Control.** If a secured party fails to comply with the requirements of subsection (b) [subsection (2)], the debtor has the remedy set forth in Section 9-625(e) [30-9A-625(5)]. This remedy is identical to that applicable to failure to provide or file a termination statement under Section 9-513 [30-9A-513].
4. **Duty to Relinquish Possession.** Although Section 9-207 [30-9A-207] addresses directly the duties of a secured party in possession of collateral, that section does not require the secured party to relinquish possession when the secured party ceases to hold a security interest. Under common law, absent agreement to the contrary, the failure to relinquish possession of collateral upon satisfaction of the secured obligation would constitute a conversion. Inasmuch as problems apparently have not surfaced in the absence of statutory duties under former Article 9 [Title 30, chapter 9, now repealed] and the common-law duty appears to have been sufficient, this Article [Title 30, chapter 9A] does not impose a statutory duty to relinquish possession.

Compiler's Comments

2005 Amendment: Chapter 575 inserted (2)(f) relating to control of an electronic document; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-9A-209. Duties of secured party if account debtor has been notified of assignment.

Official Comments

1. **Source.** New.
2. **Scope and Purpose.** Like Sections 9-208 and 9-513 [30-9A-208 and 30-9A-513], which require a secured party to relinquish control of collateral and to file or provide a termination statement for a financing statement, this section requires a secured party to free up collateral when there no longer is any outstanding secured obligation or any commitment to give value in the future. This section addresses the case in which account debtors have been notified to pay a secured party to whom the receivables have been assigned. It requires the secured party (assignee) to inform the account debtors that they no longer are obligated to make payment to the secured party. See subsection (b) [subsection (2)]. It does not apply to account debtors whose obligations on an account, chattel paper, or payment intangible have been sold. See subsection (c) [subsection (3)].

Case Notes

CASES DECIDED PRIOR TO 1999 REVISION

Inadequate Notice of Assignment — Escrow Agent Not Liable for Failure to Disburse Funds to Party With No Escrow Rights: Brandts invested in a condominium development corporation, loaning $20,000 to the corporation president. The promissory note exchanged for the loan provided that Brandts would be repaid with interest upon sale of a condominium to a family trust. Sande acted as escrow agent for the closing of the real estate sale and purchase transaction. The corporation president had instructed the title company to repay Brandts upon closing, but later rescinded that instruction, so funds from the purchase of the condominium were disbursed to the corporation and to various creditors instead of to Brandts. When the corporation was later sold, Brandts signed an agreement releasing and discharging their claims against the corporation. Nearly 2 years later, Brandts sued Sande and the title company for negligently and wrongfully applying $20,000 from the escrow account. The District Court summarily dismissed the suit and ordered sanctions against Brandts for filing a frivolous complaint. The court determined that there was neither a valid assignment nor legal notice of an assignment of Brandts' interest in the funds from the closing, so Sande owed no legal duty to Brandts. However, Brandts never asserted an irrevocable interest in the closing proceeds either prior to or during the time that the funds were in Sande's possession, nor did they execute a written assignment to ensure that the repayment instruction would not be rescinded. Under Montana law, an escrow agent or other account debtor must have adequate notice of an assignment before an assignee can hold the agent liable for wrongful payment. The promissory note did not reasonably identify the rights assigned and was thus ineffective. Brandts did not dispute that they were not a party to the escrow agreement, and because Sande had no notice of an assignment of the closing proceeds, he was not liable under an assignment theory. Sande simply fulfilled his fiduciary duty by strictly following the instructions of the principles to the escrow account, which did not assign any funds to Brandts. Summary dismissal was affirmed on grounds that Sande owed no legal duty to Brandts. Brandt v. Sande, 2000 MT 98, 299 M 256, 1 P3d 929, 57 St. Rep. 400 (2000), distinguishing Merchants & Miners Nat'l Bank v. Barnes, 18 M 335, 45 P 218 (1896).

30-9A-210. Request for accounting — request regarding list of collateral or statement of account.

Official Comments

1. **Source.** Former Section 9-208 [30-9-208, now repealed].

2. **Scope and Purpose.** This section provides a procedure whereby a debtor may obtain from a secured party information about the secured obligation and the collateral in which the secured party may claim a security interest. It clarifies and resolves some of the issues that arose under former Section 9-208 [30-9-208, now repealed] and makes information concerning the secured indebtedness readily available to debtors, both before and after default. It applies to agricultural lien transactions (see the definitions of "debtor," "secured party," and "collateral" in Section 9-102 [30-9A-102]), but generally not to sales of receivables. See subsection (b) [subsection (2)].

3. **Requests by Debtors Only.** A financing statement filed under Part 5 [Title 30, chapter 9A, part 5] may disclose only that a secured party may have a security interest in specified types of collateral. In most cases the financing statement will contain no indication of the obligation (if any) secured, whether any security interest actually exists, or the particular property subject to a security interest. Because creditors of and prospective purchasers from a debtor may have legitimate needs for more detailed information, it is necessary to provide a procedure under which the secured party will be required to provide information. On the other hand, the secured party should not be under a duty to disclose any details of the debtor's financial affairs to any casual inquirer or competitor who may inquire. For this reason, this section gives the right to request information to the debtor only. The debtor may submit a request in connection with negotiations with subsequent creditors and purchasers, as well as for the purpose of determining the status of its credit relationship or demonstrating which of its assets are free of a security interest.

4. **Permitted Types of Requests for Information.** Subsection (a) [subsection (1)] contemplates that a debtor may request three types of information by submitting three types of "requests" to the secured party. First, the debtor may request the secured party to prepare and send an "accounting" (defined in Section 9-102 [30-9A-102]). Second, the debtor may submit to the secured party a list of collateral for the secured party's approval or correction. Third, the debtor may submit to the secured party for its approval or correction a statement of the aggregate amount of unpaid secured obligations. Inasmuch as a secured party may have numerous transactions and relationships with a debtor, each request must identify the relevant transactions or relationships. Subsections (b) and (c) [subsections (2) and (3)] require the secured party to respond to a request within 14 days following receipt of the request.

5. **Recipients Claiming No Interest in the Transaction.** A debtor may be unaware that a creditor with whom it has dealt has assigned its security interest or the secured obligation. Subsections (d) and (e) [subsections (4) and (5)] impose upon recipients of requests under this section the duty to inform the debtor that they claim no interest in the collateral or secured obligation, respectively, and to inform the debtor of the name and mailing address of any known assignee or successor. As under subsections (b) and (c) [subsections (2) and (3)], a response to a request under subsection (d) or (e) [subsection (4) or (5)] is due 14 days following receipt.

6. **Waiver; Remedy for Failure to Comply.** The debtor's rights under this section may not be waived or varied. See Section 9-602(2) [30-9A-602(2)]. Section 9-625(e) [30-9A-625(5)] sets forth the remedy for noncompliance with the requirements of this section.

7. **Limitation on Free Responses to Requests.** Under subsection (f) [subsection (6)], during a six-month period a debtor is entitled to receive from the secured party one free response to a request. The debtor is not entitled to a free response to each type of request (i.e., three free responses) during a six-month period.

Compiler's Comments

2001 Amendment: Chapter 179 in (4)(b) before "interest" deleted "security". Amendment effective July 1, 2001.

Part 3
Perfection and Priority

Part Compiler's Comments

Saving Clause: Section 169, Ch. 305, L. 1999, provided: "(1) Except as otherwise provided in [sections 164 through 169] [sections 162 through 167—30-9A-703 through 30-9A-706, 30-9A-708, and 30-9A-709], [this act] applies to a transaction or lien within its scope, even if the transaction or lien was entered into or created before [this act] takes effect.

(2) Except as otherwise provided in subsection (3) and [sections 164 through 169] [sections 162 through 167—30-9A-703 through 30-9A-706, 30-9A-708, and 30-9A-709]:

(a) transactions and liens that were not governed by [former chapter 9, now repealed] were validly entered into or created before [this act] takes effect and would be subject to [this act] if they had been entered into or created after [this act] takes effect, and the rights, duties, and interests flowing from those transactions and liens remain valid after [this act] takes effect; and

(b) the transactions and liens may be terminated, completed, consummated, or enforced as required or permitted by [this act] or by the law that otherwise would apply if [this act] did not take effect.

(3) [This act] does not affect an action, case, or proceeding commenced before [this act] takes effect."

30-9A-301. Law governing perfection and priority of security interests.

Official Comments

[*Corresponding U.C.C Section:* Section 9-301, U.C.C.]

1. **Source.** Former Sections 9-103(1)(a), (b), 9-103(3)(a), (b), 9-103(5) [30-9-103(1)(a), (1)(b), 30-9-103(3)(a), (3)(b), 30-9-103(5), all now repealed], substantially modified.

2. **Scope of This Subpart [30-9A-301 through 30-9A-307].** Part 3, Subpart 1 (Sections 9-301 through 9-307 [30-9A-301 through 30-9A-307]) contains choice-of-law rules similar to those of former Section 9-103 [30-9-103, now repealed]. Former Section 9-103 [30-9-103, now repealed] generally addresses which State's law governs "perfection and the effect of perfection or non-perfection of" security interests. See, e.g., former Section 9-103(1)(b) [30-9-103(1)(b), now repealed]. This Article [Title 30, chapter 9A] follows the broader and more precise formulation in former Section 9-103(6)(b) [30-9-103(6)(b), now repealed], which was revised in connection with the promulgation of Revised Article 8 [Title 30, chapter 8] in 1994: "perfection, the effect of perfection or non-perfection, and the priority of" security interests. Priority, in this context, subsumes all of the rules in Part 3 [Title 30, chapter 9A, part 3], including "cut off" or "take free" rules such as Sections 9-317(b), (c), and (d), 9-320(a), (b), and (d), and 9-332 [30-9A-317(2), (3), and (4), 30-9A-320(1), (2), and (4), and 30-9A-332]. This subpart [30-9A-301 through 30-9A-307] does not address choice of law for other purposes. For example, the law applicable to issues such as attachment, validity, characterization (e.g., true lease or security interest), and enforcement is governed by the rules in Section 1-301 [30-1-301]; that governing law typically is specified in the same agreement that contains the security agreement. And, another jurisdiction's law may govern other third-party matters addressed in this Article [Title 30, chapter 9A]. See Section 9-401 [30-9A-401], Comment 3.

3. **Scope of Referral.** In designating the jurisdiction whose law governs, this Article [Title 30, chapter 9A] directs the court to apply only the substantive ("local") law of a particular jurisdiction and not its choice-of-law rules.

Example 1: Litigation over the priority of a security interest in accounts arises in State X. State X has adopted the official text of this Article [Title 30, chapter 9A], which provides that priority is determined by the local law of the jurisdiction in which the debtor is located. See Section 9-301(1) [30-9A-301(1)]. The debtor is located in State Y. Even if State Y has retained former Article 9 [Title 30, chapter 9, now repealed] or enacted a nonuniform choice-of-law rule (e.g., one that provides that perfection is governed by the law of State Z), a State X court should look only to the substantive law of State Y and disregard State Y's choice-of-law rule. State Y's substantive law (e.g., its Section 9-501 [30-9A-501]) provides that financing statements should be filed in a filing office in State Y. Note, however, that if the identical perfection issue were to be litigated in State Y, the court would look to State Y's former Section 9-103 [30-9-103, now repealed] or nonuniform 9-301 [30-9A-301] and conclude that a filing in State Y is ineffective.

Example 2: In the preceding Example, assume that State X has adopted the official text of this Article [Title 30, chapter 9A], and State Y has adopted a nonuniform Section 9-301(1) [30-9A-301(1)] under which perfection is governed by the whole law of State X, including its choice-of-law rules. If litigation occurs in State X, the court should look to the substantive law of State Y, which provides that financing statements are to be filed in a filing office in State Y. If litigation occurs in State Y, the court should look to the law of State X, whose choice-of-law rule requires that the court apply the substantive law of State Y. Thus, regardless of the jurisdiction in which the litigation arises, the financing statement should be filed in State Y.

4. **Law Governing Perfection: General Rule.** Paragraph (1) [subsection (1)] contains the general rule: the law governing perfection of security interests in both tangible and intangible collateral, whether perfected by filing or automatically, is the law of the jurisdiction of the debtor's location, as determined under Section 9-307 [30-9A-307].

Paragraph (1) [subsection (1)] substantially simplifies the choice-of-law rules. Former Section 9-103 [30-9-103, now repealed] contained different choice-of-law rules for different types of collateral. Under Section 9-301(1) [30-9A-301(1)], the law of a single jurisdiction governs perfection with respect to most types of collateral, both tangible and intangible. Paragraph (1) [subsection (1)] eliminates the need for former Section 9-103(1)(c) [30-9-103(1)(c), now repealed], which concerned purchase-money security interests in tangible collateral that is intended to move from one jurisdiction to the other. It is likely to reduce the frequency of cases in which the governing law changes after a financing statement is properly filed. (Presumably, debtors change their own location less frequently than they change the location of their collateral.) The approach taken in paragraph (1) [subsection (1)] also eliminates some difficult priority issues and the need to distinguish between "mobile" and "ordinary" goods, and it reduces the number of filing offices in which secured parties must file or search when collateral is located in several jurisdictions.

5. **Law Governing Perfection: Exceptions.** The general rule is subject to several exceptions. It does not apply to goods covered by a certificate of title (see Section 9-303 [30-9A-303]), deposit accounts (see Section 9-304 [30-9A-304]), investment property (see Section 9-305 [30-9A-305]), or letter-of-credit rights (see Section 9-306 [30-9A-306]). Nor does it apply to possessory security interests, i.e., security interests that the secured party has perfected by taking possession of the collateral (see paragraph (2) [subsection (2)]), security interests perfected by filing a fixture filing (see paragraph (3)(A) [subsection (3)(a)]), security interests in timber to be cut (paragraph (3)(B) [subsection (3)(b)]), or security interests in as-extracted collateral (see paragraph (4) [subsection (4)]).

a. **Possessory Security Interests.** Paragraph (2) [subsection (2)] applies to possessory security interests and provides that perfection is governed by the local law of the jurisdiction in which the collateral is located. This is the rule of former Section 9-103(1)(b) [30-9-103(1)(b), now repealed], except paragraph (2) [subsection (2)] eliminates the troublesome "last event" test of former law.

The distinction between nonpossessory and possessory security interests creates the potential for the same jurisdiction to apply two different choice-of-law rules to determine perfection in the same collateral. For example, were a secured party in possession of an instrument or a tangible document to relinquish possession in reliance on temporary perfection, the applicable law immediately would change from that of the location of the collateral to that of the location of the debtor. The applicability of two different choice-of-law rules for perfection is unlikely to lead to any material practical problems. The perfection rules of one Article 9 [Title 30, chapter 9A] jurisdiction are likely to be identical to those of another. Moreover, under paragraph (3) [subsection (3)], the relative priority of competing security interests in tangible collateral is resolved by reference to the law of the jurisdiction in which the collateral is located, regardless of how the security interests are perfected.

b. **Fixtures.** Under the general rule in paragraph (1) [subsection (1)], a security interest in fixtures may be perfected by filing in the office specified by Section 9-501(a) [30-9A-501(1)] as enacted in the jurisdiction in which the debtor is located. However, application of this rule to perfection of a security interest by filing a fixture filing could yield strange results. For example, perfection of a security interest in fixtures located in Arizona and owned by a Delaware corporation would be governed by the law of Delaware. Although Delaware law would send one to a filing office in Arizona for the place to file a financing statement as a fixture filing, see Section 9-501 [30-9A-501], Delaware law would not take account of local, nonuniform, real-property filing and recording requirements that Arizona law might impose. For this reason, paragraph (3)(A) [subsection (3)(a)] contains a special rule for security interests perfected by a fixture filing; the law of the jurisdiction in which the fixtures are located governs perfection, including the formal requisites of a fixture filing. Under paragraph (3)(C) [subsection (3)(c)], the same law governs priority. Fixtures are "goods" as defined in Section 9-102 [30-9A-102].

The filing of a financing statement to perfect a security interest in collateral of a transmitting utility constitutes a fixture filing with respect to goods that are or become fixtures. See Section 9-501(b) [30-9A-501(2)]. Accordingly, to perfect a security interest in goods of this kind by a fixture filing, a financing statement must be filed in the office specified by Section 9-501(b) [30-9A-501(2)] as enacted in the jurisdiction in which the goods are located. If the fixtures collateral is located in more than one State, filing in all of those States will be necessary to perfect a security interest in all the fixtures collateral by a fixture filing. Of course, a security interest in nearly all types of collateral (including fixtures) of a transmitting utility may be perfected by filing in the office specified by Section 9-501(b) [30-9A-501(2)] as enacted in the jurisdiction in which the transmitting utility is located. However, such a filing will not be effective as a fixture filing except with respect to goods that are located in that jurisdiction.

c. **Timber to Be Cut.** Application of the general rule in paragraph (1) [subsection (1)] to perfection of a security interest in timber to be cut would yield undesirable results analogous to those described with respect to fixtures. Paragraph (3)(B) [subsection (3)(b)] adopts a similar solution: perfection is governed by the law of the jurisdiction in which the timber is located. As with fixtures, under paragraph (3)(C) [subsection (3)(c)], the same law governs priority. Timber to be cut also is "goods" as defined in Section 9-102 [30-9A-102].

Paragraph (3)(B) [subsection (3)(b)] applies only to "timber to be cut," not to timber that has been cut. Consequently, once the timber is cut, the general choice-of-law rule in paragraph (1) [subsection (1)] becomes applicable. To ensure continued perfection, a secured party should file in both the jurisdiction in which the timber to be cut is located and in the state where the debtor is located. The former filing would be with the office in which a real property mortgage would be filed, and the latter would be a central filing. See Section 9-501 [30-9A-501].

d. **As-Extracted Collateral.** Paragraph (4) [subsection (4)] adopts the rule of former Section 9-103(5) [subsection 30-9A-103(5)] with respect to certain security interests in minerals and related accounts. Like security interests in fixtures perfected by filing a fixture filing, security interests in minerals that are as-extracted collateral are perfected by filing in the office designated for the filing or recording of a mortgage on the real property. For the same reasons, the law governing perfection and priority is the law of the jurisdiction in which the wellhead or minehead is located.

6. **Change in Law Governing Perfection.** When the debtor changes its location to another jurisdiction, the jurisdiction whose law governs perfection under paragraph (1) [subsection (1)] changes, as well. Similarly, the law governing perfection of a possessory security interest in collateral under paragraph (2) [subsection (2)] changes when the collateral is removed to another jurisdiction. Nevertheless, these changes will not result in an immediate loss of perfection. See Section 9-316(a), (b) [30-9A-316(1) and (2).

7. **Law Governing Effect of Perfection and Priority: Goods, Documents, Instruments, Money, Negotiable Documents, and Tangible Chattel Paper.** Under former Section 9-103 [30-9-103, now repealed], the law of a single jurisdiction governed both questions of perfection and those of priority. This Article [Title 30, chapter 9A] generally adopts that approach. See paragraph (1) [subsection (1)]. But the approach may create problems if the debtor and collateral are located in different jurisdictions. For example, assume a security interest in equipment located in Pennsylvania is perfected by filing in Illinois, where the debtor is located. If the law of the jurisdiction in which the debtor is located were to govern priority, then the priority of an execution lien on goods located in Pennsylvania would be governed by rules enacted by the Illinois legislature.

To address this problem, paragraph (3)(C) [subsection (3)(c)] divorces questions of perfection from questions of "the effect of perfection or nonperfection and the priority of a security interest." Under paragraph (3)(C) [subsection (3)(c)], the rights of competing claimants to tangible collateral are resolved by reference to the law of the jurisdiction in which the collateral is located. A similar bifurcation applied to security interests in investment property under former Section 9-103(6) [30-9-103(6), now repealed]. See Section 9-305 [30-9A-305].

Paragraph (3)(C) [subsection (3)(c)] applies the law of the situs to determine priority only with respect to goods (including fixtures), instruments, money, tangible negotiable documents, and tangible chattel paper. Compare former Section 9-103(1) [30-9-103(1), now repealed], which applied the law of the location of the collateral to documents, instruments, and "ordinary" (as opposed to "mobile") goods. This Article [Title 30, chapter 9A] does not distinguish among types of goods. The ordinary/mobile goods distinction appears to address concerns about where to file and search, rather than concerns about priority. There is no reason to preserve this distinction under the bifurcated approach.

Particularly serious confusion may arise when the choice-of-law rules of a given jurisdiction result in each of two competing security interests in the same collateral being governed by a different priority rule. The potential for this confusion existed under former Section 9-103(4) [30-9-103(4), now repealed] with respect to chattel paper: Perfection by possession was governed by the law of the location of the paper, whereas perfection by filing was governed by the law of the location of the debtor. Consider the mess that would have been created if the language or interpretation of former Section 9-308 [30-9-308, now repealed, see 30-9A-330] were to differ in the two relevant States, or if one of the relevant jurisdictions (e.g., a foreign country) had not adopted Article 9 [Title 30, chapter 9A]. The potential for confusion could have been exacerbated when a secured party perfected both by taking possession in the State where the collateral is located (State A) and by filing in the State where the debtor is located (State B)-a common practice for some chattel paper financers. By providing that the law of the jurisdiction in which the collateral is located governs priority, paragraph (3) [subsection (3)] substantially diminishes this problem.

8. **Non-U.S. Debtors.** This Article [Title 30, chapter 9A] applies the same choice-of-law rules to all debtors, foreign and domestic. For example, it adopts the bifurcated approach for determining the law applicable to security interests in goods and other tangible collateral. See Comment 5.a., above. The Article [Title 30, chapter 9A] contains a new rule specifying the location of non-U.S. debtors for purposes of this Part [Title 30, chapter 9A, part 3]. The rule appears in Section 9-307 [30-9A-307] and is explained in the Reporters' Comments following that section. Former Section 9-103(3)(c) [30-9-103(3)(c), now repealed], which contained a special choice-of-law rule governing security interests created by debtors located in a non-U.S. jurisdiction, proved unsatisfactory and was deleted.

Compiler's Comments

2005 Amendment: Chapter 575 in (3) near beginning inserted "tangible". Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

Case Notes

CASES DECIDED AFTER 1999 REVISION

Applicability of Local Law When Perfecting Agricultural Liens: In a dispute over priority of an agricultural lien versus a security interest in the same profits from agricultural products, plaintiff who held a security interest asserted that defendant who held an agricultural lien did not satisfy the requirements of the Uniform Commercial Code (U.C.C.) regarding perfection because defendant's lien was not perfected in North Dakota where the farm products were located, as required by 30-9A-302, at the time that the dispute arose. However, agricultural liens follow the location of the farm products, not the location of the debtor, and when defendant's lien was created, the products in question were located in Montana. Therefore, Montana's local law was the local law designated by the U.C.C. to govern perfection of the lien. Defendant properly filed the lien in Montana and therefore did not violate the U.C.C. in perfecting the lien. Stockman Bank of Mont. v. Mon-Kota, Inc., 2008 MT 74, 342 M 115, 180 P3d 1125 (2008).

CASES DECIDED PRIOR TO 1999 REVISION

Purchase by Lessee Does Not Make Lessor a Buyer: Paccar leased trucks to MPT. MPT entered into an agreement to buy tires from Les Schwab on credit. When MPT defaulted on its purchase agreement, Paccar argued that it had a superior interest to Les Schwab in the tires on the basis that Paccar purchased the tires as a buyer, not in the ordinary course of business. The Supreme Court held that Paccar was not a buyer in that it had never given any money to Les Schwab and title had never passed to Paccar nor had it taken delivery. Paccar Financial Corp. v. Les Schwab Tire Centers of Mont., Inc., 277 M 171, 920 P2d 977, 53 St. Rep. 652 (1996).

30-9A-302. Law governing perfection and priority of agricultural liens.

Official Comments

1. **Source.** New.

2. **Agricultural Liens.** This section provides choice-of-law rules for agricultural liens on farm products. Perfection, the effect of perfection or nonperfection, and priority all are governed by the law of the jurisdiction in which the farm products are located. Other choice-of-law rules, including Section 1-301 [30-1-301], determine which jurisdiction's law governs other matters, such as the secured party's rights on default. See Section 9-301 [30-9A-301], Comment 2. Inasmuch as no agricultural lien on proceeds arises under this Article [Title 30, chapter 9A], this section does not expressly apply to proceeds of agricultural liens. However, if another statute creates an agricultural lien on proceeds, it may be appropriate for courts to apply the choice-of-law rule in this section to determine priority in the proceeds.

Compiler's Comments

2005 Amendment: Chapter 207 at beginning inserted "Subject to the provisions of 30-9A-501"; and made minor changes in style. Amendment effective October 1, 2005.

Administrative Rules

ARM 44.6.112 Farm bill master list.

Case Notes

Applicability of Local Law When Perfecting Agricultural Liens: In a dispute over priority of an agricultural lien versus a security interest in the same profits from agricultural products, plaintiff who held a security interest asserted that defendant who held an agricultural lien did not satisfy the requirements of the Uniform Commercial Code (U.C.C.) regarding perfection because defendant's lien was not perfected in North Dakota where the farm products were located, as required by 30-9A-302, at the time that the dispute arose. However, agricultural liens follow the location of the farm products, not the location of the debtor, and when defendant's lien was created, the products in question were located in Montana. Therefore, Montana's local law was the local law designated by the U.C.C. to govern perfection of the lien. Defendant properly filed the lien in Montana and therefore did not violate the U.C.C. in perfecting the lien. Stockman Bank of Mont. v. Mon-Kota, Inc., 2008 MT 74, 342 M 115, 180 P3d 1125 (2008).

Continuation of Agricultural Lien of Farm Products After Sale, but Not on Sale Proceeds — Inchoate, Unperfected Agricultural Lien Interests Allowed: The Uniform Commercial Code (U.C.C.) leaves to other law the determination of whether an agricultural lien extends to proceeds. Montana's agricultural lien law, 71-3-901, does not extend to an agricultural supplier the right to a lien on the proceeds from the sale of liened farm products. However, a perfected agricultural lien remains attached to the collateral, even after its sale or transfer, until the secured party releases its lien. The right to judicially enforce or foreclose an agricultural lien is not lost upon sale or transfer of farm products. Stockman Bank of Mont. v. Mon-Kota, Inc., 2008 MT 74, 342 M 115, 180 P3d 1125 (2008).

30-9A-303. Law governing perfection and priority of security interests in goods covered by a certificate of title.

Official Comments

1. **Source.** Former Section 9-103(2)(a), (b) [30-9-103(2)(a), (2)(b), now repealed], substantially revised.

2. **Scope of This Section.** This section applies to "goods covered by a certificate of title." The new definition of "certificate of title" in Section 9-102 [30-9A-102] makes clear that this section applies not only to certificate-of-title statutes under which perfection occurs upon notation of the security interest on the certificate but also to those that contemplate notation but provide that perfection is achieved by another method, e.g., delivery of designated documents to an official. Subsection (a) [subsection (1)], which is new, makes clear that this section applies to certificates

of a jurisdiction having no other contacts with the goods or the debtor. This result comports with most of the reported cases on the subject and with contemporary business practices in the trucking industry.

3. **Law Governing Perfection and Priority.** Subsection (c) [subsection (3)] is the basic choice-of-law rule for goods covered by a certificate of title. Perfection and priority of a security interest are governed by the law of the jurisdiction under whose certificate of title the goods are covered from the time the goods become covered by the certificate of title until the goods cease to be covered by the certificate of title.

Normally, under the law of the relevant jurisdiction, the perfection step would consist of compliance with that jurisdiction's certificate-of-title statute and a resulting notation of the security interest on the certificate of title. See Section 9-311(b) [30-9A-311(2)]. In the typical case of an automobile or over-the-road truck, a person who wishes to take a security interest in the vehicle can ascertain whether it is subject to any security interests by looking at the certificate of title. But certificates of title cover certain types of goods in some States but not in others. A secured party who does not realize this may extend credit and attempt to perfect by filing in the jurisdiction in which the debtor is located. If the goods had been titled in another jurisdiction, the lender would be unperfected.

Subsection (b) [subsection (2)] explains when goods become covered by a certificate of title and when they cease to be covered. Goods may become covered by a certificate of title, even though no certificate of title has issued. Former Section 9-103(2)(b) [30-9-103(2)(b), now repealed] provided that the law of the jurisdiction issuing the certificate ceases to apply upon "surrender" of the certificate. This Article [Title 30, chapter 9A] eliminates the concept of "surrender." However, if the certificate is surrendered in conjunction with an appropriate application for a certificate to be issued by another jurisdiction, the law of the original jurisdiction ceases to apply because the goods became covered subsequently by a certificate of title from another jurisdiction. Alternatively, the law of the original jurisdiction ceases to apply when the certificate "ceases to be effective" under the law of that jurisdiction. Given the diversity in certificate-of-title statutes, the term "effective" is not defined.

4. **Continued Perfection.** The fact that the law of one State ceases to apply under subsection (b) [subsection (2)] does not mean that a security interest perfected under that law becomes unperfected automatically. In most cases, the security interest will remain perfected. See Section 9-316(d), (e) [30-9A-316(4) and (5)]. Moreover, a perfected security interest may be subject to defeat by certain buyers and secured parties. See Section 9-337 [30-9A-337].

5. **Inventory.** Compliance with a certificate-of-title statute generally is not the method of perfecting security interests in inventory. Section 9-311(d) [30-9A-311(4)] provides that a security interest created in inventory held by a person in the business of selling or leasing goods of that kind is subject to the normal filing rules; compliance with a certificate-of-title statute is not necessary or effective to perfect the security interest. Most certificate-of-title statutes are in accord.

The following example explains the subtle relationship between this rule and the choice-of-law rules in Section 9-303 [30-9A-303] and former Section 9-103(2) [30-9-103(2), now repealed]:

Example: Goods are located in State A and covered by a certificate of title issued under the law of State A. The State A certificate of title is "clean"; it does not reflect a security interest. Owner takes the goods to State B and sells (trades in) the goods to Dealer, who is located (within the meaning of Section 9-307 [30-9A-307]) in State B. As is customary, Dealer retains the duly assigned State A certificate of title pending resale of the goods. Dealer's inventory financer, SP, obtains a security interest in the goods under its after-acquired property clause.

Under Section 9-311(d) [30-9A-311(4)] of both State A and State B, Dealer's inventory financer, SP, must perfect by filing instead of complying with a certificate-of-title statute. If Section 9-303 [30-9A-303] were read to provide that the law applicable to perfection of SP's security interest is that of State A, because the goods are covered by a State A certificate, then SP would be required to file in State A under State A's Section 9-501 [30-9A-501]. That result would be anomalous, to say the least, since the principle underlying Section 9-311(d) [30-9A-311(4)] is that the inventory should be treated as ordinary goods.

Section 9-303 [30-9A-303] (and former Section 9-103(2) [30-9-103(2), now repealed, see 30-9A-316, 30-9A-337, and this section]) should be read as providing that the law of State B, not State A, applies. A court looking to the forum's Section 9-303(a) [30-9A-303(1)] would find that Section 9-303 [30-9A-303] applies only if two conditions are met: (i) the goods are covered by the certificate as explained in Section 9-303(b) [30-9A-303(2)], i.e., application had been made for a State (here, State A) to issue a certificate of title covering the goods and (ii) the certificate is a "certificate of title" as defined in Section 9-102 [30-9A-102], i.e., "a statute provides for the security interest in question to be indicated on the certificate as a condition or result of the security interest's obtaining priority over the rights of a lien creditor." Stated otherwise, Section 9-303 [30-9A-303] applies only when compliance with a certificate-of-title statute, and not filing, is the appropriate method of perfection. Under the law of State A, for purposes of perfecting SP's security interest in the dealer's inventory, the proper method of perfection is filing-not compliance with State A's certificate-of-title statute. For that reason, the goods are not covered by a "certificate of title," and the second condition is not met. Thus, Section 9-303 [30-9A-303] does not apply to the goods. Instead, Section 9-301 [30-9A-301] applies, and the applicable law is that of State B, where the debtor (dealer) is located.

6. **External Constraints on This Section.** The need to coordinate Article 9 [Title 30, chapter 9A] with a variety of nonuniform certificate-of-title statutes, the need to provide rules to take account of situations in which multiple certificates of title are outstanding with respect to particular goods, and the need to govern the transition from perfection by filing in one jurisdiction to perfection by notation in another all create pressure for a detailed and complex set of rules. In an effort to minimize complexity, this Article [Title 30, chapter 9A] does not attempt to coordinate Article 9 [Title 30, chapter 9A] with the entire array of certificate-of-title statutes. In particular, Sections 9-303, 9-311, and 9-316(d) and (e) [30-9A-303, 30-9A-311, and 30-9A-316(4) and (5)] assume that the certificate-of-title statutes to which they apply do not have relation-back provisions (i.e., provisions under which perfection is deemed to occur at a time earlier than when the perfection steps actually are taken). A Legislative Note to Section 9-311 [30-9A-311] recommends the elimination of relation-back provisions in certificate-of-title statutes affecting perfection of security interests.

Ideally, at any given time, only one certificate of title is outstanding with respect to particular goods. In fact, however, sometimes more than one jurisdiction issues more than one certificate of title with respect to the same goods. This situation results from defects in certificate-of-title laws and the interstate coordination of those laws, not from deficiencies in this Article [Title 30, chapter 9A]. As long as the possibility of multiple certificates of title remains, the potential for innocent parties to suffer losses will continue. At best, this Article [Title 30, chapter 9A] can identify clearly which innocent parties will bear the losses in familiar fact patterns.

Case Notes

Failure to Demonstrate That Equitable Interest in Cattle Sold Displaced Perfected Security Interest in Cattle as After-Acquired Property: Bellanger obtained loans from the Daniels-Sheridan Federal Credit Union to finance a ranching operation, securing the loans with several promissory notes securing an interest in the cattle on the ranch. Bellanger subsequently defaulted on the loans, and the credit union initiated an action to enforce the promissory notes pursuant to the Uniform Commercial Code (U.C.C.). The case broadened to encompass disputes over proceeds from the sale of the cattle to include Smith, the owner of the auction company where Bellanger customarily sold cattle, whom the credit union alleged had an inferior security interest in some of the cattle that Smith had sold to Bellanger. The credit union pointed out that Smith had only an unperfected security interest because he failed to perfect a security interest pursuant to the U.C.C. Smith contended that Bellanger had obtained only a leasehold interest in the cattle and that the credit union thus had no security interest in those cattle. The cattle were subsequently seized and sold for $79,012.27, and the District Court split the proceeds, with $45,467.94 paid to the credit union and a judgment for the remainder owed on the promissory notes, and $33,544.33 paid to Smith. The credit union appealed, and the Supreme Court reversed. The District Court erred in equitably subordinating the credit union's prior perfected security interest to Smith's unperfected security interest. The Supreme Court held that Smith's transaction with Bellanger was a sale, not a lease or bailment, and as such, the hierarchy of priorities for security interests set forth in Article 9 of the U.C.C. (now Title 30, ch. 9A) applied in the credit union's favor. Smith failed to demonstrate that any equitable interest that he had in the cattle displaced the credit union's perfected security interest in the cattle as an after-acquired property of Bellanger, so an equitable carve-out from the U.C.C. principles of hierarchy priority was not justified. Daniels-Sheridan Fed. Credit Union v. Bellanger, 2001 MT 235, 307 M 22, 36 P3d 397 (2001), following Rudio v. Yellowstone Merchandising Corp., 200 M 537, 652 P2d 1163 (1982), and distinguishing NW. Potato Sales, Inc. v. Beck, 208 M 310, 678 P2d 1138 (1984), and Ninth District Prod. Credit Ass'n v. Ed Duggan, Inc., 821 P2d 788 (Colo. 1991).

30-9A-304. Law governing perfection and priority of security interests in deposit accounts.

Official Comments

1. **Source.** New; derived from Section 8-110(e) [30-8-120(5)] and former Section 9-103(6) [30-9-103(6), now repealed, see 30-9A-305, 30-9A-306, and this section].

2. **Deposit Accounts.** Under this section, the law of the "bank's jurisdiction" governs perfection and priority of a security interest in deposit accounts. Subsection (b) [subsection (2)] contains rules for determining the "bank's jurisdiction." The substance of these rules is substantially similar to that of the rules determining the "security intermediary's jurisdiction" under former Section 8-110(e) [30-8-120(5)], except that subsection (b)(1) [subsection (2)(a)] provides more flexibility than the analogous provision in former Section 8-110(e)(1) [30-8-120(5)(a)]. Subsection (b)(1) [subsection (2)(a)] permits the parties to choose the law of one jurisdiction to govern perfection and priority of security interests and a different governing law for other purposes. The parties' choice is effective, even if the jurisdiction whose law is chosen bears no relationship to the parties or the transaction. Section 8-110(e)(1) [30-8-120(5)(a)] has been conformed to subsection (b)(1) [subsection (2)(a)] of this section, and Section 9-305(b)(1) [30-9A-305(2)(a)], concerning a commodity intermediary's jurisdiction, makes a similar departure from former Section 9-103(6)(e)(i) [30-9-103(6)(e)(i), now repealed].

3. **Change in Law Governing Perfection.** When the bank's jurisdiction changes, the jurisdiction whose law governs perfection under subsection (a) [subsection (1)] changes, as well. Nevertheless, the change will not result in an immediate loss of perfection. See Section 9-316(f), (g) [30-9A-316(6) and (7)].

30-9A-305. Law governing perfection and priority of security interests in investment property.

Official Comments

1. **Source.** Former Section 9-103(6) [30-9-103(6), now repealed, see 30-9A-304, 30-9A-306, and this section].

2. **Investment Property: General Rules.** This section specifies choice-of-law rules for perfection and priority of security interests in investment property. Subsection (a)(1) [subsection (1)(a)] covers security interests in certificated securities. Subsection (a)(2) [subsection (1)(b)] covers security interests in uncertificated securities. Subsection (a)(3) [subsection (1)(c)] covers security interests in security entitlements and securities accounts. Subsection (a)(4) [subsection (1)(d)] covers security interests in commodity contracts and commodity accounts. The approach of each of these paragraphs is essentially the same. They identify the jurisdiction's law that governs questions of perfection and priority by using the same principles that Article 8 [Title 30, chapter 8] uses to determine other questions concerning that form of investment property. Thus, for certificated securities, the law of the jurisdiction in which the certificate is located governs. Cf. Section 8-110(c) [30-8-120(3)]. For uncertificated securities, the law of the issuer's jurisdiction governs. Cf. Section 8-110(a) [30-8-120(1)]. For security entitlements and securities accounts, the law of the securities intermediary's jurisdiction governs. Cf. Section 8-110(b) [30-8-120(2)]. For commodity contracts and commodity accounts, the law of the commodity intermediary's jurisdiction governs. Because commodity contracts and commodity accounts are not governed by Article 8 [Title 30, chapter 8], subsection (b) [subsection (2)] contains rules that specify the commodity intermediary's jurisdiction. These are analogous to the rules in Section 8-110(e) [30-8-120(5)] specifying a securities intermediary's jurisdiction. Subsection (b)(1) [subsection (2)(a)] affords the parties greater flexibility than did former Section 9-103(6)(3) [30-9-103(6)(c), now repealed]. See also Section 9-304(b) [30-9A-304(2)] (bank's jurisdiction); Revised Section 8-110(e)(1) [30-8-120(5)(a)] (securities intermediary's jurisdiction).

3. **Investment Property: Exceptions.** Subsection (c) [subsection (3)] establishes an exception to the general rules set out in subsection (a) [subsection (1)]. It provides that perfection of a security interest by filing, automatic perfection of a security interest in investment property created by a debtor who is a broker or securities intermediary (see Section 9-309(10) [30-9A-309(10)]), and automatic perfection of a security interest in a commodity contract or commodity account of a debtor who is a commodity intermediary (see Section 9-309(11) [30-9A-309(11)]) are governed by the law of the jurisdiction in which the debtor is located, as determined under Section 9-307 [30-9A-307].

4. **Examples:** The following examples illustrate the rules in this section:

Example 1: A customer residing in New Jersey maintains a securities account with Able & Co. The agreement between the customer and Able specifies that it is governed by Pennsylvania law but expressly provides that the law of California is Able's jurisdiction for purposes of the Uniform Commercial Code. Through the account the customer holds securities of a Massachusetts corporation, which Able holds through a clearing corporation located in New York. The customer obtains a margin loan from Able. Subsection (a)(3) [subsection (1)(c)] provides that California law-the law of the securities intermediary's jurisdiction-governs perfection and priority of the security interest, even if California has no other relationship to the parties or the transaction.

Example 2: A customer residing in New Jersey maintains a securities account with Able & Co. The agreement between the customer and Able specifies that it is governed by Pennsylvania law. Through the account the customer holds securities of a Massachusetts corporation, which Able holds through a clearing corporation located in New York. The customer obtains a loan from a lender located in Illinois. The lender takes a security interest and perfects by obtaining an agreement among the debtor, itself, and Able, which satisfies the requirement of Section 8-106(d)(2) [30-8-120(5)(b)] to give the lender control. Subsection (a)(3) [subsection (1)(c)] provides that Pennsylvania law-the law of the securities intermediary's jurisdiction-governs perfection and priority of the security interest, even if Pennsylvania has no other relationship to the parties or the transaction.

Example 3: A customer residing in New Jersey maintains a securities account with Able & Co. The agreement between the customer and Able specifies that it is governed by Pennsylvania law. Through the account, the customer holds securities of a Massachusetts corporation, which Able holds through a clearing corporation located in New York. The customer borrows from SP-1, and SP-1 files a financing statement in New Jersey. Later, the customer obtains a loan from SP-2. SP-2 takes a security interest and perfects by obtaining an agreement among the debtor, itself, and Able, which satisfies the requirement of Section 8-106(d)(2) [30-8-120(5)(b)] to give the SP-2 control. Subsection (c) [subsection (3)] provides that perfection of SP-1's security interest by filing is governed by the location of the debtor, so the filing in New Jersey was appropriate. Subsection (a)(3) [subsection (1)(c)], however, provides that Pennsylvania law-the law of the securities intermediary's jurisdiction-governs all other questions of perfection and priority. Thus, Pennsylvania law governs perfection of SP-2's security interest, and Pennsylvania law also governs the priority of the security interests of SP-1 and SP-2.

5. **Change in Law Governing Perfection.** When the issuer's jurisdiction, the securities intermediary's jurisdiction, or commodity intermediary's jurisdiction changes, the jurisdiction whose law governs perfection under subsection (a) [subsection (1)] changes, as well. Similarly, the law governing perfection of a possessory security interest in a certificated security changes when the collateral is removed to another jurisdiction, see subsection (a)(1) [subsection (1)(a)], and the law governing perfection by filing changes when the debtor changes its location. See subsection (c) [subsection (3)]. Nevertheless, these changes will not result in an immediate loss of perfection. See Section 9-316(f), (g) [30-9A-316(6), (7)].

30-9A-306. Law governing perfection and priority of security interests in letter-of-credit rights.

Official Comments

1. **Source.** New; derived in part from Section 8-110(e) [30-8-120(5)] and former Section 9-103(6) [30-9-103(6), now repealed, see 30-9A-304, 30-9A-305, and this section].

2. **Sui Generis Treatment.** This section governs the applicable law for perfection and priority of security interests in letter-of-credit rights, other than a security interest perfected only under Section 9-308(d) [30-9A-308(4)] (i.e., as a supporting obligation). The treatment differs substantially from that provided in Section 9-304 [30-9A-304] for deposit accounts. The basic rule is that the law of the issuer's or nominated person's (e.g., confirmer's) jurisdiction, derived from the terms of the letter of credit itself, controls perfection and priority, but only if the issuer's or nominated person's jurisdiction is a State, as defined in Section 9-102 [30-9A-102]. If the issuer's or nominated person's jurisdiction is not a State, the baseline rule of Section 9-301 [30-9A-301] applies-perfection and priority are governed by the law of the debtor's location, determined under Section 9-307 [30-9A-307]. Export transactions typically involve a foreign issuer and a domestic nominated person, such as a confirmer, located in a State. The principal goal of this section is to reduce the likelihood that perfection and priority would be governed by the law of a foreign jurisdiction in a transaction that is essentially domestic from the standpoint of the debtor-beneficiary, its creditors, and a domestic nominated person.

3. **Issuer's or Nominated Person's Jurisdiction.** Subsection (b) [subsection (2)] defers to the rules established under Section 5-116 [30-5-136] for determination of an issuer's or nominated person's jurisdiction.

Example: An Italian bank issues a letter of credit that is confirmed by a New York bank. The beneficiary is a Connecticut corporation. The letter of credit provides that the issuer's liability is governed by Italian law, and the confirmation provides that the confirmer's liability is governed by the law of New York. Under Sections 9-306(b) and 5-116(a) [30-9A-306(2) and 30-5-136(1)], Italy is the issuer's jurisdiction and New York is the confirmer's (nominated person's) jurisdiction. Because the confirmer's jurisdiction is a State, the law of New York governs perfection and priority of a security interest in the beneficiary's letter-of-credit right against the confirmer. See Section 9-306(a) [30-9A-306(1)]. However, because the issuer's jurisdiction is not a State, the law of that jurisdiction does not govern. See Section 9-306(a) [30-9A-306(1)]. Rather, the choice-of-law rule in Section 9-301(1) [30-9A-301(1)] applies to perfection and priority of a security interest in the beneficiary's letter-of-credit right against the issuer. Under that section, perfection and priority are governed by the law of the jurisdiction in which the debtor (beneficiary) is located. That jurisdiction is Connecticut. See Section 9-307 [30-9A-307].

4. **Scope of this Section.** This section specifies only the law governing perfection, the effect of perfection or nonperfection, and priority of security interests. Section 5-116 [30-5-136] specifies the law governing the liability of, and Article 5 [Title 30, chapter 5] (or other applicable law) deals with the rights and duties of, an issuer or nominated person. Perfection, nonperfection, and priority have no effect on those rights and duties.

5. **Change in Law Governing Perfection.** When the issuer's jurisdiction, or nominated person's jurisdiction changes, the jurisdiction whose law governs perfection under subsection (a) [subsection (1)] changes, as well. Nevertheless, this change will not result in an immediate loss of perfection. See Section 9-316(f), (g) [30-9A-316(6) and (7)].

30-9A-307. Location of debtor.

Official Comments

1. **Source.** Former Section 9-103(3)(d) [30-9-103(3)(d), now repealed], substantially revised.

2. **General Rules.** As a general matter, the location of the debtor determines the jurisdiction whose law governs perfection of a security interest. See Sections 9-301(1), 9-305(c) [30-9A-301(1) and 30-9A-305(3)]. It also governs priority of a security interest in certain types of intangible collateral, such as accounts, electronic chattel paper, and general intangibles. This section determines the location of the debtor for choice-of-law purposes, but not for other purposes. See subsection (k) [subsection (11)].

Subsection (b) [subsection (2)] states the general rules: An individual debtor is deemed to be located at the individual's principal residence with respect to both personal and business assets. Any other debtor is deemed to be located at its place of business if it has only one, or at its chief executive office if it has more than one place of business.

As used in this section, a "place of business" means a place where the debtor conducts its affairs. See subsection (a) [subsection (1)]. Thus, every organization, even eleemosynary institutions and other organizations that do not conduct "for profit" business activities, has a "place of business." Under subsection (d) [subsection (4)], a person who ceases to exist, have a residence, or have a place of business continues to be located in the jurisdiction determined by subsection (b) [subsection (2)].

The term "chief executive office" is not defined in this Section or elsewhere in the Uniform Commercial Code. "Chief executive office" means the place from which the debtor manages the main part of its business operations or other affairs. This is the place where persons dealing with the debtor would normally look for credit information, and is the appropriate place for filing. With respect to most multi-state debtors, it will be simple to determine which of the debtor's offices is the "chief executive office." Even when a doubt arises, it would be rare that there could be more than two possibilities. A secured party in such a case may protect itself by perfecting under the law of each possible jurisdiction.

Similarly, the term "principal residence" is not defined. If the security interest in question is a purchase-money security interest in consumer goods which is perfected upon attachment, see Section 9-309(1) [30-9A-309(1)], the choice of law may make no difference. In other cases, when a doubt arises, prudence may dictate perfecting under the law of each jurisdiction that might be the debtor's "principal residence."

Questions sometimes arise about the location of the debtor with respect to collateral held in a common-law trust. A typical common-law trust is not itself a juridical entity capable of owning property and so would not be a "debtor" as defined in Section 9-102 [30-9A-102]. Rather, the debtor with respect to property held in a common-law trust typically is the trustee of the trust acting in the capacity of trustee. (The beneficiary would be a "debtor" with respect to its beneficial interest in the trust, but not with respect to the property held in the trust.) If a common-law trust has multiple trustees located in different jurisdictions, a secured party who perfects by filing would be well advised to file a financing statement in each jurisdiction in which a trustee is located, as determined under Section 9-307 [30-9A-307]. Filing in all relevant jurisdictions would insure perfection and minimize any priority complications that otherwise might arise.

The general rules are subject to several exceptions, each of which is discussed below.

3. **Non-U.S. Debtors.** Under the general rules of this section, a non-U.S. debtor normally would be located in a foreign jurisdiction and, as a consequence, foreign law would govern perfection. When foreign law affords no public notice of security interests, the general rule yields unacceptable results.

Accordingly, subsection (c) [subsection (3)] provides that the normal rules for determining the location of a debtor (i.e., the rules in subsection (b) [subsection (2)]) apply only if they yield a location that is "a jurisdiction whose law generally requires information concerning the existence of a nonpossessory security interest to be made generally available in a filing, recording, or registration system as a condition or result of the security interest's obtaining priority over the rights of a lien creditor with respect to the collateral." The phrase "generally requires" is meant to include legal regimes that generally require notice in a filing or recording system as a condition of perfecting nonpossessory security interests, but which permit perfection by another method (e.g., control, automatic perfection, temporary perfection) in limited circumstances. A jurisdiction that has adopted this Article [Title 30, chapter 9A] or an earlier version of this Article [Title 30, chapter 9, now repealed] is such a jurisdiction. If the rules in subsection (b) [subsection (2)] yield a jurisdiction whose law does not generally require notice in a filing or registration system and none of the special rules in subsections (e), (f), (i), and (j) [subsections (5), (6), (9), and (10)] applies, the debtor is located in the District of Columbia.

Example 1: Debtor is an English corporation with 7 offices in the United States and its chief executive office in London, England. Debtor creates a security interest in its accounts. Under subsection (b)(3) [subsection (2)(c)], Debtor would be located in England. However, subsection (c) [subsection (3)] provides that subsection (b) [subsection (2)] applies only if English law generally conditions perfection on giving public notice in a filing, recording, or registration system. Otherwise, Debtor is located in the District of Columbia. Under Section 9-301(1) [30-9A-301(1)], perfection, the effect of perfection, and priority are governed by the law of the jurisdiction of the debtor's location-here, England or the District of Columbia (depending on the content of English law).

Example 2: Debtor is an English corporation with 7 offices in the United States and its chief executive office in London, England. Debtor creates a security interest in equipment located in London. Under subsection (b)(3) [subsection (2)(c)] Debtor would be located in England. However, subsection (c) [subsection (3)] provides that subsection (b) [subsection (2)] applies only if English law generally conditions perfection on giving public notice in a filing, recording, or registration system. Otherwise, Debtor is located in the District of Columbia. Under Section 9-301(1) [30-9A-301(1)], perfection is governed by the law of the jurisdiction of the debtor's location, whereas, under Section 9-301(3) [30-9A-301(3)], the law of the jurisdiction in which the collateral is located-here, England-governs priority.

The foregoing discussion assumes that each transaction bears an appropriate relation to the forum State. In the absence of an appropriate relation, the forum State's entire UCC, including the choice-of-law provisions in Article 9 [Title 30, chapter 9A] (Sections 9-301 through 9-307 [30-9A-301 through 30-9A-307]), will not apply. See Section 9-109 [30-9A-109], Comment 9.

4. **Registered Organizations Organized Under Law of a State.** Under subsection (e) [subsection (5)], a "registered organization" (defined in Section 9-102 [30-91-102] so as to ordinarily include corporations, limited partnerships, limited liability companies, and statutory trusts) organized under the law of a "State" (defined in Section 9-102 [30-9A-102]) is located in its State of organization. The term "registered organization" includes a business trust described in the second sentence of the term's definition. See Section 9-102 [30-9A-102]. The trust's public organic record, typically the trust agreement, usually will indicate the jurisdiction under whose law the trust is organized.

Subsection (g) [subsection (7)] makes clear that events affecting the status of a registered organization, such as the dissolution of a corporation or revocation of its charter, do not affect its location for purposes of subsection (e) [subsection (5)]. However, certain of these events may result in, or be accompanied by, a transfer of collateral from the registered organization to another debtor. This section does not determine whether a transfer occurs, nor does it determine the legal consequences of any transfer.

Determining the registered organization-debtor's location by reference to the jurisdiction of organization could provide some important side benefits for the filing systems. A jurisdiction could structure its filing system so that it would be impossible to make a mistake in a registered organization-debtor's name on a financing statement. For example, a filer would be informed if a filed record designated an incorrect corporate name for the debtor. Linking filing to the jurisdiction of organization also could reduce pressure on the system imposed by transactions in which registered organizations cease to exist-as a consequence of merger or consolidation, for example. The jurisdiction of organization might prohibit such transactions unless steps were taken to ensure that existing filings were refiled against a successor or terminated by the secured party.

5. **Registered Organizations Organized Under Law of United States; Branches and Agencies of Banks Not Organized Under Law of United States.** Subsection (f) [subsection (6)] specifies the location of a debtor that is a registered organization organized under the law of the United States. It defers to law of the United States, to the extent that that law determines, or authorizes the debtor to determine, the debtor's location. Thus, if the law of the United States designates a particular State as the debtor's location, that State is the debtor's location for purposes of this Article's [Title 30, chapter 9A] choice-of-law rules. Similarly, if the law of the United States authorizes the registered organization to designate its State of location, the State that the registered organization designates is the State in which it is located for purposes of this Article's [Title 30, chapter 9A] choice-of-law rules. In other cases, the debtor is located in the District of Columbia.

In some cases, the law of the United States authorizes the registered organization to designate a main office, home office, or other comparable office. See, e.g., 12 U.S.C. Sections 22 and 1464(a); 12 C.F.R. Section 552.3. Designation of such an office constitutes the designation of the State of location for purposes of Section 9-307 (f)(2) [30-9A-397(6)(b)].

Subsection (f) [subsection 6] also specifies the location of a branch or agency in the United States of a foreign bank that has one or more branches or agencies in the United States. The law of the United States authorizes a foreign bank (or, on behalf of the bank, a federal agency) to designate a single home state for all of the foreign bank's branches and agencies in the United States. See 12 U.S.C. Section 3103(c) and 12 C.F.R. Section 211.22. As authorized, the designation constitutes the State of location for the branch or agency for purposes of Section 9-307(f) [30-9A-307(6)], unless all of a foreign bank's branches or agencies that are in the United States are licensed in only one State, in which case the branches and agencies are located in that State. See subsection (i) [subsection 9].

In cases not governed by subsection (f) or (i) [subsection (6) or (9)], the location of a foreign bank is determined by subsections (b) and (c) [subsections (2) and (3)].

6. **United States.** To the extent that Article 9 [Title 30, chapter 9A] governs (see Sections 1-301, 9-109(c) [30-1-301, 30-9A-109(3)]), the United States is located in the District of Columbia for purposes of this Article's [Title 30, chapter 9A] choice-of-law rules. See subsection (h) [subsection (8)].

7. **Foreign Air Carriers.** Subsection (j) [subsection (10)] follows former Section 9-103(3)(d) [30-9-103(3)(d), now repealed]. To the extent that it is applicable, the Convention on the International Recognition of Rights in Aircraft (Geneva Convention) supersedes state legislation on this subject, as set forth in Section 9-311(b) [30-9A-311(2)], but some nations are not parties to that Convention.

Compiler's Comments

2013 Amendment: Chapter 75 in (6)(b) in two places inserted "branch, or agency" and at end after "location" inserted provision regarding main office, home office, or other comparable office; and made minor changes in style. Amendment effective July 1, 2013.

Saving Clause: Section 26, Ch. 75, L. 2013, provided: "(1) Except as otherwise provided in [sections 19 through 25] [Title 30, chapter 9A, part 8], this chapter applies to a transaction or lien within its scope, even if the transaction or lien was entered into or created before [the effective of this act] [July 1, 2013].

(2) This chapter does not affect an action, case, or proceeding commenced before [the effective date of this act] [July 1, 2013]."

30-9A-308. When security interest or agricultural lien is perfected — continuity of perfection.

Official Comments

[*Corresponding U.C.C Section:* Section 9-308, U.C.C.]

1. **Source.** Former Sections 9-303, 9-115(2) [30-9-303, 30-9-115(2), both now repealed, see 30-9A-203 and this section].

2. **General Rule.** This Article [Title 30, chapter 9A] uses the term "attach" to describe the point at which property becomes subject to a security interest. The requisites for attachment are stated in Section 9-203 [30-9A-203]. When it attaches, a security interest may be either perfected or unperfected. "Perfected" means that the security interest has attached and the secured party has taken all the steps required by this Article [Title 30, chapter 9A] as specified in Sections 9-310 through 9-316 [30-9A-310 through 30-9A-316]. A perfected security interest may still be or become subordinate to other interests. See, e.g., Sections 9-320, 9-322 [30-9A-320 and 30-9A-322]. However, in general, after perfection the secured party is protected against creditors and transferees of the debtor and, in particular, against any representative of creditors in insolvency proceedings instituted by or against the debtor. See, e.g., Section 9-317 [30-9A-317].

Subsection (a) [subsection (1)] explains that the time of perfection is when the security interest has attached and any necessary steps for perfection, such as taking possession or filing, have been taken. The "except" clause refers to the perfection-upon-attachment rules appearing in Section 9-309 [30-9A-309]. It also reflects that other subsections of this section, e.g., subsection (d) [subsection (4)], contain automatic-perfection rules. If the steps for perfection have been taken in advance, as when the secured party files a financing statement before giving value or before the debtor acquires rights in the collateral, then the security interest is perfected when it attaches.

3. **Agricultural Liens.** Subsection (b) [subsection (2)] is new. It describes the elements of perfection of an agricultural lien.

4. **Continuous Perfection.** The following example illustrates the operation of subsection (c) [subsection (3)]:

Example 1: Debtor, an importer, creates a security interest in goods that it imports and the documents of title that cover the goods. The secured party, Bank, takes possession of a tangible negotiable bill of lading covering certain imported goods and thereby perfects its security interest in the bill of lading and the goods. See Sections 9-313(a), 9-312(c)(1) [30-9A-313(1) and 30-9A-312(3)(a)]. Bank releases the bill of lading to the debtor for the purpose of procuring the goods from the carrier and selling them. Under Section 9-312(f) [30-9A-312(6)], Bank continues to have a perfected security interest in the document and goods for 20 days. Bank files a financing statement covering the collateral before the expiration of the 20-day period. Its security interest now continues perfected for as long as the filing is good.

If the successive stages of Bank's security interest succeed each other without an intervening gap, the security interest is "perfected continuously," and the date of perfection is when the security interest first became perfected (i.e., when Bank received possession of the tangible bill of lading). If, however, there is a gap between stages-for example, if Bank does not file until after the expiration of the 20-day period specified in Section 9-312(f) [30-9A-312(6)] and leaves the collateral in the debtor's possession-then, the chain being broken, the perfection is no longer continuous. The date of perfection would now be the date of filing (after expiration of the 20-day period). Bank's security interest would be vulnerable to any interests arising during the gap period which under Section 9-317 [30-9A-317] take priority over an unperfected security interest.

5. **Supporting Obligations.** Subsection (d) [subsection (4)] is new. It provides for automatic perfection of a security interest in a supporting obligation for collateral if the security interest in the collateral is perfected. This is unlikely to effect any change in the law prior to adoption of this Article [Title 30, chapter 9A].

Example 2: Buyer is obligated to pay Debtor for goods sold. Buyer's president guarantees the obligation. Debtor creates a security interest in the right to payment (account) in favor of Lender. Under Section 9-203(f) [30-9A-203(6)], the security interest attaches to Debtor's rights under the guarantee (supporting obligation). Under subsection (d) [subsection (4)], perfection of the security interest in the account constitutes perfection of the security interest in Debtor's rights under the guarantee.

6. **Rights to Payment Secured by Lien.** Subsection (e) [subsection (5)] is new. It deals with the situation in which a security interest is created in a right to payment that is secured by a security interest, mortgage, or other lien.

Example 3: Owner gives to Mortgagee a mortgage on Blackacre to secure a loan. Owner's obligation to pay is evidenced by a promissory note. In need of working capital, Mortgagee borrows from Financer and creates a security interest in the note in favor of Financer. Section 9-203(g) [30-9A-203(7)] adopts the traditional view that the mortgage follows the note; i.e., the transferee of the note acquires the mortgage, as well. This subsection adopts a similar principle: perfection of a security interest in the right to payment constitutes perfection of a security interest in the mortgage securing it.

An important consequence of the rules in Section 9-203(g) [30-9A-203(7)] and subsection (e) [subsection (5)] is that, by acquiring a perfected security interest in a mortgage (or other secured) note, the secured party acquires a security interest in the mortgage (or other lien) that is senior to the rights of a person who becomes a lien creditor of the mortgagee (Article 9 [Title 30, chapter 9A] debtor). See Section 9-317(a)(2) [30-9A-317(1)(b)]. This result helps prevent the separation of the mortgage (or other lien) from the note.

Under this Article [Title 30, chapter 9A], attachment and perfection of a security interest in a secured right to payment do not of themselves affect the obligation to pay. For example, if the obligation is evidenced by a negotiable note, then Article 3 [Title 30, chapter 3] dictates the person whom the maker must pay to discharge the note and any lien securing it. See Section 3-602 [30-3-601(2)]. If the right to payment is a payment intangible, then Section 9-406 [30-9A-406] determines whom the account debtor must pay.

Similarly, this Article [Title 30, chapter 9A] does not determine who has the power to release a mortgage of record. That issue is determined by real-property law.

7. **Investment Property.** Subsections (f) and (g) [subsections (6) and (7)] follow former Section 9-115(2) [30-9-115(2), now repealed, see 30-9A-203 and this section].

Case Notes

Failure to Demonstrate That Equitable Interest in Cattle Sold Displaced Perfected Security Interest in Cattle as After-Acquired Property: Bellanger obtained loans from the Daniels-Sheridan Federal Credit Union to finance a ranching operation, securing the loans with several promissory notes securing an interest in the cattle on the ranch. Bellanger subsequently defaulted on the loans, and the credit union initiated an action to enforce the promissory notes pursuant to the Uniform Commercial Code (U.C.C.). The case broadened to encompass disputes over proceeds from the sale of the cattle to include Smith, the owner of the auction company where Bellanger customarily sold cattle, whom the credit union alleged had an inferior security interest in some of the cattle that Smith had sold to Bellanger. The credit union pointed out that Smith had only an unperfected security interest because he failed to perfect a security interest pursuant to the U.C.C. Smith contended that Bellanger had obtained only a leasehold interest in the cattle and that the credit union thus had no security interest in those cattle. The cattle were subsequently seized and sold for $79,012.27, and the District Court split the proceeds, with $45,467.94 paid to the credit union and a judgment for the remainder owed on the promissory notes, and $33,544.33 paid to Smith. The credit union appealed, and the Supreme Court reversed. The District Court erred in equitably subordinating the credit union's prior perfected security interest to Smith's unperfected security interest. The Supreme Court held that Smith's transaction with Bellanger was a sale, not a lease or bailment, and as such, the hierarchy of priorities for security interests set forth in Article 9 of the U.C.C. (now Title 30, ch. 9A) applied in the credit union's favor. Smith failed to demonstrate that any equitable interest that he had in the cattle displaced the credit union's perfected security interest in the cattle as an after-acquired property of Bellanger, so an equitable carve-out from the U.C.C. principles of hierarchy priority was not justified. Daniels-Sheridan Fed. Credit Union v. Bellanger, 2001 MT 235, 307 M 22, 36 P3d 397 (2001), following Rudio v. Yellowstone Merchandising Corp., 200 M 537, 652 P2d 1163 (1982), and distinguishing NW. Potato Sales, Inc. v. Beck, 208 M 310, 678 P2d 1138 (1984), and Ninth District Prod. Credit Ass'n v. Ed Duggan, Inc., 821 P2d 788 (Colo. 1991).

30-9A-309. Security interest perfected on attachment.

Official Comments

1. **Source.** Derived from former Sections 9-302(1), 9-115(4)(c), (d), 9-116 [30-9-302(1), 30-9-115(4)(c), (4)(d), 30-9-116, all now repealed].

2. **Automatic Perfection.** This section contains the perfection-upon-attachment rules previously located in former Sections 9-302(1), 9-115(4)(c), (d), and 9-116 [30-9-302(1), 30-9-115(4)(c), (4)(d), 30-9-116, all now repealed]. Rather than continue to state the rule by indirection, this section explicitly provides for perfection upon attachment.

3. **Purchase-Money Security Interest in Consumer Goods.** Former Section 9-302(1)(d) [30-9-302(1)(d), now repealed] has been revised and appears here as paragraph (1) [subsection (1)]. No filing or other step is required to perfect a purchase-money security interest in consumer goods, other than goods, such as automobiles, that are subject to a statute or treaty described in Section 9-311(a) [30-9A-311(1)]. However, filing is required to perfect a non-purchase-money security interest in consumer goods and is necessary to prevent a buyer of consumer goods from taking free of a security interest under Section 9-320(b) [30-9A-320(2)]. A fixture filing is

required for priority over conflicting interests in fixtures to the extent provided in Section 9-334 [30-9A-334].

4. **Rights to Payment.** Paragraph (2) [subsection (2)] expands upon former Section 9-302(1)(e) [30-9-302(1)(e), now repealed] by affording automatic perfection to certain assignments of payment intangibles as well as accounts. The purpose of paragraph (2) [subsection (2)] is to save from ex post facto invalidation casual or isolated assignments-assignments which no one would think of filing. Any person who regularly takes assignments of any debtor's accounts or payment intangibles should file. In this connection Section 9-109(d)(4) through (7) [30-9A-109(4)(d) through (4)(g)], which excludes certain transfers of accounts, chattel paper, payment intangibles, and promissory notes from this Article [Title 30, chapter 9A], should be consulted.

Paragraphs (3) and (4) [subsections (3) and (4)], which are new, afford automatic perfection to sales of payment intangibles and promissory notes, respectively. They reflect the practice under former Article 9 [Title 30, chapter 9, now repealed]. Under that Article [Title 30, chapter 9, now repealed], filing a financing statement did not affect the rights of a buyer of payment intangibles or promissory notes, inasmuch as the former Article [Title 30, chapter 9, now repealed] did not cover those sales. To the extent that the exception in paragraph (2) [subsection (2)] covers outright sales of payment intangibles, which automatically are perfected under paragraph (3) [subsection (3)], the exception is redundant.

5. **Health-Care-Insurance Receivables.** Paragraph (5) [subsection (5)] extends automatic perfection to assignments of health-care-insurance receivables if the assignment is made to the health-care provider that provided the health-care goods or services. The primary effect is that, when an individual assigns a right to payment under an insurance policy to the person who provided health-care goods or services, the provider has no need to file a financing statement against the individual. The normal filing requirements apply to other assignments of health-care-insurance receivables covered by this Article [Title 30, chapter 9A], e.g., assignments from the health-care provider to a financer.

6. **Investment Property.** Paragraph (9) [subsection (9)] replaces the last clause of former Section 9-116(2) [30-9-116(2), now repealed], concerning security interests that arise in the delivery of a financial asset.

Paragraphs (10) and (11) [subsections (10) and (11)] replace former Section 9-115(4)(c) and (d) [30-9-115(4)(c) and (4)(d), now repealed], concerning secured financing of securities and commodity firms and clearing corporations. The former sections indicated that, with respect to certain security interests created by a securities intermediary or commodity intermediary, "[t]he filing of a financing statement . . . has no effect for purposes of perfection or priority with respect to that security interest." No change in meaning is intended by the deletion of the quoted phrase.

Secured financing arrangements for securities firms are currently implemented in various ways. In some circumstances, lenders may require that the transactions be structured as "hard pledges," where the securities are transferred on the books of a clearing corporation from the debtor's account to the lender's account or to a special pledge account for the lender where they cannot be disposed of without the specific consent of the lender. In other circumstances, lenders are content with so-called "agreement to pledge" or "agreement to deliver" arrangements, where the debtor retains the positions in its own account, but reflects on its books that the positions have been hypothecated and promises that the securities will be transferred to the secured party's account on demand.

The perfection and priority rules of this Article [Title 30, chapter 9A] are designed to facilitate current secured financing arrangements for securities firms as well as to provide sufficient flexibility to accommodate new arrangements that develop in the future. Hard pledge arrangements are covered by the concept of control. See Sections 9-314, 9-106, 8-106 [30-9A-314, 30-9A-106, and 30-8-116]. Non-control secured financing arrangements for securities firms are covered by the automatic perfection rule of paragraph (10) [subsection (10)]. Before the 1994 revision of Articles 8 and 9 [Title 30, chapters 8 and 9A], agreement to pledge arrangements could be implemented under a provision that a security interest in securities given for new value under a written security agreement was perfected without filing or possession for a period of 21 days. Although the security interests were temporary in legal theory, the financing arrangements could, in practice, be continued indefinitely by rolling over the loans at least every 21 days. Accordingly, a knowledgeable creditor of a securities firm realizes that the firm's securities may be subject to security interests that are not discoverable from any public records. The automatic-perfection rule of paragraph (10) [subsection (10)] makes it unnecessary to engage in the purely formal practice of rolling over these arrangements every 21 days.

In some circumstances, a clearing corporation may be the debtor in a secured financing arrangement. For example, a clearing corporation that settles delivery-versus-payment transactions among its participants on a net, same-day basis relies on timely payments from all participants with net obligations due to the system. If a participant that is a net debtor were to default on its payment obligation, the clearing corporation would not receive some of the funds needed to settle with participants that are net creditors to the system. To complete end-of-day settlement after a payment default by a participant, a clearing corporation that settles on a net, same-day basis may need to draw on credit lines and pledge securities of the defaulting participant or other securities pledged by participants in the clearing corporation to secure such drawings. The clearing corporation may be the top-tier securities intermediary for the securities pledged, so that it would not be practical for the lender to obtain control. Even where the clearing corporation holds some types of securities through other intermediaries, however, the clearing corporation is unlikely to be able to complete the arrangements necessary to convey "control" over the securities to be pledged in time to complete settlement in a timely manner. However, the term "securities intermediary" is defined in Section 8-102(a)(14) [30-8-112(1)(n)] to include clearing corporations. Thus, the perfection rule of paragraph (10) [subsection (10)] applies to security interests in investment property granted by clearing corporations.

7. **Beneficial Interests in Trusts.** Under former Section 9-302(1)(c) [30-9-302(1)(c), now repealed, see 30-9A-310 and this section], filing was not required to perfect a security interest created by an assignment of a beneficial interest in a trust. Because beneficial interests in trusts are now used as collateral with greater frequency in commercial transactions, under this Article [Title 30, chapter 9A] filing is required to perfect a security interest in a beneficial interest.

8. **Assignments for Benefit of Creditors.** No filing or other action is required to perfect an assignment for the benefit of creditors. These assignments are not financing transactions, and the debtor ordinarily will not be engaging in further credit transactions.

30-9A-310. When filing required to perfect security interest or agricultural lien — security interests and agricultural liens to which filing provisions do not apply.

Official Comments

1. **Source.** Former Section 9-302(1), (2) [30-9-302(1), (2), now repealed].

2. **General Rule.** Subsection (a) [subsection (1)] establishes a central Article 9 [Title 30, chapter 9A] principle: Filing a financing statement is necessary for perfection of security interests and agricultural liens. However, filing is not necessary to perfect a security interest that is perfected by another permissible method, see subsection (b) [subsection (2)], nor does filing ordinarily perfect a security interest in a deposit account, letter-of-credit right, or money. See Section 9-312(b) [30-9A-312(2)]. Part 5 of the Article [Title 30, chapter 9A, part 5] deals with the office in which to file, mechanics of filing, and operations of the filing office.

3. **Exemptions from Filing.** Subsection (b) [subsection (2)] lists the security interests for which filing is not required as a condition of perfection, because they are perfected automatically upon attachment (subsections (b)(2) and (b)(9) [subsections (2)(b), and (2)(i)]) or upon the occurrence of another event (subsections (b)(1), (b)(5), and (b)(9) [subsections (2)(a), (2)(e), and (2)(i)]), because they are perfected under the law of another jurisdiction (subsection (b)(10) [subsection (2)(j)]), or because they are perfected by another method, such as by the secured party's taking possession or control (subsections (b)(3), (b)(4), (b)(5), (b)(6), (b)(7), and (b)(8) [subsections (2)(c), (2)(d), (2)(e), (2)(f), (2)(g), and (2)(h)]).

4. **Assignments of Perfected Security Interests.** Subsection (c) [subsection (3)] concerns assignment of a perfected security interest or agricultural lien. It provides that no filing is necessary in connection with an assignment by a secured party to an assignee in order to maintain perfection as against creditors of and transferees from the original debtor.

Example 1: Buyer buys goods from Seller, who retains a security interest in them. After Seller perfects the security interest by filing, Seller assigns the perfected security interest to X. The security interest, in X's hands and without further steps on X's part, continues perfected against Buyer's transferees and creditors.

Example 2: Dealer creates a security interest in specific equipment in favor of Lender. After Lender perfects the security interest in the equipment by filing, Lender assigns the chattel paper (which includes the perfected security interest in Dealer's equipment) to X. The security interest in the equipment, in X's hands and without further steps on X's part, continues perfected against Dealer's transferees and creditors. However, regardless of whether Lender made the assignment to secure Lender's obligation to X or whether the assignment was an outright sale of the chattel paper, the assignment creates a security interest in the chattel paper in favor of X. Accordingly, X must take whatever steps may be required for perfection in order to be protected against Lender's transferees and creditors with respect to the chattel paper.

Subsection (c) [subsection (3)] applies not only to an assignment of a security interest perfected by filing but also to an assignment of a security interest perfected by a method other than by filing, such as by control or by possession. Although subsection (c) [subsection (3)] addresses explicitly only the absence of an additional filing requirement, the same result normally will follow in the case of an assignment of a security interest perfected by a method other than by filing. For example, as long as possession of collateral is maintained by an assignee or by the assignor or another person on behalf of the assignee, no further perfection steps need be taken on account of the assignment to continue perfection as against creditors and transferees of the original debtor. Of course, additional action may be required for perfection of the assignee's interest as against creditors and transferees of the assignor.

Similarly, subsection (c) [subsection (3)] applies to the assignment of a security interest perfected by compliance with a statute, regulation, or treaty under Section 9-311(b) [30-9A-311(2)], such as a certificate-of-title statute. Unless the statute expressly provides to the contrary, the security interest will remain perfected against creditors of and transferees from the original debtor, even if the assignee takes no action to cause the certificate of title to reflect the assignment or to cause its name to appear on the certificate of title. See PEB Commentary No. 12, which discusses this issue under former Section 9-302(3) [30-9-302(3), now repealed, see 30-9A-311]. Compliance with the statute is "equivalent to filing" under Section 9-311(b) [30-9A-311(2)].

Compiler's Comments

2005 Amendment: Chapter 575 in (2)(h) inserted "electronic document". Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

Case Notes

CASES DECIDED PRIOR TO 1999 REVISION

Business Equipment for Lease: A trencher held by a leasing business falls into none of the categories for which filing is not required. Since it is business equipment for lease, the perfection of a security interest in the trencher required filing with the Secretary of State. Between two rival security interests, one filed with the Secretary of State on June 19, 1978, and one filed initially with a County Clerk and Recorder on December 13, 1979, and subsequently filed with the Secretary of State on March 13, 1981, the former prevailed. Taylor Rental Corp. v. First Citizens Bank, 539 F. Supp. 228, 39 St. Rep. 985 (D.C. Mont. 1982).

30-9A-311. Perfection of security interests in property subject to certain statutes, regulations, and treaties.

Official Comments

1. **Source.** Former Section 9-302(3), (4) [30-9-302(3), (4), now repealed].
2. **Federal Statutes, Regulations, and Treaties.** Subsection (a)(1) [subsection (1)(a)] exempts from the filing provisions of this Article [Title 30, chapter 9A] transactions as to which a system of filing-state or federal-has been established under federal law. Subsection (b) [subsection (2)] makes clear that when such a system exists, perfection of a relevant security interest can be achieved only through compliance with that system (i.e., filing under this Article [Title 30, chapter 9A] is not a permissible alternative).

An example of the type of federal statute referred to in subsection (a)(1) [subsection (1)(a)] is 49 U.S.C. §§ 44107-11, for civil aircraft of the United States. The Assignment of Claims Act of 1940, as amended, provides for notice to contracting and disbursing officers and to sureties on bonds but does not establish a national filing system and therefore is not within the scope of subsection (a)(1) [subsection (1)(a)]. An assignee of a claim against the United States may benefit from compliance with the Assignment of Claims Act. But regardless of whether the assignee complies with that Act, the assignee must file under this Article [Title 30, chapter 9A] in order to perfect its security interest against creditors and transferees of its assignor.

Subsection (a)(1) [subsection (1)(a)] provides explicitly that the filing requirement of this Article [Title 30, chapter 9A] defers only to federal statutes, regulations, or treaties whose requirements for a security interest's obtaining priority over the rights of a lien creditor preempt Section 9-310(a) [30-9A-310(1)]. The provision eschews reference to the term "perfection," inasmuch as Section 9-308 [30-9A-308] specifies the meaning of that term and a preemptive rule may use other terminology.

3. **State Statutes.** Subsections (a)(2) and (3) [subsections (1)(b) and (1)(c)] exempt from the filing requirements of this Article [Title 30, chapter 9A] transactions covered by State certificate-of-title statutes covering motor vehicles and the like. The description of certificate-of-title statutes in subsections (a)(2) and (a)(3) [subsection (1)(b) and (1)(c)] tracks the language of the definition of "certificate of title" in Section 9-102 [30-9A-102]. For a discussion of the operation of state certificate-of-title statutes in interstate contexts, see the Comments to Section 9-303 [30-9A-303].

Some states have enacted central filing statutes with respect to secured transactions in kinds of property that are of special importance in the local economy. Subsection (a)(2) [subsection (1)(b)] defers to these statutes with respect to filing for that property.

4. **Inventory Covered by Certificate of Title.** Under subsection (d) [subsection (4)], perfection of a security interest in the inventory of a dealer is governed by the normal perfection rules, even if the inventory is covered by a certificate of title. Under former Section 9-302(3) [30-9-302(3), now repealed], a secured party who financed a dealer may have needed to perfect by filing for goods held for sale and by compliance with a certificate-of-title statute for goods held for lease. In some cases, this may have required notation on thousands of certificates. The problem would have been compounded by the fact that dealers, particularly of automobiles, often do not know whether a particular item of inventory will be sold or leased. Under subsection (d) [subsection (4)], notation is both unnecessary and ineffective.

The filing and other perfection provisions of this Article [Title 30, chapter 9A] apply to goods covered by a certificate of title only "during any period in which collateral is inventory held for sale or lease or leased." If the debtor takes goods of this kind out of inventory and uses them, say, as equipment, a filed financing statement would not remain effective to perfect a security interest.

5. **Compliance with Perfection Requirements of Other Statute.** Subsection (b) [subsection (2)] makes clear that compliance with the perfection requirements (i.e., the requirements for obtaining priority over a lien creditor), but not other requirements, of a statute, regulation, or treaty described in subsection (a) [subsection (1)] is sufficient for perfection under this Article [Title 30, chapter 9A]. Perfection of a security interest under such a statute, regulation, or treaty has all the consequences of perfection under this Article [Title 30, chapter 9A].

The interplay of this section with certain certificate-of-title statutes may create confusion and uncertainty. For example, statutes under which perfection does not occur until a certificate of title is issued will create a gap between the time that the goods are covered by the certificate under Section 9-303 [30-9A-303] and the time of perfection. If the gap is long enough, it may result in turning some unobjectionable transactions into avoidable preferences under Bankruptcy Code Section 547. (The preference risk arises if more than 30 days passes between the time a security interest attaches (or the debtor receives possession of the collateral, in the case of a purchase-money security interest) and the time it is perfected.) Accordingly, the Legislative Note to this section instructs the legislature to amend the applicable certificate-of-title statute to provide that perfection occurs upon receipt by the appropriate State official of a properly tendered application for a certificate of title on which the security interest is to be indicated.

Under some certificate-of-title statutes, including the Uniform Motor Vehicle Certificate of Title and Anti-Theft Act, perfection generally occurs upon delivery of specified documents to a state official but may, under certain circumstances, relate back to the time of attachment. This relation-back feature can create great difficulties for the application of the rules in Sections 9-303 and 9-311(b) [30-9A-303 and 30-9A-311(2)]. Accordingly, the Legislative Note also recommends to legislatures that they remove any relation-back provisions from certificate-of-title statutes affecting security interests.

6. **Compliance with Perfection Requirements of Other Statute as Equivalent to Filing.** Under Subsection (b) [subsection (2)], compliance with the perfection requirements (i.e., the requirements for obtaining priority over a lien creditor) of a statute, regulation, or treaty described in subsection (a) [subsection (1)] "is equivalent to the filing of a financing statement."

The quoted phrase appeared in former Section 9-302(3) [30-9-302(3), now repealed]. Its meaning was unclear, and many questions arose concerning the extent to which and manner in which Article 9 [Title 30, chapter 9, now repealed] rules referring to "filing" were applicable to perfection by compliance with a certificate-of-title statute. This Article [Title 30, chapter 9A] takes a variety of approaches for applying Article 9's [Title 30, chapter 9A] filing rules to compliance with other statutes and treaties. First, as discussed above in Comment 5, it leaves the determination of some rules, such as the rule establishing time of perfection (Section 9-516(a) [30-9A-516(1)]), to the other statutes themselves. Second, this Article [Title 30, chapter 9A] explicitly applies some Article 9 [Title 30, chapter 9A] filing rules to perfection under other statutes or treaties. See, e.g., Section 9-505 [30-9A-505]. Third, this Article [Title 30, chapter 9A] makes other Article 9 [Title 30, chapter 9A] rules applicable to security interests perfected by compliance with another statute through the "equivalent to . . . filing" provision in the first sentence of Section 9-311(b) [30-9A-311(2)]. The third approach is reflected for the most part in occasional Comments explaining how particular rules apply when perfection is accomplished under Section 9-311(b) [30-9A-311(2)]. See, e.g., Section 9-310 [30-9A-310], Comment 4; Section 9-315 [30-9A-315], Comment 6; Section 9-317 [30-9A-317], Comment 8. The absence of a Comment indicating that a particular filing provision applies to perfection pursuant to Section 9-311(b) [30-9A-311(2)] does not mean the provision is inapplicable.

7. **Perfection by Possession of Goods Covered by Certificate-of-Title Statute.** A secured party who holds a security interest perfected under the law of State A in goods that subsequently are covered by a State B certificate of title may face a predicament. Ordinarily, the secured party will have four months under State B's Section 9-316(c) and (d) [30-9A-316(3) and (4)] in which to (re)perfect as against a purchaser of the goods by having its security interest noted on a State B certificate. This procedure is likely to require the cooperation of the debtor and any competing secured party whose security interest has been noted on the certificate. Comment 4(e) to former Section 9-103 [30-9-103, now repealed, see 30-9A-303 and 30-9A-337] observed that "that cooperation is not likely to be forthcoming from an owner who wrongfully procured the issuance of a new certificate not showing the out-of-state security interest, or from a local secured party finding himself in a priority contest with the out-of-state secured party." According to that Comment, "[t]he only solution for the out-of-state secured party under present certificate of title statutes seems to be to reperfect by possession, i.e., by repossessing the goods." But the "solution" may not have worked: Former Section 9-302(4) [30-9-302(4), now repealed] provided that a security interest in property subject to a certificate-of-title statute "can be perfected only by compliance therewith."

Sections 9-316(d) and (e), 9-311(c), and 9-313(b) [30-9A-316(4) and (5), 30-9A-311(3), and 30-9A-313(2)] of this Article [Title 30, chapter 9A] resolve the conflict by providing that a security interest that remains perfected solely by virtue of Section 9-316(e) [30-9A-316(5)] can be (re) perfected by the secured party's taking possession of the collateral. These sections contemplate only that taking possession of goods covered by a certificate of title will work as a method of perfection. None of these sections creates a right to take possession. Section 9-609 [30-9A-609] and the agreement of the parties define the secured party's right to take possession.

Compiler's Comments

2013 Amendment: Chapter 75 in (1)(c) before "statute" deleted "certificate of title"; and made minor changes in style. Amendment effective July 1, 2013.

Saving Clause: Section 26, Ch. 75, L. 2013, provided: "(1) Except as otherwise provided in [sections 19 through 25] [Title 30, chapter 9A, part 8], this chapter applies to a transaction or lien within its scope, even if the transaction or lien was entered into or created before [the effective of this act] [July 1, 2013].

(2) This chapter does not affect an action, case, or proceeding commenced before [the effective date of this act] [July 1, 2013]."

2003 Amendment: Chapter 477 in (1)(b) substituted "certificate of title" for "certificate of ownership"; in (1)(c) near middle after "certificate" inserted "of title"; and made minor changes in style. Amendment effective January 1, 2004.

Applicability: Section 85(1), Ch. 477, L. 2003, provided that this section applies to motor vehicle certificates of title and registrations on or after January 1, 2004.

2001 Amendment: Chapter 179 near beginning of (4) after "collateral" inserted "subject to a statute specified in subsection (1)(b)", near middle after "selling" deleted "or leasing", and at end deleted "as debtor"; and made minor changes in style. Amendment effective July 1, 2001.

30-9A-312. Perfection of security interests in chattel paper, deposit accounts, documents, goods covered by documents, instruments, investment property, letter-of-credit rights, and money — perfection by permissive filing — temporary perfection without filing or transfer of possession.

Official Comments

[*Corresponding U.C.C Section:* Section 9-312, U.C.C.]

1. **Source.** Former Section 9-304 [30-9-304, now repealed], with additions and some changes.

2. **Instruments.** Under subsection (a) [subsection (1)], a security interest in instruments may be perfected by filing. This rule represents an important change from former Article 9 [Title 30, chapter 9, now repealed], under which the secured party's taking possession of an instrument was the only method of achieving long-term perfection. The rule is likely to be particularly useful in transactions involving a large number of notes that a debtor uses as collateral but continues to collect from the makers. A security interest perfected by filing is subject to defeat by certain subsequent purchasers (including secured parties). Under Section 9-330(d) [30-9A-330(4)], purchasers for value who take possession of an instrument without knowledge that the purchase violates the rights of the secured party generally would achieve priority over a security interest in the instrument perfected by filing. In addition, Section 9-331 [30-9A-331] provides that filing a financing statement does not constitute notice that would preclude a subsequent purchaser from becoming a holder in due course and taking free of all claims under Section 3-306 [30-9A-306].

3. **Chattel Paper; Negotiable Documents.** Subsection (a) [subsection (1)] further provides that filing is available as a method of perfection for security interests in chattel paper and negotiable documents. Tangible chattel paper is sometimes delivered to the assignee, and sometimes left in the hands of the assignor for collection. Subsection (a) [subsection (1)] allows the assignee to perfect its security interest by filing in the latter case. Alternatively, the assignee may perfect by taking possession. See Section 9-313(a) [30-9A-313(1)]. An assignee of electronic chattel paper may perfect by taking control. See Sections 9-314(a), 9-105 [30-9A-314(1) and 30-9A-105]. The security interest of an assignee who takes possession or control may qualify for priority over a competing security interest perfected by filing. See Section 9-330 [30-9A-330].

Negotiable documents may be, and usually are, delivered to the secured party. See Article 1, Section 1-201 [30-1-201] (definition of "delivery"). The secured party's taking possession of a tangible document or control of an electronic document will suffice as a perfection step. See Sections 9-313(a), 9-314 and 7-106 [30-9A-313(1), 30-9A-314, and 30-7-107]. However, as is the case with chattel paper, a security interest in a negotiable document may be perfected by filing.

4. **Investment Property.** A security interest in investment property, including certificated securities, uncertificated securities, security entitlements, and securities accounts, may be perfected by filing. However, security interests created by brokers, securities intermediaries, or commodity intermediaries are automatically perfected; filing is of no effect. See Section 9-309(10), (11) [30-9A-309(10) and (11)]. A security interest in all kinds of investment property also may be perfected by control, see Sections 9-314, 9-106 [30-9A-314 and 30-9A-106], and a security interest in a certificated security also may be perfected by the secured party's taking delivery under Section 8-301 [30-8-331]. See Section 9-313(a) [30-9A-313(1)]. A security interest perfected only by filing is subordinate to a conflicting security interest perfected by control or delivery. See Section 9-328(1), (5) [30-9A-328(1) and (5)]. Thus, although filing is a permissible method of perfection, a secured party who perfects by filing takes the risk that the debtor has granted or will grant a security interest in the same collateral to another party who obtains control. Also, perfection by filing would not give the secured party protection against other types of adverse claims, since the Article 8 [Title 30, chapter 8] adverse claim cut-off rules require control. See Section 8-510 [30-8-510].

5. **Deposit Accounts.** Under new subsection (b)(1) [subsection (2)(a)], the only method of perfecting a security interest in a deposit account as original collateral is by control. Filing is ineffective, except as provided in Section 9-315 [30-9A-315] with respect to proceeds. As explained in Section 9-104 [30-9A-104], "control" can arise as a result of an agreement among the secured party, debtor, and bank, whereby the bank agrees to comply with instructions of the secured party with respect to disposition of the funds on deposit, even though the debtor retains the right to direct disposition of the funds. Thus, subsection (b)(1) [subsection (2)(a)] takes an intermediate position between certain non-UCC law, which conditions the effectiveness of a security interest on the secured party's enjoyment of such dominion and control over the deposit account that the debtor is unable to dispose of the funds, and the approach this Article [Title 30, chapter 9A] takes to securities accounts, under which a secured party who is unable to reach the collateral without resort to judicial process may perfect by filing. By conditioning perfection on "control,"

rather than requiring the secured party to enjoy absolute dominion to the exclusion of the debtor, subsection (b)(1) [subsection (2)(a)] permits perfection in a wide variety of transactions, including those in which the secured party actually relies on the deposit account in extending credit and maintains some meaningful dominion over it, but does not wish to deprive the debtor of access to the funds altogether.

6. **Letter-of-Credit Rights.** Letter-of-credit rights commonly are "supporting obligations," as defined in Section 9-102 [30-9A-102]. Perfection as to the related account, chattel paper, document, general intangible, instrument, or investment property will perfect as to the letter-of-credit rights. See Section 9-308(d) [30-9A-308(4)]. Subsection (b)(2) [subsection (2)(b)] provides that, in other cases, a security interest in a letter-of-credit right may be perfected only by control. "Control," for these purposes, is explained in Section 9-107 [30-9A-107].

7. **Goods Covered by Document of Title.** Subsection (c) [subsection (3)] applies to goods in the possession of a bailee who has issued a negotiable document covering the goods. Subsection (d) [subsection (4)] applies to goods in the possession of a bailee who has issued a nonnegotiable document of title, including a document of title that is "non-negotiable" under Section 7-104 [30-7-104]. Section 9-313 [30-9A-313] governs perfection of a security interest in goods in the possession of a bailee who has not issued a document of title.

Subsection (c) [subsection (3)] clarifies the perfection and priority rules in former Section 9-304(2) [30-9-304(2), now repealed]. Consistently with the provisions of Article 7 [Title 30, chapter 7], subsection (c) [subsection (3)] takes the position that, as long as a negotiable document covering goods is outstanding, title to the goods is, so to say, locked up in the document. Accordingly, a security interest in goods covered by a negotiable document may be perfected by perfecting a security interest in the document. The security interest also may be perfected by another method, e.g., by filing. The priority rule in subsection (c) [subsection (3)] governs only priority between (i) a security interest in goods which is perfected by perfecting in the document and (ii) a security interest in the goods which becomes perfected by another method while the goods are covered by the document.

Example 1: While wheat is in a grain elevator and covered by a negotiable warehouse receipt, Debtor creates a security interest in the wheat in favor of SP-1 and SP-2. SP-1 perfects by filing a financing statement covering "wheat." Thereafter, SP-2 perfects by filing a financing statement describing the warehouse receipt. Subsection (c)(1) [subsection (3)(a)] provides that SP-2's security interest is perfected. Subsection (c)(2) [subsection (3)(b)] provides that SP-2's security interest is senior to SP-1's.

Example 2: The facts are as in Example 1, but SP-1's security interest attached and was perfected before the goods were delivered to the grain elevator. Subsection (c)(2) [subsection (3)(b)] does not apply, because SP-1's security interest did not become perfected during the time that the wheat was in the possession of a bailee. Rather, the first-to-file-or-perfect priority rule applies. See Sections 9-322 [30-9A-322] and 7-503 [30-7-503].

A secured party may become "a holder to whom a negotiable document of title has been duly negotiated" under Section 7-501 [30-7-501]. If so, the secured party acquires the rights specified by Article 7 [Title 30, chapter 7]. Article 9 [Title 30, chapter 9A] does not limit those rights, which may include the right to priority over an earlier-perfected security interest. See Section 9-331(a) [30-9A-331(1)].

Subsection (d) [subsection (4)] takes a different approach to the problem of goods covered by a nonnegotiable document. Here, title to the goods is not looked on as being locked up in the document, and the secured party may perfect its security interest directly in the goods by filing as to them. The subsection provides two other methods of perfection: issuance of the document in the secured party's name (as consignee of a straight bill of lading or the person to whom delivery would be made under a non-negotiable warehouse receipt) and receipt of notification of the secured party's interest by the bailee. Perfection under subsection (d) [subsection (4)] occurs when the bailee receives notification of the secured party's interest in the goods, regardless of who sends the notification. Receipt of notification is effective to perfect, regardless of whether the bailee responds. Unlike former Section 9-304(3) [30-9-304(3), now repealed], from which it derives, subsection (d) [subsection (4)] does not apply to goods in the possession of a bailee who has not issued a document of title. Section 9-313(c) [30-9A-313(3)] covers that case and provides that perfection by possession as to goods not covered by a document requires the bailee's acknowledgment.

8. **Temporary Perfection Without Having First Otherwise Perfected.** Subsection (e) [subsection (5)] follows former Section 9-304(4) [30-9-304(4), now repealed] in giving perfected status to security interests in certificated securities, instruments, and negotiable documents

for a short period (reduced from 21 to 20 days, which is the time period generally applicable in this Article [Title 30, chapter 9A]), although there has been no filing and the collateral is in the debtor's possession or control. The 20-day temporary perfection runs from the date of attachment. There is no limitation on the purpose for which the debtor is in possession, but the secured party must have given "new value" (defined in Section 9-102 [30-9A-102]) under an authenticated security agreement.

9. **Maintaining Perfection After Surrendering Possession.** There are a variety of legitimate reasons-many of them are described in subsections (f) and (g) [subsections (6) and (7)]-why certain types of collateral must be released temporarily to a debtor. No useful purpose would be served by cluttering the files with records of such exceedingly short term transactions.

Subsection (f) [subsection (6)] affords the possibility of 20-day perfection in negotiable documents and goods in the possession of a bailee but not covered by a negotiable document. Subsection (g) [subsection (7)] provides for 20-day perfection in certificated securities and instruments. These subsections derive from former Section 9-305(5) [30-9-305(5), now repealed, see 30-9A-313]. However, the period of temporary perfection has been reduced from 21 to 20 days, which is the time period generally applicable in this Article [Title 30, chapter 9A], and "enforcement" has been added in subsection (g) [subsection (7)] as one of the special and limited purposes for which a secured party can release an instrument or certificated security to the debtor and still remain perfected. The period of temporary perfection runs from the date a secured party who already has a perfected security interest turns over the collateral to the debtor. There is no new value requirement, but the turnover must be for one or more of the purposes stated in subsection (f) or (g) [subsection (6) or (7)]. The 20-day period may be extended by perfecting as to the collateral by another method before the period expires. However, if the security interest is not perfected by another method until after the 20-day period expires, there will be a gap during which the security interest is unperfected.

Temporary perfection extends only to the negotiable document or goods under subsection (f) [subsection (6)] and only to the certificated security or instrument under subsection (g) [subsection (7)]. It does not extend to proceeds. If the collateral is sold, the security interest will continue in the proceeds for the period specified in Section 9-315 [30-9A-315].

Subsections (f) and (g) [subsections (6) and (7)] deal only with perfection. Other sections of this Article [Title 30, chapter 9A] govern the priority of a security interest in goods after surrender of possession or control of the document covering them. In the case of a purchase-money security interest in inventory, priority may be conditioned upon giving notification to a prior inventory financer. See Section 9-324 [30-9A-324].

Compiler's Comments

2005 Amendment: Chapter 575 in (6) near beginning after "possession" inserted "or control". Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

Case Notes

Failure to Demonstrate That Equitable Interest in Cattle Sold Displaced Perfected Security Interest in Cattle as After-Acquired Property: Bellanger obtained loans from the Daniels-Sheridan Federal Credit Union to finance a ranching operation, securing the loans with several promissory notes securing an interest in the cattle on the ranch. Bellanger subsequently defaulted on the loans, and the credit union initiated an action to enforce the promissory notes pursuant to the Uniform Commercial Code (U.C.C.). The case broadened to encompass disputes over proceeds from the sale of the cattle to include Smith, the owner of the auction company where Bellanger customarily sold cattle, whom the credit union alleged had an inferior security interest in some of the cattle that Smith had sold to Bellanger. The credit union pointed out that Smith had only an unperfected security interest because he failed to perfect a security interest pursuant to the U.C.C. Smith contended that Bellanger had obtained only a leasehold interest in the cattle and that the credit union thus had no security interest in those cattle. The cattle were subsequently seized and sold for $79,012.27, and the District Court split the proceeds, with $45,467.94 paid to the credit union and a judgment for the remainder owed on the promissory notes, and $33,544.33 paid to Smith. The credit union appealed, and the Supreme Court reversed. The District Court erred in equitably subordinating the credit union's prior perfected security interest to Smith's unperfected security interest. The Supreme Court held that Smith's transaction with Bellanger was a sale, not a lease or bailment, and as such, the hierarchy of priorities for security interests set forth in Article 9 of the U.C.C. (now Title 30, ch. 9A) applied in the credit union's favor. Smith failed to demonstrate that any equitable interest that he had in the cattle displaced the credit union's perfected security interest in the cattle as an after-acquired property of Bellanger, so an equitable carve-out from the U.C.C. principles of hierarchy priority was not justified. Daniels-Sheridan Fed. Credit Union v. Bellanger, 2001 MT 235, 307 M 22, 36 P3d 397 (2001), following Rudio v. Yellowstone Merchandising Corp., 200 M 537, 652 P2d 1163 (1982), and distinguishing NW. Potato Sales, Inc. v. Beck, 208 M 310, 678 P2d 1138 (1984), and Ninth District Prod. Credit Ass'n v. Ed Duggan, Inc., 821 P2d 788 (Colo. 1991).

30-9A-313. When possession by or delivery to secured party perfects security interest without filing.

Official Comments

[*Corresponding U.C.C Section:*] Section 9-313, U.C.C.]

1. **Source.** Former Sections 9-305, 9-115(6) [30-9-305, 30-9-115(6), both now repealed].

2. **Perfection by Possession.** As under the common law of pledge, no filing is required by this Article [Title 30, chapter 9A] to perfect a security interest if the secured party takes possession of the collateral. See Section 9-310(b)(6) [30-9A-310(2)(f)].

This section permits a security interest to be perfected by the taking of possession only when the collateral is goods, instruments, tangible negotiable documents, money, or tangible chattel paper. Accounts, commercial tort claims, deposit accounts, investment property, letter-of-credit rights, letters of credit, and oil, gas, or other minerals before extraction are excluded. (But see Comment 6, below, regarding certificated securities.) A security interest in accounts and payment intangibles-property not ordinarily represented by any writing whose delivery operates to transfer the right to payment-may under this Article [Title 30, chapter 9A] be perfected only by filing. This rule would not be affected by the fact that a security agreement or other record described the assignment of such collateral as a "pledge." Section 9-309(2) [30-9A-309(2)] exempts from filing certain assignments of accounts or payment intangibles which are out of the ordinary course of financing. These exempted assignments are perfected when they attach. Similarly, under Section 9-309(3) [30-9A-309(3)], sales of payment intangibles are automatically perfected.

3. **"Possession."** This section does not define "possession." In determining whether a particular person has possession, the principles of agency apply. For example, if the collateral clearly is in possession of an agent of the secured party for the purposes of possessing on behalf of the secured party, and if the agent is not also an agent of the debtor, the secured party has taken actual possession without the need to rely on a third-party acknowledgment. See subsection (c) [subsection (3)] and Comments 4 and 8. However, if the agent is an agent of both the secured party and the debtor, prudence might suggest that the secured party obtain the agent's acknowledgment in order to ensure perfection by possession. The debtor cannot qualify as an agent for the secured party for purposes of the secured party's taking possession. And, under appropriate circumstances, a court may determine that a third person in possession is so closely connected to or controlled by the debtor that the debtor has retained effective possession, even though the third person may have agreed to take possession on behalf of the secured party. If so, the third person's taking possession would not constitute the secured party's taking possession and would not be sufficient for perfection. See also Section 9-205(b) [30-9A-205(2)]. In a typical escrow arrangement, where the escrowee holds possession of collateral as agent for both the secured party and the debtor, the debtor's relationship to the escrowee is not such as to constitute retention of possession by the debtor.

4. **Goods in Possession of Third Party: Perfection.** Former Section 9-305 [30-9-305, now repealed] permitted perfection of a security interest by notification to a bailee in possession of collateral. This Article [Title 30, chapter 9A] distinguishes between goods in the possession of a bailee who has issued a document of title covering the goods and goods in the possession of a third party who has not issued a document. Section 9-312(c) or (d) [30-9A-312(3) or (4)] applies to the former, depending on whether the document is negotiable. Section 9-313(c) [30-9A-313(3)] applies to the latter. It provides a method of perfection by possession when the collateral is possessed by a third person who is not the secured party's agent.

Notification of a third person does not suffice to perfect under Section 9-313(c) [30-9A-313(3)]. Rather, perfection does not occur unless the third person authenticates an acknowledgment that it holds possession of the collateral for the secured party's benefit. Compare Section 9-312(d) [30-9A-312(4)], under which receipt of notification of the security party's interest by a bailee holding goods covered by a nonnegotiable document is sufficient to perfect, even if the bailee does not acknowledge receipt of the notification. A third person may acknowledge that it will hold for the secured party's benefit goods to be received in the future. Under these circumstances, perfection by possession occurs when the third person obtains possession of the goods.

Under subsection (c) [subsection (3)], acknowledgment of notification by a "lessee . . . in . . . ordinary course of . . . business" (defined in Section 2A-103 [30-2A-103]) does not suffice for possession. The section thus rejects the reasoning of In re Atlantic Systems, Inc., 135 B.R. 463 (Bankr. S.D.N.Y. 1992) (holding that notification to debtor-lessor's lessee sufficed to perfect security interest in leased goods). See Steven O. Weise, Perfection by Possession: The Need for an Objective Test, 29 Idaho Law Rev. 705 (1992-93) (arguing that lessee's possession in ordinary course of debtor-lessor's business does not provide adequate public notice of possible security interest in leased goods). Inclusion of a per se rule concerning lessees is not meant to preclude a court, under appropriate circumstances, from determining that a third person is so closely connected to or controlled by the debtor that the debtor has retained effective possession. If so, the third person's acknowledgment would not be sufficient for perfection.

5. **No Relation Back.** Former Section 9-305 [30-9-305, now repealed] provided that a security interest is perfected by possession from the time possession is taken "without a relation back." As the Comment to former Section 9-305 [30-9-305, now repealed] observed, the relation-back theory, under which the taking of possession was deemed to relate back to the date of the original security agreement, has had little vitality since the 1938 revision of the Federal Bankruptcy Act. The theory is inconsistent with former Article 9 [Title 30, chapter 9, now repealed] and with this Article [Title 30, chapter 9A]. See Section 9-313(d) [30-9A-313(4)]. Accordingly, this Article [Title 30, chapter 9A] deletes the quoted phrase as unnecessary. Where a pledge transaction is contemplated, perfection dates only from the time possession is taken, although a security interest may attach, unperfected. The only exceptions to this rule are the short, 20-day periods of perfection provided in Section 9-312(e), (f), and (g) [30-9A-312(5), (6), and (7)], during which a debtor may have possession of specified collateral in which there is a perfected security interest.

6. **Certificated Securities.** The second sentence of subsection (a) [subsection (1)] reflects the traditional rule for perfection of a security interest in certificated securities. Compare Section 9-115(6) [30-9-115(6), now repealed] (1994 Official Text); Sections 8-321, 8-313(1)(a) [both now repealed] (1978 Official Text); Section 9-305 [30-9-305, now repealed] (1972 Official Text). It has been modified to refer to "delivery" under Section 8-301 [30-8-331]. Corresponding changes appear in Section 9-203(b) [30-9A-203(2)].

Subsections (e), (f), and (g) [subsections (5), (6), and (7)], which are new, apply to a person in possession of security certificates or holding security certificates for the secured party's benefit under Section 8-301 [30-8-331]. For delivery to occur when a person other than a secured party holds possession for the secured party, the person may not be a securities intermediary.

Under subsection (e) [subsection (5)], a possessory security interest in a certificated security remains perfected until the debtor obtains possession of the security certificate. This rule is analogous to that of Section 9-314(c) [30-9A-314(3)], which deals with perfection of security interests in investment property by control. See Section 9-314 [30-9A-314], Comment 3.

7. **Goods Covered by Certificate of Title.** Subsection (b) [subsection (2)] is necessary to effect changes to the choice-of-law rules governing goods covered by a certificate of title. These changes are described in the Comments to Section 9-311 [30-9A-311]. Subsection (b) [subsection (2)], like subsection (a) [subsection (1)], does not create a right to take possession. Rather, it indicates the circumstances under which the secured party's taking possession of goods covered by a certificate of title is effective to perfect a security interest in the goods: the goods become covered by a certificate of title issued by this State at a time when the security interest is perfected by any method under the law of another jurisdiction.

8. **Goods in Possession of Third Party: No Duty to Acknowledge; Consequences of Acknowledgment.** Subsections (f) and (g) [subsections (6) and (7)] are new and address matters as to which former Article 9 [Title 30, chapter 9, now repealed] was silent. They derive in part from Section 8-106(g) [30-8-116(7)]. Subsection (f) [subsection (6)] provides that a person in possession of collateral is not required to acknowledge that it holds for a secured party. Subsection (g)(1) [subsection (7)(a)] provides that an acknowledgment is effective even if wrongful as to the debtor. Subsection (g)(2) [subsection (7)(b)] makes clear that an acknowledgment does not give

rise to any duties or responsibilities under this Article [Title 30, chapter 9A]. Arrangements involving the possession of goods are hardly standardized. They include bailments for services to be performed on the goods (such as repair or processing), for use (leases), as security (pledges), for carriage, and for storage. This Article [Title 30, chapter 9A] leaves to the agreement of the parties and to any other applicable law the imposition of duties and responsibilities upon a person who acknowledges under subsection (c) [subsection (3)]. For example, by acknowledging, a third party does not become obliged to act on the secured party's direction or to remain in possession of the collateral unless it agrees to do so or other law so provides.

9. **Delivery to Third Party by Secured Party.** New subsections (h) and (i) [subsections (8) and (9)] address the practice of mortgage warehouse lenders. These lenders typically send mortgage notes to prospective purchasers under cover of letters advising the prospective purchasers that the lenders hold security interests in the notes. These lenders relied on notification to maintain perfection under former 9-305 [30-9-305, now repealed]. Requiring them to obtain authenticated acknowledgments from each prospective purchaser under subsection (c) [subsection (3)] could be unduly burdensome and disruptive of established practices. Under subsection (h) [subsection (8)], when a secured party in possession itself delivers the collateral to a third party, instructions to the third party would be sufficient to maintain perfection by possession; an acknowledgment would not be necessary. Under subsection (i) [subsection (9)], the secured party does not relinquish possession by making a delivery under subsection (h) [subsection (8)], even if the delivery violates the rights of the debtor. That subsection also makes clear that a person to whom collateral is delivered under subsection (h) [subsection (8)] does not owe any duty to the secured party and is not required to confirm the delivery to another person unless the person otherwise agrees or law other than this Article [Title 30, chapter 9A] provides otherwise.

Compiler's Comments

2005 Amendment: Chapter 575 in (1) in first sentence near middle inserted "tangible". Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-9A-314. Perfection by control.

Official Comments

[*Corresponding U.C.C. Section:* Section 9-314, U.C.C.]

1. **Source.** Substantially new; derived in part from former Section 9-115(4) [30-9-115(4), now repealed].

2. **Control.** This section provides for perfection by control with respect to investment property, deposit accounts, letter-of-credit rights, electronic chattel paper, and electronic documents. For explanations of how a secured party takes control of these types of collateral, see Sections 9-104 through 9-107 and Section 7-106 [30-9A-104 through 30-9A-107 and 30-7-107]. Subsection (b) [subsection (2)] explains when a security interest is perfected by control and how long a security interest remains perfected by control. Like Section 9-313(d) [30-9A-313(4)] and for the same reasons, subsection (b) [subsection (2)] makes no reference to the doctrine of "relation back." See Section 9-313 [30-9A-313], Comment 5. As to an electronic document that is reissued in a tangible medium, Section 7-105 [30-7-106], a secured party that is perfected by control in the electronic document should file as to the document before relinquishing control in order to maintain continuous perfection in the document. See Section 9-308 [30-9A-308].

3. **Investment Property.** Subsection (c) [subsection (3)] provides a special rule for investment property. Once a secured party has control, its security interest remains perfected by control until the secured party ceases to have control and the debtor receives possession of collateral that is a certificated security, becomes the registered owner of collateral that is an uncertificated security, or becomes the entitlement holder of collateral that is a security entitlement. The result is particularly important in the "repledge" context. See Section 9-207 [30-9A-207], Comment 5.

In a transaction in which a secured party who has control grants a security interest in investment property or sells outright the investment property, by virtue of the debtor's consent or applicable legal rules, a purchaser from the secured party typically will cut off the debtor's rights in the investment property or be immune from the debtor's claims. See Section 9-207 [30-9A-207], Comments 5 and 6. If the investment property is a security, the debtor normally would retain no interest in the security following the purchase from the secured party, and a claim of the debtor against the secured party for redemption (Section 9-623) [30-9A-623] or otherwise with respect to the security would be a purely personal claim. If the investment property transferred by the secured party is a financial asset in which the debtor had a security entitlement credited to a securities account maintained with the secured party as a securities intermediary, the debtor's claim against the secured party could arise as a part of its securities account notwithstanding its personal nature. (This claim would be analogous to a "credit balance" in the securities account, which is a component of the securities account even though it is a personal claim against the intermediary.) In the case in which the debtor may retain an interest in investment property notwithstanding a repledge or sale by the secured party, subsection (c) [subsection (3)] makes clear that the security interest will remain perfected by control.

Compiler's Comments

2005 Amendment: Chapter 575 in (1) near end inserted "30-7-107"; in (2) near middle inserted "or electronic document" and "30-7-107"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-9A-315. Secured party's rights on disposition of collateral and in proceeds.

Official Comments

1. **Source.** Former Section 9-306 [30-9-306, now repealed].

2. **Continuation of Security Interest or Agricultural Lien Following Disposition of Collateral.** Subsection (a)(1) [subsection (1)(a)], which derives from former Section 9-306(2) [30-9-306(2), now repealed], contains the general rule that a security interest survives disposition of the collateral. In these cases, the secured party may repossess the collateral from the transferee or, in an appropriate case, maintain an action for conversion. The secured party may claim both any proceeds and the original collateral but, of course, may have only one satisfaction.

In many cases, a purchaser or other transferee of collateral will take free of a security interest, and the secured party's only right will be to proceeds. For example, the general rule does not apply, and a security interest does not continue in collateral, if the secured party authorized the disposition, in the agreement that contains the security agreement or otherwise. Subsection (a)(1) [subsection (1)(a)] adopts the view of PEB Commentary No. 3 and makes explicit that the authorized disposition to which it refers is an authorized disposition "free of" the security interest or agricultural lien. The secured party's right to proceeds under this section or under the express terms of an agreement does not in itself constitute an authorization of disposition. The change in language from former Section 9-306(2) [30-9-306(2), now repealed] is not intended to address the frequently litigated situation in which the effectiveness of the secured party's consent to a disposition is conditioned upon the secured party's receipt of the proceeds. In that situation, subsection (a) [subsection (1)] leaves the determination of authorization to the courts, as under former Article 9 [Title 30, chapter 9, now repealed].

This Article [Title 30, chapter 9A] contains several provisions under which a transferee takes free of a security interest or agricultural lien. For example, Section 9-317 [30-9A-317] states when transferees take free of unperfected security interests; Sections 9-320 and 9-321 [30-9A-320 and 30-9A-321] on goods, 9-321 [30-9A-321] on general intangibles, 9-330 [30-9A-330] on chattel paper and instruments, and 9-331 [30-9A-331] on negotiable instruments, negotiable documents, and securities state when purchasers of such collateral take free of a security interest, even though perfected and even though the disposition was not authorized. Section 9-332 [30-9A-332] enables most transferees (including non-purchasers) of funds from a deposit account and most transferees of money to take free of a perfected security interest in the deposit account or money.

Likewise, the general rule that a security interest survives disposition does not apply if the secured party entrusts goods collateral to a merchant who deals in goods of that kind and the merchant sells the collateral to a buyer in ordinary course of business. Section 2-403(2) [30-2-403 (2)] gives the merchant the power to transfer all the secured party's rights to the buyer, even if the sale is wrongful as against the secured party. Thus, under subsection (a)(1) [subsection (1)(a)], an entrusting secured party runs the same risk as any other entruster.

3. **Secured Party's Right to Identifiable Proceeds.** Under subsection (a)(2) [subsection (1)(b)], which derives from former Section 9-306(2) [30-9-306(2), now repealed], a security interest attaches to any identifiable "proceeds," as defined in Section 9-102 [30-9A-102]. See also Section 9-203(f) [30-9A-203(6)]. Subsection (b) [subsection (2)] is new. It indicates when proceeds commingled with other property are identifiable proceeds and permits the use of whatever methods of tracing other law permits with respect to the type of property involved. Among the "equitable principles" whose use other law may permit is the "lowest intermediate balance rule." See Restatement (2d), Trusts § 202.

4. **Automatic Perfection in Proceeds: General Rule.** Under subsection (c) [subsection (3)], a security interest in proceeds is a perfected security interest if the security interest in the original collateral was perfected. This Article [Title 30, chapter 9A] extends the period of automatic perfection in proceeds from 10 days to 20 days. Generally, a security interest in proceeds becomes unperfected on the 21st day after the security interest attaches to the proceeds. See subsection (d) [subsection (4)]. The loss of perfected status under subsection (d) [subsection 4] is prospective only. Compare, e.g., Section 9-515(c) [30-9A-515 (3)] (deeming security interest unperfected retroactively).

5. **Automatic Perfection in Proceeds: Proceeds Acquired with Cash Proceeds.** Subsection (d)(1) [subsection (4)(a)] derives from former Section 9-306(3)(a) [30-9-306(3)(a), now repealed]. It carries forward the basic rule that a security interest in proceeds remains perfected beyond the period of automatic perfection if a filed financing statement covers the original collateral (e.g., inventory) and the proceeds are collateral in which a security interest may be perfected by filing in the office where the financing statement has been filed (e.g., equipment). A different rule applies if the proceeds are acquired with cash proceeds, as is the case if the original collateral (inventory) is sold for cash (cash proceeds) that is used to purchase equipment (proceeds). Under these circumstances, the security interest in the equipment proceeds remains perfected only if the description in the filed financing indicates the type of property constituting the proceeds (e.g., "equipment").

This section reaches the same result but takes a different approach. It recognizes that the treatment of proceeds acquired with cash proceeds under former Section 9-306(3)(a) [30-9-306(3)(a), now repealed] essentially was superfluous. In the example, had the filing covered "equipment" as well as "inventory," the security interest in the proceeds would have been perfected under the usual rules governing after-acquired equipment (see former Sections 9-302, 9-303) [30-9-302, 30-9-303, both now repealed, see 30-9A-308 through 30-9A-311]; paragraph (3)(a) [subsection (3)(a)] added only an exception to the general rule. Subsection (d)(1)(C) [subsection (4)(a)(iii)] of this section takes a more direct approach. It makes the general rule of continued perfection inapplicable to proceeds acquired with cash proceeds, leaving perfection of a security interest in those proceeds to the generally applicable perfection rules under subsection (d)(3) [subsection (4)(c)].

Example 1: Lender perfects a security interest in Debtor's inventory by filing a financing statement covering "inventory." Debtor sells the inventory and deposits the buyer's check into a deposit account. Debtor draws a check on the deposit account and uses it to pay for equipment. Under the "lowest intermediate balance rule," which is a permitted method of tracing in the relevant jurisdiction, see Comment 3, the funds used to pay for the equipment were identifiable proceeds of the inventory. Because the proceeds (equipment) were acquired with cash proceeds (deposit account), subsection (d)(1) [subsection (4)(a)] does not extend perfection beyond the 20-day automatic period.

Example 2: Lender perfects a security interest in Debtor's inventory by filing a financing statement covering "all debtor's property." As in Example 1, Debtor sells the inventory, deposits the buyer's check into a deposit account, draws a check on the deposit account, and uses the check to pay for equipment. Under the "lowest intermediate balance rule," which is a permitted method of tracing in the relevant jurisdiction, see Comment 3, the funds used to pay for the equipment were identifiable proceeds of the inventory. Because the proceeds (equipment) were acquired with cash proceeds (deposit account), subsection (d)(1) [subsection (4)(a)] does not extend perfection beyond the 20-day automatic period. However, because the financing statement is sufficient to perfect a security interest in debtor's equipment, under subsection (d)(3) [subsection (4)(c)] the security interest in the equipment proceeds remains perfected beyond the 20-day period.

6. **Automatic Perfection in Proceeds: Lapse or Termination of Financing Statement During 20-Day Period; Perfection Under Other Statute or Treaty.** Subsection (e) [subsection (5)] provides that a security interest in proceeds perfected under subsection (d)(1) [subsection (4)(a)] ceases to be perfected when the financing statement covering the original collateral lapses or is terminated. If the lapse or termination occurs before the 21st day after the security interest attaches, however, the security interest in the proceeds remains perfected until the 21st day. Section 9-311(b) [30-9A-311(2)] provides that compliance with the perfection requirements of a statute or treaty described in Section 9-311(a) [30-9A-311(1)] "is equivalent to the filing of a financing statement." It follows that collateral subject to a security interest perfected by such compliance under Section 9-311(b) [30-9A-311(2)] is covered by a "filed financing statement" within the meaning of Section 9-315(d) and (e) [30-9A-315(4) and (5)].

7. **Automatic Perfection in Proceeds: Continuation of Perfection in Cash Proceeds.** Former Section 9-306(3)(b) [30-9-306(3)(b), now repealed] provided that if a filed financing statement covered original collateral, a security interest in identifiable cash proceeds of the collateral remained perfected beyond the ten-day period of automatic perfection. Former Section 9-306(3)(c) [not adopted in Montana] contained a similar rule with respect to identifiable cash proceeds of investment property. Subsection (d)(2) [subsection (4)(b)] extends the benefits of former Sections 9-306(3)(b) and (3)(c) [30-9-306(3)(b), now repealed] to identifiable cash proceeds of all types of original collateral in which a security interest is perfected by any method. Under subsection (d)(2) [subsection (4)(b)], if the security interest in the original collateral was perfected, a security interest in identifiable cash proceeds will remain perfected indefinitely, regardless of whether the security interest in the original collateral remains perfected. In many cases, however, a purchaser or other transferee of the cash proceeds will take free of the perfected security interest. See, e.g., Sections 9-330(d) [30-9A-330(4)] (purchaser of check), 9-331 [30-9A-331] (holder in due course of check), 9-332 [30-9A-332] (transferee of money or funds from a deposit account).

8. **Insolvency Proceedings; Returned and Repossessed Goods.** This Article [Title 30, chapter 9A] deletes former Section 9-306(4) [30-9-306(4), now repealed], which dealt with proceeds in insolvency proceedings. Except as otherwise provided by the Bankruptcy Code, the debtor's entering into bankruptcy does not affect a secured party's right to proceeds.

This Article [Title 30, chapter 9A] also deletes former Section 9-306(5) [30-9-306(5), now repealed], which dealt with returned and repossessed goods. Section 9-330 [30-9A-330], Comments 9 to 11 explain and clarify the application of priority rules to returned and repossessed goods as proceeds of chattel paper.

9. **Proceeds of Collateral Subject to Agricultural Lien.** This Article [Title 30, chapter 9A] does not determine whether a lien extends to proceeds of farm products encumbered by an agricultural lien. If, however, the proceeds are themselves farm products on which an "agricultural lien" (defined in Section 9-102 [30-9A-102]) arises under other law, then the agricultural-lien provisions of this Article [Title 30, chapter 9A] apply to the agricultural lien on the proceeds in the same way in which they would apply had the farm products not been proceeds.

Case Notes

CASES DECIDED AFTER 1999 REVISION

Secured Party Entitled to Book of Business — Contracts Analyzed — Secured Interest Survived Termination of Prior Business — Insurance Company Liable for Conversion for Taking Book of Business From Secured Party: The defendant, an exclusive insurance agent for the plaintiff insurance company, sold her business to another agent and retained an economic interest as a secured creditor in the book of business. The purchasing agent was approved by the insurance company, but the insurance company terminated the relationship when the purchasing agent falsified an insurance claim. The insurance company then parked the book of business at another insurance agency and filed a complaint in interpleader to determine the rights of the parties to a contractual termination payment that was elected by the purchasing agent. In District Court, the defendant argued that she had a right to the termination payment, ongoing commissions generated by the policies, an economic interest in the agency book of business, and proceeds under 30-9A-315, while the insurance company argued that under 30-9A-203, the security interest terminated when the insurance company made the termination payment. The District Court held that the defendant retained no security interest in the book of business sold to the purchasing agent. On appeal, the Supreme Court reversed the District Court after analyzing the terms of the contracts between the parties. The court held that the defendant's position in holding an economic interest in the book of business, having the right as a secured creditor to possess the book of business upon default of the purchasing agent, and the insurance company's unauthorized control over the book of business by excluding it from the defendant after the purchasing agent's default satisfied the liability elements of conversion. Allstate Ins. Co. v. Posnien, Inc., 2015 MT 162, 379 Mont. 398, 352 P.3d 1.

Continuation of Agricultural Lien of Farm Products After Sale, but Not on Sale Proceeds — Inchoate, Unperfected Agricultural Lien Interests Allowed: The Uniform Commercial Code (U.C.C.) leaves to other law the determination of whether an agricultural lien extends to proceeds. Montana's agricultural lien law, 71-3-901, does not extend to an agricultural supplier the right to a lien on the proceeds from the sale of liened farm products. However, a perfected agricultural lien remains attached to the collateral, even after its sale or transfer, until the secured party releases its lien. The right to judicially enforce or foreclose an agricultural lien is not lost upon sale or transfer of farm products. Stockman Bank of Mont. v. Mon-Kota, Inc., 2008 MT 74, 342 M 115, 180 P3d 1125 (2008).

Failure to Demonstrate That Equitable Interest in Cattle Sold Displaced Perfected Security Interest in Cattle as After-Acquired Property: Bellanger obtained loans from the Daniels-Sheridan Federal Credit Union to finance a ranching operation, securing the loans with several promissory notes securing an interest in the cattle on the ranch. Bellanger subsequently defaulted on the loans, and the credit union initiated an action to enforce the promissory notes pursuant to the Uniform Commercial Code (U.C.C.). The case broadened to encompass disputes over proceeds from the sale of the cattle to include Smith, the owner of the auction company where Bellanger customarily sold cattle, whom the credit union alleged had an inferior security interest in some of the cattle that Smith had sold to Bellanger. The credit union pointed out that Smith had only an unperfected security interest because he failed to perfect a security interest pursuant to the U.C.C. Smith contended that Bellanger had obtained only a leasehold interest in the cattle and that the credit union thus had no security interest in those cattle. The cattle were subsequently seized and sold for $79,012.27, and the District Court split the proceeds, with $45,467.94 paid to the credit union and a judgment for the remainder owed on the promissory notes, and $33,544.33 paid to Smith. The credit union appealed, and the Supreme Court reversed. The District Court erred in equitably subordinating the credit union's prior perfected security interest to Smith's unperfected security interest. The Supreme Court held that Smith's transaction with Bellanger was a sale, not a lease or bailment, and as such, the hierarchy of priorities for security interests set forth in Article 9 of the U.C.C. (now Title 30, ch. 9A) applied in the credit union's favor. Smith failed to demonstrate that any equitable interest that he had in the cattle displaced the credit union's perfected security interest in the cattle as an after-acquired property of Bellanger, so an equitable carve-out from the U.C.C. principles of hierarchy priority was not justified. Daniels-Sheridan Fed. Credit Union v. Bellanger, 2001 MT 235, 307 M 22, 36 P3d 397 (2001), following Rudio v. Yellowstone Merchandising Corp., 200 M 537, 652 P2d 1163 (1982), and distinguishing NW. Potato Sales, Inc. v. Beck, 208 M 310, 678 P2d 1138 (1984), and Ninth District Prod. Credit Ass'n v. Ed Duggan, Inc., 821 P2d 788 (Colo. 1991).

CASES DECIDED PRIOR TO 1999 REVISION

Giving Payoff Figure Not Considered Consent to Sale of Collateral or Extinguishment of Security Interest: A debtor contacted a lending bank to obtain a loan payoff figure, informing the bank that the loan would be paid from proceeds of the sale of collateral. Merely cooperating by giving a payoff figure did not constitute the bank's acquiescence in the sale of the collateral or extinguishment of the bank's security interest. Am. Fed. S&L Ass'n v. Madison Valley Properties, Inc., 1998 MT 93, 288 M 365, 958 P2d 57, 55 St. Rep. 366 (1998).

Promisor's Death — Bank Allowed to Offset Deposits and Credit to Promissory Notes: Promissory notes provided that if promisor died, bank could declare, without notice, the notes to be due and owing. The bank could then, without notice, offset against the notes' balances any balance standing to the deceased's credit. The proceeds from a cattle sale were not "standing to the deceased's credit" at the time of his death. However, since that money was derived directly from the sale of collateral, it also became collateral for the promissory notes. The bank's actions were supported by its security interest in proceeds from the cattle sale and its adherence to the terms of the promissory notes and the articles of co-partnership of promisor's business. NW. Bank of Lewistown v. Estate of Coppedge, 219 M 473, 713 P2d 523, 43 St. Rep. 102 (1986).

Foreclosure by Secured Party Who Is Also Escrow Agent: Plaintiff bought a photography business and executed a promissory note with defendant. As collateral he assigned stock in the business. Plaintiff sold the business to Wolfe. Wolfe was to make payments to defendant to discharge his obligations, and these payments were to be directly applied to plaintiff's obligation under the promissory note. Defendant was escrow agent. Plaintiff later signed a financing statement granting defendant a security interest in the stock held in escrow. The defendant filed the security agreement. Wolfe became delinquent in his payments, and defendant notified plaintiff his payments were therefore delinquent. A later letter was sent by certified mail to the same address advising plaintiff the stock would be sold and applied to plaintiff's past-due loan. At the sale Wolfe bought the stock for the amount due on plaintiff's note. Plaintiff claimed defendant had breached its fiduciary duty by foreclosing on the stock. The security interest became binding before the parties entered the escrow agreement. The security interest continued in the collateral notwithstanding the sale to Wolfe. Upon default defendant acted within its statutory rights to foreclose on the collateral to satisfy plaintiff's obligation. The escrow arrangement did not prevent defendant as a secured party from exercising its rights to foreclose on collateral on which the debtor defaulted. Dulan v. Mont. Nat'l Bank of Roundup, 203 M 177, 661 P2d 28, 40 St. Rep. 376 (1983), followed in Weldon v. First Citizens Bank of Billings, 259 M 305, 856 P2d 225, 50 St. Rep. 807 (1993).

Security Interest in Inventory — Subsidiary Corporation Transfers to Parent Corporation: A subsidiary corporation owed money to plaintiff under a contract by which plaintiff sold his business and took a security interest in the subsidiary's inventory to cover the balance due on the purchase price. The subsidiary's parent corporation later guaranteed a bank's loan to the subsidiary. The subsidiary defaulted on the loan, the parent paid it upon request of the bank, and the parent took over from the bank a security interest in the subsidiary's inventory, which the bank was given upon granting the loan. This security interest, both in the hands of the bank and in the hands of the parent, was secondary to plaintiff's security interest, which plaintiff had perfected. The subsidiary corporation then sold its entire inventory and placed the proceeds of the sale in the parent corporation's account. The argument that the parent corporation was not liable to plaintiff for the remainder of the purchase price of plaintiff's business because plaintiff knew of and did not object to the sale of the inventory by the subsidiary and thus waived his security interest could not stand. The parent corporation was simply a secured creditor of the subsidiary with a security interest inferior to plaintiff's. Whether or not plaintiff waived his security interest in the subsidiary's inventory has no bearing on plaintiff's right to the proceeds of the sale by the subsidiary of the subsidiary's inventory, as against competing creditors such as the parent corporation. The plaintiff had priority, to the extent of his security interest, in the proceeds of the sale of the inventory whether or not he consented to the sale. Any consent by plaintiff to the sale affected only his rights as against the purchaser of the inventory, barring him from obtaining possession from the purchaser. As against the parent corporation, the plaintiff's security interest took precedence over the parent corporation's security interest. The same person owned the parent and the subsidiary, and the parent had in fact liquidated the subsidiary and deposited the proceeds in the parent's account. This was very close to a fraudulent transaction in that plaintiff's security interest was violated. Therefore, the parent corporation was secondarily liable to the plaintiff for the balance due on the purchase of his business, the subsidiary being primarily liable. Rudio v. Yellowstone Merchandising Corp., 200 M 537, 652 P2d 1163, 39 St. Rep. 1923 (1982).

Res Judicata: Bankruptcy court's rulings that bankrupt did not exchange collateral within 12 months of petition in bankruptcy and that bankrupt did not hold legal title to property received in exchange did not preclude holder of security interest in the collateral from attempting to trace the collateral, and the holder was not liable for malicious prosecution even though it was later held that the security interest was unperfected because filed in the wrong office. 3-D Lumber Co. v. Belgrade St. Bank, 157 M 481, 487 P2d 1136 (1971).

Unperfected Security Interest: Section 30-9-306(2) (section now repealed, see this section) did not apply and holder of security interest was not allowed to trace the proceeds of collateral exchanged, where the security interest had not been perfected because it had been filed in the wrong office. Belgrade St. Bank v. Elder, 157 M 1, 482 P2d 135 (1971).

Application of Proceeds: Where debtor's liquor license had been purchased with advances from bank under security agreement, proceeds from sale of such license were to be applied first to notes secured by such security agreement, then to note secured by an attachment, and finally to other obligations, since sale contract provided that all proceeds were to be placed in escrow with bank to whom all debts were owed. Gallatin Trust & Sav. Bank v. Darrah, 153 M 228, 456 P2d 288 (1969).

30-9A-316. Effect of change in applicable law.

Official Comments

1. **Source.** Former Section 9-103(1)(d), (2)(b), (3)(e) [30-9-103(1)(d), (2)(b), (3)(e), now repealed], as modified.

2. **Continued Perfection.** Subsections (a) through (g) [subsections (1) through (7)] deal with continued perfection of security interests that have been perfected under the law of another jurisdiction. The fact that the law of a particular jurisdiction ceases to govern perfection under Sections 9-301 through 9-307 [30-9A-301 through 30-9A-307] does not necessarily mean that a security interest perfected under that law automatically becomes unperfected. To the contrary: This section generally provides that a security interest perfected under the law of one jurisdiction remains perfected for a fixed period of time (four months or one year, depending on the circumstances), even though the jurisdiction whose law governs perfection changes. However, cessation of perfection under the law of the original jurisdiction cuts short the fixed period. The four-month and one-year periods are long enough for a secured party to discover in most cases that the law of a different jurisdiction governs perfection and to reperfect (typically by filing) under the law of that jurisdiction. If a secured party properly reperfects a security interest before it becomes unperfected under subsection (a) [subsection (1)], then the security interest remains perfected continuously thereafter. See subsection (b) [subsection (2)].

Example 1: Debtor is a general partnership whose chief executive office is in Pennsylvania. Lender perfects a security interest in Debtor's equipment by filing in Pennsylvania on May 15, 2002. On April 1, 2005, without Lender's knowledge, Debtor moves its chief executive office to New Jersey. Lender's security interest remains perfected for four months after the move. See subsection (a)(2) [subsection (1)(b)].

Example 2: Debtor is a general partnership whose chief executive office is in Pennsylvania. Lender perfects a security interest in Debtor's equipment by filing in Pennsylvania on May 15, 2002. On April 1, 2007, without Lender's knowledge, Debtor moves its chief executive office to New Jersey. Lender's security interest remains perfected only through May 14, 2007, when the effectiveness of the filed financing statement lapses. See subsection (a)(1) [subsection (1)(a)]. Although, under these facts, Lender would have only a short period of time to discover that Debtor had relocated and to reperfect under New Jersey law, Lender could have protected itself by filing a continuation statement in Pennsylvania before Debtor relocated. By doing so, Lender would have prevented lapse and allowed itself the full four months to discover Debtor's new location and refile there or, if Debtor is in default, to perfect by taking possession of the equipment.

Example 3: Under the facts of Example 2, Lender files a financing statement in New Jersey before the effectiveness of the Pennsylvania financing statement lapses. Under subsection (b) [subsection (2)], Lender's security interest is continuously perfected beyond May 14, 2007, for a period determined by New Jersey's Article 9 [Title 30, chapter 9A].

Subsection (a)(3) [subsection (1)(c)] allows a one-year period in which to reperfect. The longer period is necessary, because, even with the exercise of due diligence, the secured party may be unable to discover that the collateral has been transferred to a person located in another jurisdiction. In any event, the period is cut short if the financing statement becomes ineffective under the law of the jurisdiction in which it is filed.

Example 4: Debtor is a Pennsylvania corporation. On January 1, Lender perfects a security interest in Debtor's equipment by filing in Pennsylvania. Debtor's shareholders decide to "reincorporate" in Delaware. On March 1, they form a Delaware corporation (Newcorp) into which they merge Debtor. The merger effectuates a transfer of the collateral from Debtor to Newcorp, which thereby becomes a debtor and is located in another jurisdiction. Under subsection (a)(3) [subsection (1)(c)], the security interest remains perfected for one year after the merger. If a financing statement is filed in Delaware against Newcorp within the year following the merger, then the security interest remains perfected thereafter for a period determined by Delaware's Article 9.

Note that although Newcorp is a "new debtor" as defined in Section 9-102 [30-9A-102], the application of subsection (a)(3) [subsection (1)(c)] is not limited to transferees who are new debtors. Note also that, under Section 9-507 [30-9A-507], the financing statement naming Debtor remains effective even though Newcorp has become the debtor.

Subsection (a) [subsection (1)] addresses security interests that are perfected (i.e., that have attached and as to which any required perfection step has been taken) before the debtor changes its location. Subsection (h) [subsection (8)] applies to security interests that have not attached before the location changes. See Comment 7.

3. **Retroactive Unperfection.** Subsection (b) [subsection (2)] sets forth the consequences of the failure to reperfect before perfection ceases under subsection (a) [subsection (1)]: the security interest becomes unperfected prospectively and, as against purchasers for value, including buyers and secured parties, but not as against donees or lien creditors, retroactively. The rule applies to agricultural liens, as well. See also Section 9-515 [30-9A-515] (taking the same approach with respect to lapse). Although this approach creates the potential for circular priorities, the alternative-retroactive unperfection against lien creditors-would create substantial and unjustifiable preference risks.

Example 5: Under the facts of Example 4, six months after the merger, Buyer bought from Newcorp some equipment formerly owned by Debtor. At the time of the purchase, Buyer took subject to Lender's perfected security interest, of which Buyer was unaware. See Section 9-315(a)(1) [30-9A-315(1)(a)]. However, subsection (b) [subsection (2)] provides that if Lender fails to reperfect in Delaware within a year after the merger, its security interest becomes unperfected and is deemed never to have been perfected against Buyer. Having given value and received delivery of the equipment without knowledge of the security interest and before it was perfected, Buyer would take free of the security interest. See Section 9-317(b) [30-9A-317(2)].

Example 6: Under the facts of Example 4, one month before the merger, Debtor created a security interest in certain equipment in favor of Financer, who perfected by filing in Pennsylvania. At that time, Financer's security interest is subordinate to Lender's. See Section 9-322(a)(1) [30-9A-322(1)(a)]. Financer reperfects by filing in Delaware within a year after the merger, but Lender fails to do so. Under subsection (b) [subsection (2)], Lender's security interest is deemed never to have been perfected against Financer, a purchaser for value. Consequently, under Section 9-322(a)(2) [30-9A-322(1)(b)], Financer's security interest is now senior.

Of course, the expiration of the time period specified in subsection (a) [subsection (1)] does not of itself prevent the secured party from later reperfecting under the law of the new jurisdiction. If the secured party does so, however, there will be a gap in perfection, and the secured party may lose priority as a result. Thus, in Example 6, if Lender perfects by filing in Delaware more than one year under the merger, it will have a new date of filing and perfection for purposes of Section 9-322(a)(1) [30-9A-322(1)(a)]. Financer's security interest, whose perfection dates back to the filing in Pennsylvania under subsection (b) [subsection (2)], will remain senior.

4. **Possessory Security Interests.** Subsection (c) [subsection (3)] deals with continued perfection of possessory security interests. It applies not only to security interests perfected solely by the secured party's having taken possession of the collateral. It also applies to security interests perfected by a method that includes as an element of perfection the secured party's having taken possession, such as perfection by taking delivery of a certificated security in registered form, see Section 9-313(a) [30-9A-313(1)], and perfection by obtaining control over a certificated security. See Section 9-314(a) [30-9A-314(1)].

5. **Goods Covered by Certificate of Title.** Subsections (d) and (e) [subsections (4) and (5)] address continued perfection of a security interest in goods covered by a certificate of title. The following examples explain the operation of those subsections.

Example 7: Debtor's automobile is covered by a certificate of title issued by Illinois. Lender perfects a security interest in the automobile by complying with Illinois' certificate-of-title statute. Thereafter, Debtor applies for a certificate of title in Indiana. Six months thereafter, Creditor acquires a judicial lien on the automobile. Under Section 9-303(b) [30-9A-303(2)], Illinois law ceases to govern perfection; rather, once Debtor delivers the application and applicable fee to the appropriate Indiana authority, Indiana law governs. Nevertheless, under Indiana's Section 9-316(d) [30-9A-316(4)], Lender's security interest remains perfected until it would become unperfected under Illinois law had no certificate of title been issued by Indiana. (For example, Illinois' certificate-of-title statute may provide that the surrender of an Illinois certificate of title in connection with the issuance of a certificate of title by another jurisdiction causes a security interest noted thereon to become unperfected.) If Lender's security interest remains perfected, it is senior to Creditor's judicial lien.

Example 8: Under the facts in Example 7, five months after Debtor applies for an Indiana certificate of title, Debtor sells the automobile to Buyer. Under subsection (e)(2) [subsection (5)(b)], because Lender did not reperfect within the four months after the goods became covered by the Indiana certificate of title, Lender's security interest is deemed never to have been perfected against Buyer. Under Section 9-317(b) [30-9A-317(2)], Buyer is likely to take free of the security interest. Lender could have protected itself by perfecting its security interest either under Indiana's certificate-of-title statute, see Section 9-311 [30-9A-311], or, if it had a right to do so under an agreement or Section 9-609 [30-9A-609], by taking possession of the automobile. See Section 9-313(b) [30-9A-313(2)].

The results in Examples 7 and 8 do not depend on the fact that the original perfection was achieved by notation on a certificate of title. Subsection (d) [subsection (4)] applies regardless of the method by which a security interest is perfected under the law of another jurisdiction when the goods became covered by a certificate of title from this State.

Section 9-337 [30-9A-337] affords protection to a limited class of persons buying or acquiring a security interest in the goods while a security interest is perfected under the law of another jurisdiction but after this State has issued a clean certificate of title.

6. **Deposit Accounts, Letter-of-Credit Rights, and Investment Property.** Subsections (f) and (g) [subsections (6) and (7)] address changes in the jurisdiction of a bank, issuer of an uncertificated security, issuer of or nominated person under a letter of credit, securities intermediary, and commodity intermediary. The provisions are analogous to those of subsections (a) and (b) [subsections (1) and (2)].

7. **Security Interests that Attach after Debtor Changes Location.** In contrast to subsections (a) and (b) [subsections (1) and (2)], which address security interests that are perfected (i.e., that have attached and as to which any required perfection step has been taken) before the debtor changes its location, subsection (h) [subsection (8)] addresses security interests that attach within four months after the debtor changes its location. Under subsection (h) [subsection (8)], a filed financing statement that would have been effective to perfect a security interest in the collateral if the debtor had not changed its location is effective to perfect a security interest in collateral acquired within four months after the relocation.

Example 9: Debtor, an individual whose principal residence is in Pennsylvania, grants to Lender a security interest in Debtor's existing and after-acquired inventory. Lender perfects the security interest by filing a proper financing statement in Pennsylvania on January 2, 2014. On March 31, 2014, Debtor's principal residence is relocated to New Jersey. Upon the relocation, New Jersey law governs perfection of a security interest in Debtor's inventory. See Sections 9-301, 9-307 [30-9A-301, 30-9A-307]. Under New Jersey's Section 9-316(a) [equivalent to 30-9A-316(1)], Lender's security interest in Debtor's inventory on hand at the time of the relocation remains perfected for four months thereafter. Had Debtor not relocated, the financing statement filed in Pennsylvania would have been effective to perfect Lender's security interest in inventory acquired by Debtor after March 31, 2014. Accordingly, under subsection (h) [subsection (8)], the financing statement is effective to perfect Lender's security interest in inventory that Debtor acquires within the four months after Debtor's location changed.

In Example 9, Lender's security interest in the inventory acquired within the four months after Debtor's relocation will be perfected when it attaches. It will remain perfected if, before the expiration of the four-month period, the security interest is perfected under the law of New Jersey. Otherwise, the security interest will become unperfected at the end of the four-month period and will be deemed never to have been perfected as against a purchaser for value. See subsection (h)(2) [subsection (8)(b)].

8. **Collateral Acquired by New Debtor.** Subsection (i) [subsection (9)] is similar to subsection (h) [subsection (8)]. Whereas subsection (h) [subsection (8)] addresses security interests that attach within four months after a debtor changes its location, subsection (i) [subsection (9)] addresses security interests that attach within four months after a new debtor becomes bound as debtor by a security agreement entered into by another person. Subsection (i) [subsection (9)] also addresses collateral acquired by the new debtor before it becomes bound.

Example 10: Debtor, a Pennsylvania corporation, grants to Lender a security interest in Debtor's existing and after-acquired inventory. Lender perfects the security interest by filing a proper financing statement in Pennsylvania on January 2, 2014. On March 31, 2014, Debtor merges into Survivor, a Delaware corporation. Because Survivor is located in Delaware, Delaware law governs perfection of a security interest in Survivor's inventory. See Sections 9-301, 9-307 [30-9A-301, 30-9A-307]. Under Delaware's Section 9-316(a) [equivalent to 30-9A-316(b)], Lender's security interest in the inventory that Survivor acquired from Debtor remains perfected for one year after the transfer. See Comment 2. By virtue of the merger, Survivor becomes bound as debtor by Debtor's security agreement. See Section 9-203(d) [30-9A-203(4)]. As a consequence, Lender's security interest attaches to all of Survivor's inventory under Section 9-203 [30-9A-203], and Lender's collateral now includes inventory in which Debtor never had an interest. The financing statement filed in Pennsylvania against Debtor is effective under Delaware's Section 9-316(i) [equivalent to 30-9A-316(9)] to perfect Lender's security interest in inventory that Survivor acquired before, and within the four months after, becoming bound as debtor by Debtor's security agreement. This is because the financing statement filed in Pennsylvania would have been effective to perfect Lender's security interest in this collateral had Debtor, rather than Survivor, acquired it.

If the financing statement is effective, Lender's security interest in the collateral that Survivor acquired before, and within four months after, Survivor became bound as debtor will be perfected upon attachment. It will remain perfected if, before the expiration of the four-month period, the security interest is perfected under Delaware law. Otherwise, the security interest will become unperfected at the end of the four-month period and will be deemed never to have been perfected as against a purchaser for value.

Section 9-325 [30-9A-325] contains special rules governing the priority of competing security interests in collateral that is transferred, by merger or otherwise, to a new debtor or other person who becomes a debtor with respect to the collateral. Section 9-326 [30-9A-326] contains special rules governing the priority of competing security interests in collateral acquired by a new debtor other than by transfer from the original debtor.

9. **Agricultural Liens.** This section does not apply to agricultural liens.

Example 11: Supplier holds an agricultural lien on corn. The lien arises under an Iowa statute. Supplier perfects by filing a financing statement in Iowa, where the corn is located. See Section 9-302 [30-9A-302]. Debtor stores the corn in Missouri. Assume the Iowa agricultural lien survives or an agricultural lien arises under Missouri law (matters that this Article does not govern). Once the corn is located in Missouri, Missouri becomes the jurisdiction whose law governs perfection. See Section 9-302 [30-9A-302]. Thus, the agricultural lien will not be perfected unless Supplier files a financing statement in Missouri.

Compiler's Comments

2013 Amendment: Chapter 75 in catchline substituted "Effect of" for "Continued perfection of security interest following"; in (6)(a) substituted "the security interest" for "perfection", substituted "become unperfected" for "ceased", and substituted "that jurisdiction" for "the first jurisdiction"; in (6)(b) inserted "to another jurisdiction"; inserted (8) regarding rules that apply to certain collateral; and inserted (9) regarding rules that apply when original and new debtor are in different jurisdictions. Amendment effective July 1, 2013.

Saving Clause: Section 26, Ch. 75, L. 2013, provided: "(1) Except as otherwise provided in [sections 19 through 25] [Title 30, chapter 9A, part 8], this chapter applies to a transaction or lien within its scope, even if the transaction or lien was entered into or created before [the effective of this act] [July 1, 2013].

(2) This chapter does not affect an action, case, or proceeding commenced before [the effective date of this act] [July 1, 2013]."

30-9A-317. Interests that take priority over or take free of security interest or agricultural lien.

Official Comments

[*Corresponding U.C.C. Section:* Section 9-317, U.C.C.]

1. **Source.** Former Sections 9-301, 2A-307(2) [30-9-301, now repealed, 30-2A-307(2)].

2. **Scope of This Section.** As did former Section 9-301 [30-9-301, now repealed], this section lists the classes of persons who take priority over, or take free of, an unperfected security interest. Section 9-308 [30-9A-308] explains when a security interest or agricultural lien is "perfected." A security interest that has attached (see Section 9-203 [30-9A-203]) but as to which a required perfection step has not been taken is "unperfected." Certain provisions have been moved from former Section 9-301 [30-9-301, now repealed]. The definition of "lien creditor" now appears in Section 9-102 [30-9A-102], and the rules governing priority in future advances are found in Section 9-323 [30-9A-323].

3. **Competing Security Interests.** Section 9-322 [30-9A-322] states general rules for determining priority among conflicting security interests and refers to other sections that state special rules of priority in a variety of situations. The security interests given priority under Section 9-322 [30-9A-322] and the other sections to which it refers take priority in general even over a perfected security interest. A fortiori they take priority over an unperfected security interest.

4. **Filed but Unattached Security Interest vs. Lien Creditor.** Under former Section 9-301(1)(b) [30-9-301(1)(b), now repealed], a lien creditor's rights had priority over an unperfected security interest. Perfection required attachment (former Section 9-303 [30-9-303, now repealed, see 30-9A-308]) and attachment required the giving of value (former Section 9-203 [30-9-203, now repealed, see 30-9A-203]). It followed that, if a secured party had filed a financing statement

but had not yet given value, an intervening lien creditor whose lien arose after filing but before attachment of the security interest acquired rights that are senior to those of the secured party who later gives value. This result comported with the nemo dat concept: When the security interest attached, the collateral was already subject to the judicial lien.

On the other hand, this result treated the first secured advance differently from all other advances. The special rule for future advances in former Section 9-301(4) 30-9-301(4), now repealed] (substantially reproduced in Section 9-323(b) [30-9A-323(2)]) afforded priority to a discretionary advance made by a secured party within 45 days after the lien creditor's rights arose as long as the secured party was "perfected" when the lien creditor's lien arose-i.e., as long as the advance was not the first one and an earlier advance had been made.

Subsection (a)(2) [subsection (1)(b)] revises former Section 9-301(1)(b) [30-9-301(1)(b), now repealed] and treats the first advance the same as subsequent advances. That is, a judicial lien that arises after a financing statement is filed and before the security interest attaches and becomes perfected is subordinate to all advances secured by the security interest, even the first advance, except as otherwise provided in Section 9-323(b) [30-9A-323(2)]. However, if the security interest becomes unperfected (e.g., because the effectiveness of the filed financing statement lapses) before the judicial lien arises, the security interest is subordinate. If a financing statement is filed but a security interest does not attach, then no priority contest arises. The lien creditor has the only claim to the property.

5. **Security Interest of Consignor or Receivables Buyer vs. Lien Creditor.** Section 1-201(b)(35) [30-1-201(2)(jj)] defines "security interest" to include the interest of most true consignors of goods and the interest of most buyers of certain receivables (accounts, chattel paper, payment intangibles, and promissory notes). A consignee of goods or a seller of accounts or chattel paper each is deemed to have rights in the collateral which a lien creditor may reach, as long as the competing security interest of the consignor or buyer is unperfected. This is so even though, as between the consignor and the debtor-consignee, the latter has only limited rights, and, as between the buyer and debtor-seller, the latter does not have any rights in the collateral. See Sections 9-318 [30-9A-318] (seller), 9-319 [30-9A-319] (consignee). Security interests arising from sales of payment intangibles and promissory notes are automatically perfected. See Section 9-309 [30-9A-309]. Accordingly, a subsequent judicial lien always would be subordinate to the rights of a buyer of those types of receivables.

6. **Purchasers Other Than Secured Parties.** Subsections (b), (c), and (d) [subsections (2), (3), and (4)] afford priority over an unperfected security interest to certain purchasers (other than secured parties) of collateral. They derive from former Sections 9-301(1)(c), 2A-307(2), and 9-301(d) [30-9-301(1)(c), now repealed, 30-2A-307(2), and 30-9-301(4), now repealed, see 30-9A-323]. Former Section 9-301(1)(c) and (1)(d) [30-9-301(1)(c) and (1)(d), now repealed] provided that unperfected security interests are "subordinate" to the rights of certain purchasers. But, as former Comment 9 suggested, the practical effect of subordination in this context is that the purchaser takes free of the security interest. To avoid any possible misinterpretation, subsections (b) and (d) [subsections (2) and (4)] of this section use the phrase "takes free."

Subsection (b) [subsection (2)] governs goods, as well as intangibles of the type whose transfer is effected by physical delivery of the representative piece of paper (tangible chattel paper, tangible documents, instruments, and security certificates). To obtain priority, a buyer must both give value and receive delivery of the collateral without knowledge of the existing security interest and before perfection. Even if the buyer gave value without knowledge and before perfection, the buyer would take subject to the security interest if perfection occurred before physical delivery of the collateral to the buyer. Subsection (c) [subsection (3)] contains a similar rule with respect to lessees of goods. Note that a lessee of goods in ordinary course of business takes free of all security interests created by the lessor, even if perfected. See Section 9-321 [30-9A-321].

Normally, there will be no question when a buyer of tangible chattel paper, tangible documents, instruments, or security certificates "receives delivery" of the property. See Section 1-201 [30-1-201] (defining "delivery"). However, sometimes a buyer or lessee of goods, such as complex machinery, takes delivery of the goods in stages and completes assembly at its own location. Under those circumstances, the buyer or lessee "receives delivery" within the meaning of subsections (b) and (c) [subsections (2) and (3)] when, after an inspection of the portion of the goods remaining with the seller or lessor, it would be apparent to a potential lender to the seller or lessor that another person might have an interest in the goods.

The rule of subsection (b) [subsection (2)] obviously is not appropriate where the collateral consists of intangibles and there is no representative piece of paper whose physical delivery is the only or the customary method of transfer. Therefore, with respect to such intangibles (including accounts, electronic chattel paper, electronic documents, general intangibles, and investment property other than certificated securities), subsection (d) [subsection (4)] gives priority to any buyer who gives value without knowledge, and before perfection, of the security interest. A licensee of a general intangible takes free of an unperfected security interest in the general intangible under the same circumstances. Note that a licensee of a general intangible in ordinary course of business takes rights under a nonexclusive license free of security interests created by the licensor, even if perfected. See Section 9-321 [30-9A-321].

Unless Section 9-109 [30-9A-109] excludes the transaction from this Article [Title 30, chapter 9A], a buyer of accounts, chattel paper, payment intangibles, or promissory notes is a "secured party" (defined in Section 9-102 [30-9A-102]), and subsections (b) and (d) [subsections (2) and (4)] do not determine priority of the security interest created by the sale. Rather, the priority rules generally applicable to competing security interests apply. See Section 9-322 [30-9A-322].

7. **Agricultural Liens.** Subsections (a), (b), and (c) [subsections (1), (2), and (3)] subordinate unperfected agricultural liens in the same manner in which they subordinate unperfected security interests.

8. **Purchase-Money Security Interests.** Subsection (e) [subsection (5)] derives from former Section 9-301(2) [30-9-301(2), now repealed]. It provides that, if a purchase-money security interest is perfected by filing no later than 20 days after the debtor receives delivery of the collateral, the security interest takes priority over the rights of buyers, lessees, or lien creditors which arise between the time the security interest attaches and the time of filing. Subsection (e) [subsection (5)] differs from former Section 9-301(2) [30-9-301(2), now repealed] in two significant respects. First, subsection (e) [subsection (5)] protects a purchase-money security interest against all buyers and lessees, not just against transferees in bulk. Second, subsection (e) [subsection (5)] conditions this protection on filing within 20, as opposed to ten, days after delivery.

Section 9-311(b) [30-9A-311(2)] provides that compliance with the perfection requirements of a statute or treaty described in Section 9-311(a) [30-9A-311(1)] "is equivalent to the filing of a financing statement." It follows that a person who perfects a security interest in goods covered by a certificate of title by complying with the perfection requirements of an applicable certificate-of-title statute "files a financing statement" within the meaning of subsection (e) [subsection (5)].

Compiler's Comments

2013 Amendment: Chapter 75 in (2) substituted "certificated security" for "security certificate"; and in (4) substituted "collateral" for "accounts, electronic documents, general intangibles, or investment property" and before "a certificated security" inserted "tangible chattel paper, tangible documents, goods, instruments, or". Amendment effective July 1, 2013.

Saving Clause: Section 26, Ch. 75, L. 2013, provided: "(1) Except as otherwise provided in [sections 19 through 25] [Title 30, chapter 9A, part 8], this chapter applies to a transaction or lien within its scope, even if the transaction or lien was entered into or created before [the effective of this act] [July 1, 2013].

(2) This chapter does not affect an action, case, or proceeding commenced before [the effective date of this act] [July 1, 2013]."

2005 Amendment: Chapter 575 in (2) near beginning inserted "tangible"; and in (4) near beginning inserted "electronic documents". Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

2001 Amendment: Chapter 179 in catchline before "security interest" deleted "unperfected"; at beginning of (1) substituted "security interest" for "unperfected security interest"; at beginning of (1)(b) inserted exception clause; at beginning of (1)(b)(ii) inserted "one of the conditions specified in 30-9A-203(2)(c) is met and"; and made minor changes in style. Amendment effective July 1, 2001.

30-9A-318. No interest retained in right to payment that is sold — rights and title of seller of account or chattel paper with respect to creditors and purchasers.

Official Comments

1. **Source.** New.

2. **Sellers of Accounts, Chattel Paper, Payment Intangibles, and Promissory Notes.** Section 1-201(b)(35) [30-1-201(2)(jj)] defines "security interest" to include the interest of a buyer of accounts, chattel paper, payment intangibles, or promissory notes. See also Section 9-109(a) [30-1-129(1)] and Comment 5. Subsection (a) [subsection (1)] makes explicit what was implicit, but perfectly obvious, under former Article 9 [Title 30, chapter 9, now repealed]: The fact that a sale of an account or chattel paper gives rise to a "security interest" does not imply that the seller retains an interest in the property that has been sold. To the contrary, a seller of an account or chattel paper retains no interest whatsoever in the property to the extent that it has been sold. Subsection (a) (subsection (1)] also applies to sales of payment intangibles and promissory notes, transactions that were not covered by former Article 9 [Title 30, chapter 9, now repealed]. Neither this Article [Title 30, chapter 9A] nor the definition of "security interest" in Section 1-201 [30-1-201] provides rules for distinguishing sales transactions from those that create a security interest securing an obligation.

3. **Buyers of Accounts and Chattel Paper.** Another aspect of sales of accounts and chattel paper also was implicit, and equally obvious, under former Article 9 [Title 30, chapter 9, now repealed]: If the buyer's security interest is unperfected, then for purposes of determining the rights of certain third parties, the seller (debtor) is deemed to have all rights and title that the seller sold. The seller is deemed to have these rights even though, as between the parties, it has sold all its rights to the buyer. Subsection (b) [subsection (2)] makes this explicit. As a consequence of subsection (b) [subsection (2)], if the buyer's security interest is unperfected, the seller can transfer, and the creditors of the seller can reach, the account or chattel paper as if it had not been sold.

Example: Debtor sells accounts or chattel paper to Buyer-1 and retains no interest in them. Buyer-1 does not file a financing statement. Debtor then sells the same receivables to Buyer-2. Buyer-2 files a proper financing statement. Having sold the receivables to Buyer-1, Debtor would not have any rights in the collateral so as to permit Buyer-2's security (ownership) interest to attach. Nevertheless, under this section, for purposes of determining the rights of purchasers for value from Debtor, Debtor is deemed to have the rights that Debtor sold. Accordingly, Buyer-2's security interest attaches, is perfected by the filing, and, under Section 9-322 [30-9A-322], is senior to Buyer-1's interest.

4. **Effect of Perfection.** If the security interest of a buyer of accounts or chattel paper is perfected the usual result would take effect: transferees from and creditors of the seller could not acquire an interest in the sold accounts or chattel paper. The same result would occur if payment intangibles or promissory notes were sold, inasmuch as the buyer's security interest is automatically perfected under Section 9-309 [30-9A-309].

30-9A-319. Rights and title of consignee with respect to creditors and purchasers.

Official Comments

1. **Source.** New.

2. **Consignments.** This section takes an approach to consignments similar to that taken by Section 9-318 [30-9A-318] with respect to buyers of accounts and chattel paper. Revised Section 1-201(b)(35) [30-1-201(2)(jj)] defines "security interest" to include the interest of a consignor of goods under many true consignments. Section 9-319(a) [30-9A-319(1)] provides that, for purposes of determining the rights of certain third parties, the consignee is deemed to acquire all rights and title that the consignor had, if the consignor's security interest is unperfected. The consignee acquires these rights even though, as between the parties, it purchases a limited interest in the goods (as would be the case in a true consignment, under which the consignee acquires only the interest of a bailee). As a consequence of this section, creditors of the consignee can acquire judicial liens and security interests in the goods.

Insofar as creditors of the consignee are concerned, this Article [Title 30, chapter 9A] to a considerable extent reformulates the former law, which appeared in former Sections 2-326 and 9-114 [30-2-326 and 30-9-114, now repealed], without changing the results. However, neither Article 2 [Title 30, chapter 2] nor former Article 9 [Title 30, chapter 9, now repealed] specifically addresses the rights of non-ordinary course buyers from the consignee. Former Section 9-114 [30-9-114, now repealed] contained priority rules applicable to security interests in consigned goods. Under this Article [Title 30, chapter 9A], the priority rules for purchase-money security interests in inventory apply to consignments. See Section 9-103(d) [30-9A-103(4)]. Accordingly, a special section containing priority rules for consignments no longer is needed. Section 9-317 [30-9A-317] determines whether the rights of a judicial lien creditor are senior to the interest of the consignor, Sections 9-322 and 9-324 [30-9A-322 and 30-9A-324] govern competing security interests in consigned goods, and Sections 9-317, 9-315, and 9-320 [30-9A-317, 30-9A-315, and 30-9A-320] determine whether a buyer takes free of the consignor's interest.

The following example explains the operation of this section:

Example 1: SP-1 delivers goods to Debtor in a transaction constituting a "consignment" as defined in Section 9-102 [30-9A-102]. SP-1 does not file a financing statement. Debtor then grants a security interest in the goods to SP-2. SP-2 files a proper financing statement. Assuming Debtor is a mere bailee, as in a "true" consignment, Debtor would not have any rights in the collateral (beyond those of a bailee) so as to permit SP-2's security interest to attach to any greater rights. Nevertheless, under this section, for purposes of determining the rights of Debtor's creditors, Debtor is deemed to acquire SP-1's rights. Accordingly, SP-2's security interest attaches, is perfected by the filing, and, under Section 9-322 [30-9A-322], is senior to SP-1's interest.

3. **Effect of Perfection.** Subsection (b) [subsection (2)] contains a special rule with respect to consignments that are perfected. If application of this Article [Title 30, chapter 9A] would result in the consignor having priority over a competing creditor, then other law determines the rights and title of the consignee.

Example 2: SP-1 delivers goods to Debtor in a transaction constituting a "consignment" as defined in Section 9-102 [30-9A-102]. SP-1 files a proper financing statement. Debtor then grants a security interest in the goods to SP-2. Under Section 9-322 [30-9A-322], SP-1's security interest is senior to SP-2's. Subsection (b) [subsection (2)] indicates that, for purposes of determining SP-2's rights, other law determines the rights and title of the consignee. If, for example, a consignee obtains only the special property of a bailee, then SP-2's security interest would attach only to that special property.

Example 3: SP-1 obtains a security interest in all Debtor's existing and after-acquired inventory. SP-1 perfects its security interest with a proper filing. Then SP-2 delivers goods to Debtor in a transaction constituting a "consignment" as defined in Section 9-102 [30-9A-102]. SP-2 files a proper financing statement but does not send notification to SP-1 under Section 9-324(b) [30-9A-324(2)]. Accordingly, SP-2's security interest is junior to SP-1's under Section 9-322(a) [30-9A-322(1)]. Under Section 9-319(a) [30-9A-319(1)], Debtor is deemed to have the consignor's rights and title, so that SP-1's security interest attaches to SP-2's ownership interest in the goods. Thereafter, Debtor grants a security interest in the goods to SP-3, and SP-3 perfects by filing. Because SP-2's perfected security interest is senior to SP-3's under Section 9-322(a) [30-9A-322(1)], Section 9-319(b) [30-9A-319(2)] applies: Other law determines Debtor's rights and title to the goods insofar as SP-3 is concerned, and SP-3's security interest attaches to those rights.

30-9A-320. Buyer of goods.

Official Comments

1. **Source.** Former Section 9-307 [30-9-307, now repealed].

2. **Scope of This Section.** This section states when buyers of goods take free of a security interest even though perfected. Of course, a buyer who takes free of a perfected security interest takes free of an unperfected one. Section 9-317 [30-9A-317] should be consulted to determine what purchasers, in addition to the buyers covered in this section, take free of an unperfected security interest. Article 2 [Title 30, chapter 2] states general rules on purchase of goods from a seller with defective or voidable title (Section 2-403) [30-2-403].

3. **Buyers in Ordinary Course.** Subsection (a) [subsection (1)] derives from former Section 9-307(1) [30-9-307(1), now repealed]. The definition of "buyer in ordinary course of business" in Section 1-201 [30-1-201] restricts its application to buyers "from a person, other than a pawnbroker, in the business of selling goods of that kind." Thus subsection (a) [subsection (1)] applies primarily to inventory collateral. The subsection further excludes from its operation buyers of "farm products"(defined in Section 9-102 [30-9A-102]) from a person engaged in farming operations. The buyer in ordinary course of business is defined as one who buys goods "in good faith, without knowledge that the sale violates the rights of another person and in the ordinary course." Subsection (a) [subsection (1)] provides that such a buyer takes free of a security interest, even though perfected, and even though the buyer knows the security interest exists. Reading the definition together with the rule of law results in the buyer's taking free if the buyer merely

knows that a security interest covers the goods but taking subject if the buyer knows, in addition, that the sale violates a term in an agreement with the secured party.

As did former Section 9-307(1) [30-9-307(1), now repealed], subsection (a) [subsection (1)] applies only to security interests created by the seller of the goods to the buyer in ordinary course. However, under certain circumstances a buyer in ordinary course who buys goods that were encumbered with a security interest created by a person other than the seller may take free of the security interest, as Example 2 explains. See also Comment 6, below.

Example 1: Manufacturer, who is in the business of manufacturing appliances, owns manufacturing equipment subject to a perfected security interest in favor of Lender. Manufacturer sells the equipment to Dealer, who is in the business of buying and selling used equipment. Buyer buys the equipment from Dealer. Even if Buyer qualifies as a buyer in the ordinary course of business, Buyer does not take free of Lender's security interest under subsection (a) [subsection (1)], because Dealer did not create the security interest; Manufacturer did.

Example 2: Manufacturer, who is in the business of manufacturing appliances, owns manufacturing equipment subject to a perfected security interest in favor of Lender. Manufacturer sells the equipment to Dealer, who is in the business of buying and selling used equipment. Lender learns of the sale but does nothing to assert its security interest. Buyer buys the equipment from Dealer. Inasmuch as Lender's acquiescence constitutes an "entrusting" of the goods to Dealer within the meaning of Section 2-403(3) [30-2-403(3)] Buyer takes free of Lender's security interest under Section 2-403(2) [30-2-403(2)] if Buyer qualifies as a buyer in ordinary course of business.

4. **Buyers of Farm Products.** This section does not enable a buyer of farm products to take free of a security interest created by the seller, even if the buyer is a buyer in ordinary course of business. However, a buyer of farm products may take free of a security interest under Section 1324 of the Food Security Act of 1985, 7 U.S.C. § 1631.

5. **Buyers of Consumer Goods.** Subsection (b) [subsection (2)], which derives from former Section 9-307(2) [30-9-307(2), now repealed], deals with buyers of collateral that the debtor-seller holds as "consumer goods" (defined in Section 9-102 [30-9A-102]). Under Section 9-309(1) [30-9A-309(1)], a purchase-money interest in consumer goods, except goods that are subject to a statute or treaty described in Section 9-311(a) [30-9A-311(1)] (such as automobiles that are subject to a certificate-of-title statute), is perfected automatically upon attachment. There is no need to file to perfect. Under subsection (b) [subsection (2)] a buyer of consumer goods takes free of a security interest, even though perfected, if the buyer buys (1) without knowledge of the security interest, (2) for value, (3) primarily for the buyer's own personal, family, or household purposes, and (4) before a financing statement is filed.

As to purchase money-security interests which are perfected without filing under Section 9-309(1) [30-9A-309(1)]: A secured party may file a financing statement, although filing is not required for perfection. If the secured party does file, all buyers take subject to the security interest. If the secured party does not file, a buyer who meets the qualifications stated in the preceding paragraph takes free of the security interest.

As to security interests for which a perfection step is required: This category includes all non-purchase-money security interests, and all security interests, whether or not purchase-money, in goods subject to a statute or treaty described in Section 9-311(a) [30-9A-311(1)], such as automobiles covered by a certificate-of-title statute. As long as the required perfection step has not been taken and the security interest remains unperfected, not only the buyers described in subsection (b) [subsection (2)] but also the purchasers described in Section 9-317 [30-9A-317] will take free of the security interest. After a financing statement has been filed or the perfection requirements of the applicable certificate-of-title statute have been complied with (compliance is the equivalent of filing a financing statement; see Section 9-311(b) [30-9A-311(2)]), all subsequent buyers, under the rule of subsection (b) [subsection (2)], are subject to the security interest.

The rights of a buyer under subsection (b) [subsection (2)] turn on whether a financing statement has been filed against consumer goods. Occasionally, a debtor changes his or her location after a filing is made. Subsection (c) [subsection (3)], which derives from former Section 9-103(1)(d)(iii) [30-9-103(1)(d)(iii), now repealed, see 30-9A-316], deals with the continued effectiveness of the filing under those circumstances. It adopts the rules of Sections 9-316(a) and (b) [30-9A-316(1) and (2)]. These rules are explained in the Comments to that section.

6. **Authorized Dispositions.** The limitations that subsections (a) and (b) [subsections (1) and (2)] impose on the persons who may take free of a security interest apply of course only to unauthorized sales by the debtor. If the secured party authorized the sale in an express agreement or otherwise, the buyer takes free under Section 9-315(a) [30-9A-315(1)] without regard to the limitations of this section. (That section also states the right of a secured party to

the proceeds of a sale, authorized or unauthorized.) Moreover, the buyer also takes free if the secured party waived or otherwise is precluded from asserting its security interest against the buyer. See Section 1-103 [30-1-103].

7. **Oil, Gas, and Other Minerals.** Under subsection (d) [subsection (4)], a buyer in ordinary course of business of minerals at the wellhead or minehead or after extraction takes free of a security interest created by the seller. Specifically, it provides that qualified buyers take free not only of Article 9 [Title 30, chapter 9A] security interests but also of interests "arising out of an encumbrance." As defined in Section 9-102 [30-9A-102], the term "encumbrance" means "a right, other than an ownership interest, in real property." Thus, to the extent that a mortgage encumbers minerals not only before but also after extraction, subsection (d) [subsection (4)] enables a buyer in ordinary course of the minerals to take free of the mortgage. This subsection does not, however, enable these buyers to take free of interests arising out of ownership interests in the real property. This issue is significant only in a minority of states. Several of them have adopted special statutes and nonuniform amendments to Article 9 [Title 30, chapter 9A] to provide special protections to mineral owners, whose interests often are highly fractionalized in the case of oil and gas. See Terry I. Cross, Oil and Gas Product Liens—Statutory Security Interests for Producers and Royalty Owners Under the Statutes of Kansas, New Mexico, Oklahoma, Texas and Wyoming, 50 Consumer Fin. L. Q. Rep. 418 (1996). Inasmuch as a complete resolution of the issue would require the addition of complex provisions to this Article [Title 30, chapter 9A], and there are good reasons to believe that a uniform solution would not be feasible, this Article [Title 30, chapter 9A] leaves its resolution to other legislation.

8. **Possessory Security Interests.** Subsection (e) [subsection (5)] is new. It rejects the holding of Tanbro Fabrics Corp. v. Deering Milliken, Inc., 350 N.E.2d 590 (N.Y. 1976) and, together with Section 9-317(b) [30-9A-317(2)], prevents a buyer of goods collateral from taking free of a security interest if the collateral is in the possession of the secured party. "The secured party" referred in subsection (e) [subsection (5)] is the holder of the security interest referred to in subsection (a) or (b) [subsection (1) or (2)]. Section 9-313 [30-9A-313] determines whether a secured party is in possession for purposes of this section. Under some circumstances, Section 9-313 [30-9A-313] provides that a secured party is in possession of collateral even if the collateral is in the physical possession of a third party.

Case Notes

CASES DECIDED PRIOR TO 1999 REVISION

Security Interest — Creation by Seller: Defendant does not take free of the plaintiff's security interest under 30-9-307 (now repealed, see this section) although he purchased in good faith and in the ordinary course of business because defendant's seller did not create plaintiff's security interest as required by 30-9-307 (now repealed, see this section). Exch. Bank of Osceola v. Jarrett, 180 M 33, 588 P2d 1006 (1979).

Joint Tenancy Auto Title — Effect on Default: When defendant borrowed from plaintiff on auto collateral registered in his "and/or" another's name, the plaintiff bank was entitled to sell the auto upon defendant's default and receive one-half of the proceeds even though the bank's security interest was unperfected at the time of defendant's fraudulent assignment of his interest to his sister without value. The joint tenancy interest of the defendant was severed upon his default, and the bank became tenant in common with the holder of the remaining interest in the auto. First Westside Nat'l Bank v. Llera, 176 M 481, 580 P2d 100 (1978).

30-9A-321. Licensee of general intangible and lessee of goods in ordinary course of business.

Official Comments

1. **Source.** Derived from Sections 2A-103(1)(o), 2A-307(3) [30-2A-103(1)(o), 30-2A-307(3)].

2. **Licensee in Ordinary Course.** Like the analogous rules in Section 9-320(a) [30-9A-320(1)] with respect to buyers in ordinary course and subsection (c) [subsection (3)] with respect to lessees in ordinary course, the new rule in subsection (b) [subsection (2)] reflects the expectations of the parties and the marketplace: a licensee under a nonexclusive license takes subject to a security interest unless the secured party authorizes the license free of the security interest or other, controlling law such as that of this section (protecting ordinary-course licensees) dictates a contrary result. See Sections 9-201, 9-315 [30-9A-201 and 30-9A-315]. The definition of "licensee in ordinary course of business" in subsection (a) [subsection (1)] is modeled upon that of "buyer in ordinary course of business."

3. **Lessee in Ordinary Course.** Subsection (c) [subsection (3)] contains the rule formerly found in Section 2A-307(3) [30-2A-307(3)]. The rule works in the same way as that of Section 9-320(a) [30-9A-320(1)].

30-9A-322. Priorities among conflicting security interests and agricultural liens in same collateral.

Official Comments

[*Corresponding U.C.C. Section:* Section 9-322, U.C.C.]

1. **Source.** Former Section 9-312(5), (6) [30-9-312(5), (6), now repealed].

2. **Scope of This Section.** In a variety of situations, two or more people may claim a security interest in the same collateral. This section states general rules of priority among conflicting security interests. As subsection (f) [subsection (6)] provides, the general rules in subsections (a) through (e) [subsections (1) through (5)] are subject to the rule in subsection (g) [subsection (7)] governing perfected agricultural liens and to the other rules in this Part of this Article [Title 30, chapter 9A, part 3]. Rules that override this section include those applicable to purchase-money security interests (Section 9-324) [30-9A-324] and those qualifying for special priority in particular types of collateral. See, e.g., Section 9-327 [30-9A-327] (deposit accounts); Section 9-328 [30-9A-328] (investment property); Section 9-329 [30-9A-329] (letter-of-credit rights); Section 9-330 [30-9A-330] (chattel paper and instruments); Section 9-334 [30-9A-334] (fixtures). In addition, the general rules of sections (a) through (e) [subsections (1) through (5)] are subject to priority rules governing security interests arising under Articles 2, 2A, 4, and 5 [Title 30, chapters 2, 2A, 4, and 5].

3. **General Rules.** Subsection (a) [subsection (1)] contains three general rules. Subsection (a)(1) [subsection (1)(a)] governs the priority of competing perfected security interests. Subsection (a)(2) [subsection (1)(b)] governs the priority of competing security interests if one is perfected and the other is not. Subsection (a)(3) [subsection (1)(c)] governs the priority of competing unperfected security interests. The rules may be regarded as adaptations of the idea, deeply rooted at common law, of a race of diligence among creditors. The first two rules are based on precedence in the time as of which the competing secured parties either filed their financing statements or obtained perfected security interests. Under subsection (a)(1) [subsection (1)(a)], the first secured party who files or perfects has priority. Under subsection (a)(2) [subsection (1)(b)], which is new, a perfected security interest has priority over an unperfected one. Under subsection (a)(3) [subsection (1)(c)], if both security interests are unperfected, the first to attach has priority. Note that Section 9-708(b) [30-9A-708(2)] may affect the application of subsection (a) [subsection (1)] to a filing that occurred before the effective date of this Article [July 1, 2001] and which would be ineffective to perfect a security interest under former Article 9 [Title 30, chapter 9, now repealed] but effective under this Article [Title 30, chapter 9A].

4. **Competing Perfected Security Interests.** When there is more than one perfected security interest, the security interests rank according to priority in time of filing or perfection. "Filing," of course, refers to the filing of an effective financing statement. "Perfection" refers to the acquisition of a perfected security interest, i.e., one that has attached and as to which any required perfection step has been taken. See Section 9-308 [30-9A-308].

Example 1: On February 1, A files a financing statement covering a certain item of Debtor's equipment. On March 1, B files a financing statement covering the same equipment. On April 1, B makes a loan to Debtor and obtains a security interest in the equipment. On May 1, A makes a loan to Debtor and obtains a security interest in the same collateral. A has priority even though B's loan was made earlier and was perfected when made. It makes no difference whether A knew of B's security interest when A made its advance.

The problem stated in Example 1 is peculiar to a notice-filing system under which filing may occur before the security interest attaches (see Section 9-502) [30-9A-502]. The justification for determining priority by order of filing lies in the necessity of protecting the filing system-that is, of allowing the first secured party who has filed to make subsequent advances without each time having to check for subsequent filings as a condition of protection. Note, however, that this first-to-file protection is not absolute. For example, Section 9-324 [30-9A-324] affords priority to certain purchase-money security interests, even if a competing secured party was the first to file or perfect.

Under a notice-filing system, a filed financing statement indicates to third parties that a person may have a security interest in the collateral indicated. With further inquiry, they may discover the complete state of affairs. When a financing statement that is ineffective when filed becomes effective thereafter, the policy underlying the notice-filing system determines the "time of filing" for purposes of subsection (a)(1) [subsection (1)(a)]. For example, the unauthorized filing of an otherwise sufficient initial financing statement becomes authorized, and the financing statement becomes effective, upon the debtor's post-filing authorization or ratification of the filing. See Section 9-509 [30-9A-509], Comment 3. Because the notice value of the financing statement is independent of the timing of authorization or ratification, the time of the unauthorized filing is the "time of filing" for purposes of subsection (a)(1) [subsection (1)(a)]. The same policy applies to the other priority rules in this part.

Example 2: A and B make non-purchase-money advances secured by the same collateral. The collateral is in Debtor's possession, and neither security interest is perfected when the second advance is made. Whichever secured party first perfects its security interest (by taking possession of the collateral or by filing) takes priority. It makes no difference whether that secured party knows of the other security interest at the time it perfects its own.

The rule of subsection (a)(1) [subsection (1)(a)], affording priority to the first to file or perfect, applies to security interests that are perfected by any method, including temporarily (Section 9-312) [30-9A-312] or upon attachment (Section 9-309) [30-9A-309], even though there may be no notice to creditors or subsequent purchasers and notwithstanding any common-law rule to the contrary. The form of the claim to priority, i.e., filing or perfection, may shift from time to time, and the rank will be based on the first filing or perfection as long as there is no intervening period without filing or perfection. See Section 9-308(c) [30-9A-308(3)].

Example 3: On October 1, A acquires a temporarily perfected (20-day) security interest, unfiled, in a tangible negotiable document in the debtor's possession under Section 9-312(e) [30-9A-312(5)]. On October 5, B files and thereby perfects a security interest that previously had attached to the same document. On October 10, A files. A has priority, even after the 20-day period expires, regardless of whether A knows of B's security interest when A files. A was the first to perfect and maintained continuous perfection or filing since the start of the 20-day period. However, the perfection of A's security interest extends only "to the extent it arises for new value given." To the extent A's security interest secures advances made by A beyond the 20-day period, its security interest would be subordinate to B's, inasmuch as B was the first to file.

In general, the rule in subsection (a)(1) [subsection (1)(a)] does not distinguish among various advances made by a secured party. The priority of every advance dates from the earlier of filing or perfection. However, in rare instances, the priority of an advance dates from the time the advance is made. See Example 3 and Section 9-323 [30-9A-323].

5. **Priority in After-Acquired Property.** The application of the priority rules to after-acquired property must be considered separately for each item of collateral. Priority does not depend only on time of perfection but may also be based on priority in filing before perfection.

Example 4: On February 1, A makes advances to Debtor under a security agreement covering "all Debtor's machinery, both existing and after-acquired." A promptly files a financing statement. On April 1, B takes a security interest in all Debtor's machinery, existing and after-acquired, to secure an outstanding loan. The following day, B files a financing statement. On May 1, Debtor acquires a new machine. When Debtor acquires rights in the new machine, both A and B acquire security interests in the machine simultaneously. Both security interests are perfected simultaneously. However, A has priority because A filed before B.

When after-acquired collateral is encumbered by more than one security interest, one of the security interests often is a purchase-money security interest that is entitled to special priority under Section 9-324 [30-9A-324].

6. **Priority in Proceeds: General Rule.** Subsection (b)(1) [subsection (2)(a)] follows former Section 9-312(6) [30-9-312(6), now repealed]. It provides that the baseline rules of subsection (a) [subsection (1)] apply generally to priority conflicts in proceeds except where otherwise provided (e.g., as in subsections (c) through (e) [subsections (3) through (5)]). Under Section 9-203 [30-9A-203], attachment cannot occur (and therefore, under Section 9-308 [30-9A-308], perfection cannot occur) as to particular collateral until the collateral itself comes into existence and the debtor has rights in it. Thus, a security interest in proceeds of original collateral does not attach and is not perfected until the proceeds come into existence and the debtor acquires rights in them.

Example 5: On April 1, Debtor authenticates a security agreement granting to A a security interest in all Debtor's existing and after-acquired inventory. The same day, A files a financing statement covering inventory. On May 1, Debtor authenticates a security agreement granting B a security interest in all Debtor's existing and future accounts. On June 1, Debtor sells inventory to a customer on 30-day unsecured credit. When Debtor acquires the account, B's security interest attaches to it and is perfected by B's financing statement. At the very same time, A's security interest attaches to the account as proceeds of the inventory and is automatically perfected. See

Section 9-315 [30-9A-315]. Under subsection (b) [subsection (2)] of this section, for purposes of determining A's priority in the account, the time of filing as to the original collateral (April 1, as to inventory) is also the time of filing as to proceeds (account). Accordingly, A's security interest in the account has priority over B's. Of course, had B filed its financing statement before A filed (e.g., on March 1), then B would have priority in the accounts.

Section 9-324 [30-9A-324] governs the extent to which a special purchase-money priority in goods or software carries over into the proceeds of the original collateral.

7. **Priority in Proceeds: Special Rules.** Subsections (c), (d), and (e) [subsections (3), (4), and (5)], which are new, provide additional priority rules for proceeds of collateral in situations where the temporal (first-in-time) rules of subsection (a)(1) [subsection (1)(a)] are not appropriate. These new provisions distinguish what these Comments refer to as "non-filing collateral" from what they call "filing collateral." As used in these Comments, non-filing collateral is collateral of a type for which perfection may be achieved by a method other than filing (possession or control, mainly) and for which secured parties who so perfect generally do not expect or need to conduct a filing search. More specifically, non-filing collateral is chattel paper, deposit accounts, negotiable documents, instruments, investment property, and letter-of-credit rights. Other collateral-accounts, commercial tort claims, general intangibles, goods, nonnegotiable documents, and payment intangibles-is filing collateral.

8. **Proceeds of Non-Filing Collateral: Non-Temporal Priority.** Subsection (c)(2) [subsection (3)(b)] provides a baseline priority rule for proceeds of non-filing collateral which applies if the secured party has taken the steps required for non-temporal priority over a conflicting security interest in non-filing collateral (e.g., control, in the case of deposit accounts, letter-of-credit rights, investment property, and in some cases, electronic negotiable documents, section 9-331 [30-9A-331]). This rule determines priority in proceeds of non-filing collateral whether or not there exists an actual conflicting security interest in the original non-filing collateral. Under subsection (c)(2) [subsection (3)(b)], the priority in the original collateral continues in proceeds if the security interest in proceeds is perfected and the proceeds are cash proceeds or non-filing proceeds "of the same type" as the original collateral. As used in subsection (c)(2) [subsection (3)(b)], "type" means a type of collateral defined in the Uniform Commercial Code and should be read broadly. For example, a security is "of the same type" as a security entitlement (i.e., investment property), and a promissory note is "of the same type" as a draft (i.e., an instrument).

Example 6: SP-1 perfects its security interest in investment property by filing. SP-2 perfects subsequently by taking control of a certificated security. Debtor receives cash proceeds of the security (e.g., dividends deposited into Debtor's deposit account). If the first-to-file-or-perfect rule of subsection (a)(1) [subsection (1)(a)] were applied, SP-1's security interest in the cash proceeds would be senior, although SP-2's security interest continues perfected under Section 9-315 [30-9A-315] beyond the 20-day period of automatic perfection. This was the result under former Article 9 [Title 30, chapter 9, now repealed]. Under subsection (c) [subsection (3)], however, SP-2's security interest is senior. Note that a different result would obtain in Example 1 (i.e., SP-1's security interest would be senior) if SP-1 were to obtain control of the deposit-account proceeds. This is so because subsection (c) [subsection (3)] is subject to subsection (f) [subsection (6)], which in turn provides that the priority rules under subsections (a) through (e) [subsections (1) through (5)] are subject to "the other provisions of this part." One of those "other provisions" is Section 9-327 [30-9A-327], which affords priority to a security interest perfected by control. See Section 9-327(1) [30-9A-327(1)].

Example 7: SP-1 perfects its security interest in investment property by filing. SP-2 perfects subsequently by taking control of a certificated security. Debtor receives proceeds of the security consisting of a new certificated security issued as a stock dividend on the original collateral. Although the new security is of the same type as the original collateral (i.e., investment property), once the 20-day period of automatic perfection expires (see Section 9-315(d) [30-9A-315(4)]), SP-2's security interest is unperfected. (SP-2 has not filed or taken delivery or control, and no temporary-perfection rule applies.) Consequently, once the 20-day period expires, subsection (c) [subsection (3)] does not confer priority, and, under subsection (a)(2) [subsection (1)(b)], SP-1's security interest in the security is senior. This was the result under former Article 9 [Title 30, chapter 9, now repealed].

Example 8: SP-1 perfects its security interest in investment property by filing. SP-2 perfects subsequently by taking control of a certificated security and also by filing against investment property. Debtor receives proceeds of the security consisting of a new certificated security issued as a stock dividend of the collateral. Because the new security is of the same type as the original collateral (i.e., investment property) and (unlike Example 7) SP-2's security interest is perfected by filing, SP-2's security interest is senior under subsection (c) [subsection (3)]. If the new security were redeemed by the issuer upon surrender and yet another security were received by Debtor, SP-2's security interest would continue to enjoy priority under subsection (c) [subsection (3)]. The new security would be proceeds of proceeds.

Example 9: SP-1 perfects its security interest in instruments by filing. SP-2 subsequently perfects its security interest in investment property by taking control of a certificated security and also by filing against investment property. Debtor receives proceeds of the security consisting of a dividend check that it deposits to a deposit account. Because the check and the deposit account are cash proceeds, SP-1's and SP-2's security interests in the cash proceeds are perfected under Section 9-315 [30-9A-315] beyond the 20-day period of automatic perfection. However, SP-2's security interest is senior under subsection (c) [subsection (3)].

Example 10: SP-1 perfects its security interest in investment property by filing. SP-2 perfects subsequently by taking control of a certificated security and also by filing against investment property. Debtor receives an instrument as proceeds of the security. (Assume that the instrument is not cash proceeds.) Because the instrument is not of the same type as the original collateral (i.e., investment property), SP-2's security interest, although perfected by filing, does not achieve priority under subsection (c) [subsection (3)]. Under the first-to-file-or-perfect rule of subsection (a)(1) [subsection (1)(a)], SP-1's security interest in the proceeds is senior.

The proceeds of proceeds are themselves proceeds. See Section 9-102 [30-9A-102] (defining "proceeds" and "collateral"). Sometimes competing security interests arise in proceeds that are several generations removed from the original collateral. As the following example explains, the applicability of subsection (c) [subsection (3)] may turn on the nature of the intervening proceeds.

Example 11: SP-1 perfects its security interest in Debtor's deposit account by obtaining control. Thereafter, SP-2 files against inventory, (presumably) searches, finds no indication of a conflicting security interest, and advances against Debtor's existing and after-acquired inventory. Debtor uses funds from the deposit account to purchase inventory, which SP-1 can trace as identifiable proceeds of its security interest in Debtor's deposit account, and which SP-2 claims as original collateral. The inventory is sold and the proceeds deposited into another deposit account, as to which SP-1 has not obtained control. Subsection (c) [subsection (3)] does not govern priority in this other deposit account. This deposit account is cash proceeds and is also the same type of collateral as SP-1's original collateral, as required by subsections (c)(2)(A) and (B) [subsections (3)(b)(i) and (3)(b)(ii)]. However, SP-1's security interest does not satisfy subsection (c)(2)(C) [subsection (3)(b)(iii)] because the inventory proceeds, which intervened between the original deposit account and the deposit account constituting the proceeds at issue, are not cash proceeds, proceeds of the same type as the collateral (original deposit account), or an account relating to the collateral. Stated otherwise, once proceeds other than cash proceeds, proceeds of the same type as the original collateral, or an account relating to the original collateral intervene in the chain of proceeds, priority under subsection (c) [subsection (3)] is thereafter unavailable. The special priority rule in subsection (d) [subsection (4)] also is inapplicable to this case. See Comment 9, Example 13, below. Instead, the general first-to-file-or-perfect rule of subsections (a) and (b) [subsections (1) and (2)] apply. Under that rule, SP-1 has priority unless its security interest in the inventory proceeds became unperfected under Section 9-315(d) [30-9A-315(4)]. Had SP-2 filed against inventory before SP-1 obtained control of the original deposit account, then SP-2 would have had priority even if SP-1's security interest in the inventory proceeds remained perfected.

If two security interests in the same original collateral are entitled to priority in an item of proceeds under subsection (c)(2) [subsection (3)(b)], the security interest having priority in the original collateral has priority in the proceeds.

9. **Proceeds of Non-Filing Collateral: Special Temporal Priority.** Under subsections (d) and (e) [subsections (4) and (5)], if a security interest in non-filing collateral is perfected by a method other than filing (e.g., control or possession), it does not retain its priority over a conflicting security interest in proceeds that are filing collateral. Moreover, it is not entitled to priority in proceeds under the first-to file-or-perfect rule of subsections (a)(1) and (b) [subsections (1)(a) and (2)]. Instead, under subsection (d) [subsection (4)], priority is determined by a new first-to-file rule.

Example 12: SP-1 perfects its security interest in Debtor's deposit account by obtaining control. Thereafter, SP-2 files against equipment, (presumably) searches, finds no indication of a conflicting security interest, and advances against Debtor's equipment. SP-1 then files against Debtor's equipment. Debtor uses funds from the deposit account to purchase equipment, which SP-1 can trace as proceeds of its security interest in Debtor's deposit account. If the first-to-file-or-perfect rule were applied, SP-1's security interest would be senior under subsections (a)(1) and (b) [subsection (1)(a) and (2)], because it was the first to perfect in the original collateral and there was no period during which its security interest was unperfected. Under subsection (d) [subsection (4)], however, SP-2's security interest would be senior because it filed first. This corresponds with the likely expectations of the parties.

Note that under subsection (e) [subsection (5)], the first-to-file rule of subsection (d) [subsection (4)] applies only if the proceeds in question are other than non-filing collateral (i.e., if the proceeds are filing collateral). If the proceeds are non-filing collateral, either the first-to-file-or-perfect rule under subsections (a) and (b) [subsections (1) and (2)] or the non-temporal priority rule in subsection (c) [subsection (3)] would apply, depending on the facts.

Example 13: SP-1 perfects its security interest in Debtor's deposit account by obtaining control. Thereafter, SP-2 files against inventory, (presumably) searches, finds no indication of a conflicting security interest, and advances against Debtor's existing and after-acquired inventory. Debtor uses funds from the deposit account to purchase inventory, which SP-1 can trace as identifiable proceeds of its security interest in Debtor's deposit account, and which SP-2 claims as original collateral. The inventory is sold and the proceeds deposited into another deposit account, as to which SP-1 has not obtained control. As discussed above in Comment 8, Example 11, subsection (c) [subsection (3)] does not govern priority in this deposit account. Subsection (d) [subsection (4)] also does not govern, because the proceeds at issue (the deposit account) are cash proceeds. See subsection (e) [subsection (5)]. Rather, the general rules of subsections (a) and (b) [subsections (1) and (2)] govern.

10. **Priority in Supporting Obligations.** Under subsections (b)(2) and (c)(1) [subsections (2)(b) and (3)(a)], a security interest having priority in collateral also has priority in a supporting obligation for that collateral. However, the rules in these subsections are subject to the special rule in Section 9-329 [30-9A-329] governing the priority of security interests in a letter-of-credit right. See subsection (f) [subsection (6)]. Under Section 9-329 [30-9A-329], a secured party's failure to obtain control (Section 9-107) [30-9A-107] of a letter-of-credit right that serves as supporting collateral leaves its security interest exposed to a priming interest of a party who does take control.

11. **Unperfected Security Interests.** Under subsection (a)(3) [subsection (1)(c)], if conflicting security interests are unperfected, the first to attach has priority. This rule may be of merely theoretical interest, inasmuch as it is hard to imagine a situation where the case would come into litigation without either secured party's having perfected its security interest. If neither security interest had been perfected at the time of the filing of a petition in bankruptcy, ordinarily neither would be good against the trustee in bankruptcy under the Bankruptcy Code.

12. **Agricultural Liens.** Statutes other than this Article [Title 30, chapter 9A] may purport to grant priority to an agricultural lien as against a conflicting security interest or agricultural lien. Under subsection (g) [subsection (7)], if another statute grants priority to an agricultural lien, the agricultural lien has priority only if the same statute creates the agricultural lien and the agricultural lien is perfected. Otherwise, subsection (a) [subsection (1)] applies the same priority rules to an agricultural lien as to a security interest, regardless of whether the agricultural lien conflicts with another agricultural lien or with a security interest.

Inasmuch as no agricultural lien on proceeds arises under this Article [Title 30, chapter 9A], subsections (b) through (e) [subsections (2) through (5)] do not apply to proceeds of agricultural liens. However, if an agricultural lien has priority under subsection (g) [subsection (7)] and the statute creating the agricultural lien gives the secured party a lien on proceeds of the collateral subject to the lien, a court should apply the principle of subsection (g) [subsection (7)] and award priority in the proceeds to the holder of the perfected agricultural lien.

Case Notes

Applicability of Local Law When Perfecting Agricultural Liens: In a dispute over priority of an agricultural lien versus a security interest in the same profits from agricultural products, plaintiff who held a security interest asserted that defendant who held an agricultural lien did not satisfy the requirements of the Uniform Commercial Code (U.C.C.) regarding perfection because defendant's lien was not perfected in North Dakota where the farm products were located, as required by 30-9A-302, at the time that the dispute arose. However, agricultural liens follow the location of the farm products, not the location of the debtor, and when defendant's lien was created, the products in question were located in Montana. Therefore, Montana's local law was the local law designated by the U.C.C. to govern perfection of the lien. Defendant properly filed the lien in Montana and therefore did not violate the U.C.C. in perfecting the lien. Stockman Bank of Mont. v. Mon-Kota, Inc., 2008 MT 74, 342 M 115, 180 P3d 1125 (2008).

Interaction of Agricultural Lien Law and Uniform Commercial Code on Secured Transactions — Filing of Agricultural Lien Adequate to Fulfill Financing Statement Requirements of Uniform Commercial Code: Agricultural liens are not security interests, and only the parts of Article 9 of the Uniform Commercial Code (U.C.C.) that expressly refer to agricultural liens, rather than those that refer only to security interests, apply to agricultural liens. Merely because collateral consists of farm products does not automatically turn an agricultural lien into a security interest. The attachment rules of Article 9 do not apply to agricultural liens; rather, agricultural liens attach according to the rules in the statutes that created agricultural liens. Similarly, 71-3-902 clearly delineates the procedure for perfecting an agricultural lien. This case presented a potential conflict regarding lien priority in that 71-3-904 grants agricultural liens a superpriority status that is not dependent on being the first to file, while 30-9A-322 states that an agricultural lien has priority over a conflicting security interest on the same collateral if the lien is perfected pursuant to 30-9A-310 of the U.C.C. Thus, agricultural lienors must satisfy the perfection requirements of 30-9A-310 in addition to the perfection requirements of 71-3-902, and by doing so, the lienors will be insulated from the U.C.C. first-in-time rule and retain the superpriority status pursuant to 71-3-904. However, because agricultural liens require the same and more information as a U.C.C. filing and both filings are documented in the same database, the filing of an agricultural lien with the Secretary of State also satisfied the financing statement requirements of the U.C.C., and a duplicate filing of a U.C.C. financing statement is not required. Stockman Bank of Mont. v. Mon-Kota, Inc., 2008 MT 74, 342 M 115, 180 P3d 1125 (2008).

Failure to Demonstrate That Equitable Interest in Cattle Sold Displaced Perfected Security Interest in Cattle as After-Acquired Property: Bellanger obtained loans from the Daniels-Sheridan Federal Credit Union to finance a ranching operation, securing the loans with several promissory notes securing an interest in the cattle on the ranch. Bellanger subsequently defaulted on the loans, and the credit union initiated an action to enforce the promissory notes pursuant to the Uniform Commercial Code (U.C.C.). The case broadened to encompass disputes over proceeds from the sale of the cattle to include Smith, the owner of the auction company where Bellanger customarily sold cattle, whom the credit union alleged had an inferior security interest in some of the cattle that Smith had sold to Bellanger. The credit union pointed out that Smith had only an unperfected security interest because he failed to perfect a security interest pursuant to the U.C.C. Smith contended that Bellanger had obtained only a leasehold interest in the cattle and that the credit union thus had no security interest in those cattle. The cattle were subsequently seized and sold for $79,012.27, and the District Court split the proceeds, with $45,467.94 paid to the credit union and a judgment for the remainder owed on the promissory notes, and $33,544.33 paid to Smith. The credit union appealed, and the Supreme Court reversed. The District Court erred in equitably subordinating the credit union's prior perfected security interest to Smith's unperfected security interest. The Supreme Court held that Smith's transaction with Bellanger was a sale, not a lease or bailment, and as such, the hierarchy of priorities for security interests set forth in Article 9 of the U.C.C. (now Title 30, ch. 9A) applied in the credit union's favor. Smith failed to demonstrate that any equitable interest that he had in the cattle displaced the credit union's perfected security interest in the cattle as an after-acquired property of Bellanger, so an equitable carve-out from the U.C.C. principles of hierarchy priority was not justified. Daniels-Sheridan Fed. Credit Union v. Bellanger, 2001 MT 235, 307 M 22, 36 P3d 397 (2001), following Rudio v. Yellowstone Merchandising Corp., 200 M 537, 652 P2d 1163 (1982), and distinguishing NW. Potato Sales, Inc. v. Beck, 208 M 310, 678 P2d 1138 (1984), and Ninth District Prod. Credit Ass'n v. Ed Duggan, Inc., 821 P2d 788 (Colo. 1991).

30-9A-323. Future advances.

Official Comments

[*Corresponding U.C.C. Section:* Section 9-323, U.C.C.]

1. **Source.** Former Sections 9-312(7), 9-301(4), 9-307(3), 2A-307(4) [30-9-312(7), now repealed, 30-9-301(4), now repealed, see former 30-9-307(3) not adopted in Montana, 30-2A-307(4)].

2. **Scope of This Section.** A security agreement may provide that collateral secures future advances. See Section 9-204(c) [30-9A-204(3)]. This section collects all of the special rules dealing with the priority of advances made by a secured party after a third party acquires an interest in the collateral. Subsection (a) [subsection (1)] applies when the third party is a competing secured party. It replaces and clarifies former Section 9-312(7) [30-9-312(7), now repealed]. Subsection (b) [subsection (2)] deals with lien creditors and replaces former Section 9-301(4) [30-9-301(4), now repealed]. Subsections (d) and (e) [subsections (4) and (5)] deal with buyers and replace former Section 9-307(3) [see former 30-9-307, now repealed, see 30-9A-320]. Subsections (f) and (g) [subsections (4) and (5)] deal with lessees and replace former Section 2A-307(4) [30-2A-307(4)].

3. **Competing Security Interests.** Under a proper reading of the first-to-file-or-perfect rule of Section 9-322(a)(1) [30-9A-322(1)(a)] (and former Section 9-312(5) [30-9-312(5), now repealed, see 30-9A-322]), it is abundantly clear that the time when an advance is made plays no role in determining priorities among conflicting security interests except when a financing statement was not filed and the advance is the giving of value as the last step for attachment and perfection. Thus, a secured party takes subject to all advances secured by a competing security interest having priority under Section 9-322(a)(1) [30-9A-322(1)(a)]. This result generally obtains regardless of how the competing security interest is perfected and regardless of whether the advances are made "pursuant to commitment" (Section 9-102 [30-9A-102]). Subsection (a) [subsection (1)] of this section states the only other instance when the time of an advance figures in the priority scheme in Section 9-322 [30-9A-322]: when the security interest is perfected only automatically under Section 9-309 [30-9A-309] or temporarily under Section 9-312(e), (f), or (g) [30-9A-312 (5), (6), or (7)], and the advance is not made pursuant to a commitment entered into while the security interest was perfected by another method. Thus, an advance has priority from the date it is made only in the rare case in which it is made without commitment and while the security interest is perfected only temporarily under Section 9-312 [30-9A-312].

The new formulation in subsection (a) [subsection (1)] clarifies the result when the initial advance is paid and a new ("future") advance is made subsequently. Under former Section 9-312(7) [30-9-312(7), now repealed], the priority of the new advance turned on whether it was "made while a security interest is perfected." This section resolves any ambiguity by omitting the quoted phrase.

Example 1: On February 1, A makes an advance secured by machinery in the debtor's possession and files a financing statement. On March 1, B makes an advance secured by the same machinery and files a financing statement. On April 1, A makes a further advance, under the original security agreement, against the same machinery. A was the first to file and so, under the first-to-file-or-perfect rule of Section 9-322(a)(1) [30-9A-322(1)(a)], A's security interest has priority over B's, both as to the February 1 and as to the April 1 advance. It makes no difference whether A knows of B's intervening advance when A makes the second advance. Note that, as long as A was the first to file or perfect, A would have priority with respect to both advances if either A or B had perfected by taking possession of the collateral. Likewise, A would have priority if A's April 1 advance was not made under the original agreement with the debtor, but was under a new agreement.

Example 2: On October 1, A acquires a temporarily perfected (20-day) security interest, unfiled, in a tangible negotiable document in the debtor's possession under Section 9-312 (e) or (f) [30-9A-312(5) or (6)]. The security interest secures an advance made on that day as well as future advances. On October 5, B files and thereby perfects a security interest that previously had attached to the same document. On October 8, A makes an additional advance. On October 10, A files. Under Section 9-322(a)(1) [30-9A-322(1)(a)], because A was the first to perfect and maintained continuous perfection or filing since the start of the 20-day period, A has priority, even after the 20-day period expires. See Section 9-322 [30-9A-322], Comment 4, Example 3. However, under this section, for purposes of Section 9-322(a)(1) [30-9A-322(1)(a)], to the extent A's security interest secures the October 8 advance, the security interest was perfected on October 8. Inasmuch as B perfected on October 5, B has priority over the October 8 advance.

The rule in subsection (a) [subsection (1)] is more liberal toward the priority of future advances than the corresponding rules applicable to intervening lien creditors (subsection (b) [subsection (2)]), buyers (subsections (d) and (e) [subsections (4) and (5)]), and lessees (subsections (f) and (g) [subsections (6) and (7)]).

4. **Competing Lien Creditors.** Subsection (b) [subsection (2)] replaces former Section 9-301(4) [30-9-301(4), now repealed] and addresses the rights of a "lien creditor," as defined in Section 9-102 [30-9A-102]. Under Section 9-317(a)(2) [30-9A-317(1)(b)], a security interest is senior to the rights of person who becomes a lien creditor, unless the person becomes a lien creditor before the security interest is perfected and before a financing statement covering the collateral is filed. Subsection (b) [subsection (2)] of this section provides that a security interest is subordinate to those rights to the extent that the specified circumstances occur. Subsection (b) [subsection (2)] does not elevate the priority of a security interest that is subordinate to the rights of a lien creditor under Section 9-317(a)(2) [30-9A-317(1)(b)]; it only subordinates.

As under former Section 9-301(4) [30-9-301(4), now repealed], a secured party's knowledge does not cut short the 45-day period during which future advances can achieve priority over an intervening lien creditor's interest. Rather, because of the impact of the rule in subsection (b) [subsection (2)] on the question whether the security interest for future advances is "protected" under Section 6323(c)(2) and (d) of the Internal Revenue Code as amended by the Federal Tax Lien Act of 1966, the priority of the security interest for future advances over a lien creditor is made absolute for 45 days regardless of knowledge of the secured party concerning the lien. If, however, the advance is made after the 45 days, the advance will not have priority unless it was made or committed without knowledge of the lien.

5. **Sales of Receivables; Consignments.** Subsections (a) and (b) [subsections (1) and (2)] do not apply to outright sales of accounts, chattel paper, payment intangibles, or promissory notes, nor do they apply to consignments.

6. **Competing Buyers and Lessees.** Under subsections (d) and (e) [subsections (4) and (5)], a buyer will not take subject to a security interest to the extent it secures advances made after the secured party has knowledge that the buyer has purchased the collateral or more than 45 days after the purchase unless the advances were made pursuant to a commitment entered into before the expiration of the 45-day period and without knowledge of the purchase. Subsections (f) and (g) [subsections (6) and (7)] provide an analogous rule for lessees. Of course, a buyer in ordinary course who takes free of the security interest under Section 9-320 [30-9A-320] and a lessee in ordinary course who takes free under Section 9-321 [30-9A-321] are not subject to any future advances. Subsections (d) and (e) [subsections (4) and (5)] replace former Section 9-307(3) [see former 30-9-307, now repealed, see 30-9A-320], and subsections (f) and (g) [subsections (6) and (7)] replace former Section 2A-307(4) [30-2A-307(4)]. No change in meaning is intended.

Compiler's Comments

2001 Amendment: Chapter 179 in (2) after "lien creditor" deleted "while the security interest is perfected only"; and made minor changes in style. Amendment effective July 1, 2001.

30-9A-324. Priority of purchase-money security interests.

Official Comments

1. **Source.** Former Section 9-312(3), (4) [30-9-312(3), (4), now repealed].

2. **Priority of Purchase-Money Security Interests.** This section contains the priority rules applicable to purchase-money security interests, as defined in Section 9-103 [30-9A-103]. It affords a special, non-temporal priority to those purchase-money security interests that satisfy the statutory conditions. In most cases, priority will be over a security interest asserted under an after-acquired property clause. See Section 9-204 [30-9A-204] on the extent to which security interests in after-acquired property are validated.

A purchase-money security interest can be created only in goods and software. See Section 9-103 [30-9A-103]. Section 9-324(a) [30-9A-324(1)], which follows former Section 9-312(4) [30-9-312(4), now repealed], contains the general rule for purchase-money security interests in goods. It is subject to subsections (b) and (c) [subsections (2) and (3)], which derive from former Section 9-312(3) [30-9-312(3), now repealed] and apply to purchase-money security interests in inventory, and subsections (d) and (e) [subsections (4) and (5)], which apply to purchase-money security interests in livestock that are farm products. Subsection (f) [subsection (6)] applies to purchase-money security interests in software. Subsection (g) [subsection (7)] deals with the relatively unusual case in which a debtor creates two purchase-money security interests in the same collateral and both security interests qualify for special priority under one of the other subsections.

Former Section 9-312(2) [30-9-312(2), now repealed] contained a rule affording special priority to those who provided secured credit that enabled a debtor to produce crops. This rule proved unworkable and has been eliminated from this Article [Title 30, chapter 9A]. Instead, model Section 9-324A [not adopted in Montana] contains a revised production-money priority rule. That section is a model, not uniform, provision. The sponsors of the UCC have taken no position as to whether it should be enacted, instead leaving the matter for state legislatures to consider if they are so inclined.

3. **Purchase-Money Priority in Goods Other Than Inventory and Livestock.** Subsection (a) [subsection (1)] states a general rule applicable to all types of goods except inventory and farm-products livestock: the purchase-money interest takes priority if it is perfected when the debtor receives possession of the collateral or within 20 days thereafter. (As to the 20-day "grace period," compare Section 9-317(e) [30-9A-317(5)]. Former Sections 9-312(4) and 9-301(2) [30-9-312(4) and 30-9-301(2), both now repealed] contained a 10[20]-day grace period.) The perfection requirement means that the purchase-money secured party either has filed a financing statement before that time or has a temporarily perfected security interest in goods covered by documents under Section 9-312(e) and (f) [30-9A-312(5) and (6)] which is continued in a perfected status by filing before the expiration of the 20-day period specified in that section.

A purchase-money security interest qualifies for priority under subsection (a) [subsection (1)], even if the purchase-money secured party knows that a conflicting security interest has been created and/or that the holder of the conflicting interest has filed a financing statement covering the collateral.

Normally, there will be no question when "the debtor receives possession of the collateral" for purposes of subsection (a) [subsection (1)]. However, sometimes a debtor buys goods and takes possession of them in stages, and then assembly and testing are completed (by the seller or debtor-buyer) at the debtor's location. Under those circumstances, the buyer "takes possession" within the meaning of subsection (a) [subsection (1)] when, after an inspection of the portion of the goods in the debtor's possession, it would be apparent to a potential lender to the debtor that the debtor has acquired an interest in the goods taken as a whole.

A similar issue concerning the time when "the debtor receives possession" arises when a person acquires possession of goods under a transaction that is not governed by this Article [Title 30, chapter 9A] and then later agrees to buy the goods on secured credit. For example, a person may take possession of goods as lessee under a lease contract and then exercise an option to purchase the goods from the lessor on secured credit. Under Section 2A-307(1) [30-2A-307(1)], creditors of the lessee generally take subject to the lease contract; filing a financing statement against the lessee is unnecessary to protect the lessor's leasehold or residual interest. Once the lease is converted to a security interest, filing a financing statement is necessary to protect the seller's (former lessor's) security interest. Accordingly, the 20-day period in subsection (a) does not commence until the goods become "collateral" (defined in Section 9-102 [30-9A-102]), i.e., until they are subject to a security interest.

4. **Purchase-Money Security Interests in Inventory.** Subsections (b) and (c) [subsections (2) and (3)] afford a means by which a purchase-money security interest in inventory can achieve priority over an earlier-filed security interest in the same collateral. To achieve priority, the purchase-money security interest must be perfected when the debtor receives possession of the inventory. For a discussion of when "the debtor receives possession," see Comment 3, above. The 20-day grace period of subsection (a) [subsection (1)] does not apply.

The arrangement between an inventory secured party and its debtor typically requires the secured party to make periodic advances against incoming inventory or periodic releases of old inventory as new inventory is received. A fraudulent debtor may apply to the secured party for advances even though it has already given a purchase-money security interest in the inventory to another secured party. For this reason, subsections (b)(2) through (4) and (c) [subsections (2)(b) through (2)(d) and (3)] impose a second condition for the purchase-money security interest's achieving priority: the purchase-money secured party must give notification to the holder of a conflicting security interest who filed against the same item or type of inventory before the purchase-money secured party filed or its security interest became perfected temporarily under Section 9-312(e) or (f) [30-9A-312(5) or (6)]. The notification requirement protects the non-purchase-money inventory secured party in such a situation: if the inventory secured party has received notification, it presumably will not make an advance; if it has not received notification (or if the other security interest does not qualify as purchase-money), any advance the inventory secured party may make ordinarily will have priority under Section 9-322 [30-9A-322]. Inasmuch as an arrangement for periodic advances against incoming goods is unusual outside the inventory field, subsection (a) [subsection (1)] does not contain a notification requirement.

5. **Notification to Conflicting Inventory Secured Party: Timing.** Under subsection (b)(3) [subsection (2)(c)], the perfected purchase-money security interest achieves priority over a conflicting security interest only if the holder of the conflicting security interest receives a notification within five years before the debtor receives possession of the purchase-money collateral. If the debtor never receives possession, the five-year period never begins, and the purchase-money security interest has priority, even if notification is not given. However, where the purchase-money inventory financing began by the purchase-money secured party's possession of a negotiable document of title, to retain priority the secured party must give the notification required by subsection (b) [subsection (2)] at or before the usual time, i.e., when the debtor gets possession of the inventory, even though the security interest remains perfected for 20 days under Section 9-312(e) or (f) [30-9A-312(5) or (6)].

Some people have mistakenly read former Section 9-312(3)(b) [30-9-312(3)(b), now repealed] to require, as a condition of purchase-money priority in inventory, that the purchase-money secured party give the notification before it files a financing statement. Read correctly, the "before" clauses compare (i) the time when the holder of the conflicting security interest filed a financing statement with (ii) the time when the purchase-money security interest becomes perfected by filing or automatically perfected temporarily. Only if (i) occurs before (ii) must notification be given to the holder of the conflicting security interest. Subsection (c) [subsection (3)] has been rewritten to clarify this point.

6. **Notification to Conflicting Inventory Secured Party: Address.** Inasmuch as the address provided as that of the secured party on a filed financing statement is an "address that is reasonable under the circumstances," the holder of a purchase-money security interest may satisfy the requirement to "send" notification to the holder of a conflicting security interest in inventory by sending a notification to that address, even if the address is or becomes incorrect. See Section 9-102 [30-9A-102] (definition of "send"). Similarly, because the address is "held out by [the holder of the conflicting security interest] as the place for receipt of such communications [i.e., communications relating to security interests]," the holder is deemed to have "received" a notification delivered to that address. See Section 1-202(e) [30-1-210(5)].

7. **Consignments.** Subsections (b) and (c) [subsections (2) and (3)] also determine the priority of a consignor's interest in consigned goods as against a security interest in the goods created by the consignee. Inasmuch as a consignment subject to this Article [Title 30, chapter 9A] is defined to be a purchase-money security interest, see Section 9-103(d) [30-9A-103(4)], no inference concerning the nature of the transaction should be drawn from the fact that a consignor uses the term "security interest" in its notice under subsection (b)(4) [subsection (2)(d)]. Similarly, a notice stating that the consignor has delivered or expects to deliver goods, properly described, "on consignment" meets the requirements of subsection (b)(4) [subsection (2)(d)], even if it does not contain the term "security interest," and even if the transaction subsequently is determined to be a security interest. Cf. Section 9-505 [30-9A-505] (use of "consignor" and "consignee" in financing statement).

8. **Priority in Proceeds: General.** When the purchase-money secured party has priority over another secured party, the question arises whether this priority extends to the proceeds of the original collateral. Subsections (a), (d), and (f) [subsections (1), (4), and (6)] give an affirmative answer, but only as to proceeds in which the security interest is perfected (see Section 9-315 [30-9A-315]). Although this qualification did not appear in former Section 9-312(4) [30-9-312(4), now repealed], it was implicit in that provision.

In the case of inventory collateral under subsection (b) [subsection (2)], where financing frequently is based on the resulting accounts, chattel paper, or other proceeds, the special priority of the purchase-money secured interest carries over into only certain types of proceeds. As under former Section 9-312(3) [30-9-312(3), now repealed], the purchase-money priority in inventory under subsection (b) [subsection (2)] carries over into identifiable cash proceeds (defined in Section 9-102 [30-9A-102]) received on or before the delivery of the inventory to a buyer.

As a general matter, also like former Section 9-312(3) [30-9-312(3), now repealed], the purchase-money priority in inventory does not carry over into proceeds consisting of accounts or chattel paper. Many parties financing inventory are quite content to protect their first-priority security interest in the inventory itself. They realize that when the inventory is sold, someone else will be financing the resulting receivables (accounts or chattel paper), and the priority for inventory will not run forward to the receivables constituting the proceeds. Indeed, the cash supplied by the receivables financer often will be used to pay the inventory financing. In some situations, the party financing the inventory on a purchase-money basis makes contractual arrangements that the proceeds of receivables financing by another be devoted to paying off the inventory security interest.

However, the purchase-money priority in inventory does carry over to proceeds consisting of chattel paper and its proceeds (and also to instruments) to the extent provided in Section 9-330 [30-9A-330]. Under Section 9-330(e) [30-9A-330(5)], the holder of a purchase-money security interest in inventory is deemed to give new value for proceeds consisting of chattel paper. Taken together, Sections 9-324(b) and 9-330(e) [30-9A-324(2) and 30-9A-330(5)] enable a purchase-money inventory secured party to obtain priority in chattel paper constituting proceeds of the inventory, even if the secured party does not actually give new value for the chattel paper, provided the purchase-money secured party satisfies the other conditions for achieving priority.

When the proceeds of original collateral (goods or software) consist of a deposit account, Section 9-327 [30-9A-327] governs priority to the extent it conflicts with the priority rules of this section.

9. **Priority in Accounts Constituting Proceeds of Inventory.** The application of the priority rules in subsection (b) [subsection (2)] is shown by the following examples:

Example 1: Debtor creates a security interest in its existing and after-acquired inventory in favor of SP-1, who files a financing statement covering inventory. SP-2 subsequently takes a purchase-money security interest in certain inventory and, under subsection (b) [subsection (2)], achieves priority in this inventory over SP-1. This inventory is then sold, producing accounts. Accounts are not cash proceeds, and so the special purchase-money priority in the inventory does not control the priority in the accounts. Rather, the first-to-file-or-perfect rule of Section 9-322(a)(1) [30-9A-322(1)(a)] applies. The time of SP-1's filing as to the inventory is also the time of filing as to the accounts under Section 9-322(b) [30-9A-322(2)]. Assuming that each security interest in the accounts proceeds remains perfected under Section 9-315 [30-9A-315], SP-1 has priority as to the accounts.

Example 2: In Example 1, if SP-2 had filed directly against accounts, the date of that filing as to accounts would be compared with the date of SP-1's filing as to the inventory. The first filed would prevail under Section 9-322(a)(1) [30-9A-322(1)(a)].

Example 3: If SP-3 had filed against accounts in Example 1 before either SP-1 or SP-2 filed against inventory, SP-3's filing against accounts would have priority over the filings of SP-1 and SP-2. This result obtains even though the filings against inventory are effective to continue the perfected status of SP-1's and SP-2's security interest in the accounts beyond the 20-day period of automatic perfection. See Section 9-315 [30-9A-315]. SP-1's and SP-2's position as to the inventory does not give them a claim to accounts (as proceeds of the inventory) which is senior to someone who has filed earlier against accounts. If, on the other hand, either SP-1's or SP-2's filing against the inventory preceded SP-3's filing against accounts, SP-1 or SP-2 would outrank SP-3 as to the accounts.

10. **Purchase-Money Security Interests in Livestock.** New subsections (d) and (e) [subsections (4) and (5)] provide a purchase-money priority rule for farm-products livestock. They are patterned on the purchase-money priority rule for inventory found in subsections (b) and (c) [subsections (2) and (3)] and include a requirement that the purchase-money secured party notify earlier-filed parties. Two differences between subsections (b) and (d) [subsections (2) and (4)] are noteworthy. First, unlike the purchase-money inventory lender, the purchase-money livestock lender enjoys priority in all proceeds of the collateral. Thus, under subsection (d) [subsection (4)], the purchase-money secured party takes priority in accounts over an earlier-filed accounts financer. Second, subsection (d) [subsection (4)] affords priority in certain products of the collateral as well as proceeds.

11. **Purchase-Money Security Interests in Aquatic Farm Products.** Aquatic goods produced in aquacultural operations (e.g., catfish raised on a catfish farm) are farm products. See Section 9-102 [30-9A-102] (definition of "farm products"). The definition does not indicate whether aquatic goods are "crops," as to which the model production money security interest priority in Section 9-324A [not adopted in Montana] applies, or "livestock," as to which the purchase-money priority in subsection (d) [subsection (4)] of this section applies. This Article [Title 30, chapter 9A] leaves courts free to determine the classification of particular aquatic goods on a case-by-case basis, applying whichever priority rule makes more sense in the overall context of the debtor's business.

12. **Purchase-Money Security Interests in Software.** Subsection (f) [subsection 6] governs the priority of purchase-money security interests in software. Under Section 9-103(c) [30-9A-103(3)], a purchase-money security interest arises in software only if the debtor acquires its interest in the software for the principal purpose of using the software in goods subject to a purchase-money security interest. Under subsection (f) [subsection (6)], a purchase-money security interest in software has the same priority as the purchase-money security interest in the goods in which the software was acquired for use. This priority is determined under subsections (b) and (c) [subsections (2) and (3)] (for inventory) or (a) [subsection (1)] (for other goods).

13. **Multiple Purchase-Money Security Interests.** New subsection (g) [subsection (7)] governs priority among multiple purchase-money security interests in the same collateral. It grants priority to purchase-money security interests securing the price of collateral (i.e., created in favor of the seller) over purchase-money security interests that secure enabling loans. Section 7.2(c) of the Restatement (3d) of the Law of Property (Mortgages) (1997) adopts this rule with respect to real property mortgages. As Comment d to that section explains:

the equities favor the vendor. Not only does the vendor part with specific real estate rather than money, but the vendor would never relinquish it at all except on the understanding that the vendor will be able to use it to satisfy the obligation to pay the price. This is the case even though the vendor may know that the mortgagor is going to finance the transaction in part by borrowing from a third party and giving a mortgage to secure that obligation. In the final analysis, the law is more sympathetic to the vendor's hazard of losing real estate previously owned than to the third party lender's risk of being unable to collect from an interest in real estate that never previously belonged to it.

The first-to-file-or-perfect rule of Section 9-322 [30-9A-322] applies to multiple purchase-money security interests securing enabling loans.

30-9A-325. Priority of security interests in transferred collateral.

Official Comments

1. **Source.** New.

2. **"Double Debtor Problem."** This section addresses the "double debtor" problem, which arises when a debtor acquires property that is subject to a security interest created by another debtor.

3. **Taking Subject to Perfected Security Interest.** Consider the following scenario:

Example 1: A owns an item of equipment subject to a perfected security interest in favor of SP-A. A sells the equipment to B, not in the ordinary course of business. B acquires its interest subject to SP-A's security interest. See Sections 9-201, 9-315(a)(1) [30-9A-201 and 30-9A-315(1)(a)]. Under this section, if B creates a security interest in the equipment in favor of SP-B, SP-B's security interest is subordinate to SP-A's security interest, even if SP-B filed against B before SP-A filed against A, and even if SP-B took a purchase-money security interest. Normally, SP-B could have investigated the source of the equipment and discovered SP-A's filing before making an advance against the equipment, whereas SP-A had no reason to search the filings against someone other than its debtor, A.

4. **Taking Subject to Unperfected Security Interest.** This section applies only if the security interest in the transferred collateral was perfected when the transferee acquired the collateral. See subsection (a)(2) [subsection (1)(b)]. If this condition is not met, then the normal priority rules apply.

Example 2: A owns an item of equipment subject to an unperfected security interest in favor of SP-A. A sells the equipment to B, who gives value and takes delivery of the equipment without knowledge of the security interest. B takes free of the security interest. See Section 9-317(b) [30-9A-317(2)]. If B then creates a security interest in favor of SP-B, no priority issue arises; SP-B has the only security interest in the equipment.

Example 3: The facts are as in Example 2, except that B knows of SP-A's security interest and therefore takes the equipment subject to it. If B creates a security interest in the equipment in favor of SP-B, this section does not determine the relative priority of the security interests. Rather, the normal priority rules govern. If SP-B perfects its security interest, then, under Section 9-322(a)(2) [30-9A-322(1)(b)], SP-A's unperfected security interest will be junior to SP-B's perfected security interest. The award of priority to SP-B is premised on the belief that SP-A's failure to file could have misled SP-B.

5. **Taking Subject to Perfected Security Interest that Becomes Unperfected.** This section applies only if the security interest in the transferred collateral did not become unperfected at any time after the transferee acquired the collateral. See subsection (a)(3) [subsection (1)(c)]. If this condition is not met, then the normal priority rules apply.

Example 4: As in Example 1, A owns an item of equipment subject to a perfected security interest in favor of SP-A. A sells the equipment to B, not in the ordinary course of business. B acquires its interest subject to SP-A's security interest. See Sections 9-201, 9-315(a)(1) [30-9A-201 and 30-9A-315(1)(a)]. B creates a security interest in favor of SP-B, and SP-B perfects its security interest. This section provides that SP-A's security interest is senior to SP-B's. However, if SP-A's financing statement lapses while SP-B's security interest is perfected, then the normal priority rules would apply, and SP-B's security interest would become senior to SP-A's security interest. See Sections 9-322(a)(2), 9-515(c) [30-9A-322(1)(b) and 30-9A-515(3)].

6. **Unusual Situations.** The appropriateness of the rule of subsection (a) [subsection (1)] is most apparent when it works to subordinate security interests having priority under the basic priority rules of Section 9-322(a) [30-9A-322(1)] or the purchase-money priority rules of Section 9-324 [30-9A-324]. The rule also works properly when applied to the security interest of a buyer under Section 2-711(3) [30-2-711(3)] or a lessee under Section 2A-508(5) [30-2A-508(5)]. However, subsection (a) [subsection (1)] may provide an inappropriate resolution of the "double debtor" problem in some of the wide variety of other contexts in which the problem may arise. Although subsection (b) [subsection (2)] limits the application of subsection (a) [subsection (1)] to those cases in which subordination is known to be appropriate, courts should apply the rule in other settings, if necessary to promote the underlying purposes and policies of the Uniform Commercial Code. See Section 1-102(1) [30-1-102(1)].

30-9A-326. Priority of security interests created by new debtor.

Official Comments

1. **Source.** New.

2. **Subordination of Security Interests Created by New Debtor.** This section addresses the priority contests that may arise when a new debtor becomes bound by the security agreement of an original debtor and each debtor has a secured creditor.

Subsection (a) [subsection (1)] subordinates the original debtor's secured party's security interest perfected against the new debtor by a filed financing statement that would be ineffective to perfect the security interest but for Section 9-508 [30-9A-508] or, if the original debtor and new debtor are located in different jurisdictions, Section 9-316(i)(1) [30-9A-316(9)(a)]. The security interest is subordinated to security interests in the same collateral perfected by another method, e.g., by filing against the new debtor. This section does not subordinate a security interest perfected by a new initial financing statement providing the name of the new debtor, even if the initial financing statement is filed to maintain the effectiveness of a financing statement under the circumstances described in Section 9-508(b) [30-9A-508(2)]. Nor does it subordinate a security interest perfected by a financing statement filed against the original debtor which remains effective against collateral transferred by the original debtor to the new debtor. See Section 9-508(c) [30-9A-508(3)]. Concerning priority contests involving transferred collateral, see Sections 9-325 and 9-507 [30-9A-325 and 30-9A-507].

Example 1: SP-X holds a perfected-by-filing security interest in X Corp's existing and after-acquired inventory, and SP-Z holds a perfected-by-possession security interest in an item of Z Corp's inventory. Both X Corp and Z Corp are located in the same jurisdiction under Section 9-307 [30-9A-307]. Z Corp becomes bound as debtor by X Corp's security agreement (e.g., Z Corp buys X Corp's assets and assumes its security agreement). See Section 9-203(d) [30-9A-203(4)]. But for Section 9-508 [30-9A-508], SP-X's financing statement would be ineffective to perfect a security interest in the item of inventory in which Z Corp has rights. However, subsection (a) [subsection (1)] provides that SP-X's perfected security interest is subordinate to SP-Z's, regardless of whether SP-X's financing statement was filed before SP-Z perfected its security interest.

Example 2: SP-X holds a perfected-by-filing security interest in X Corp's existing and after-acquired inventory, and SP-Z holds a perfected-by-filing security interest in Z Corp's existing and after-acquired inventory. Both X Corp and Z Corp are located in the same jurisdiction under Section 9-307 [30-9A-307]. Z Corp becomes bound as debtor by X Corp's security agreement. Immediately thereafter, and before the effectiveness of SP-X's financing statement lapses, Z Corp acquires a new item of inventory. But for Section 9-508 [30-9A-508], SP-X's financing statement would be ineffective to perfect a security interest in the new item of inventory in which Z Corp has rights. However, because SP-Z's security interest was perfected by a filing whose effectiveness does not depend on Section 9-316(i)(1) [30-9A-316(9)(a)] or 9-508 [30-9A-508], subsection (a) [subsection (1)] subordinates SP-X's perfected security interest to SP-Z's. This would be the case even if SP-Z filed after Z Corp became bound by X Corp's security agreement, and regardless of which financing statement was filed first.

The same result would obtain if X Corp and Z Corp were located in different jurisdictions. SP-X's security interest would be perfected by a financing statement that would be ineffective but for Section 9-316(i)(1) [30-9A-316(9)(a)], whereas the effectiveness of SP-Z's filing does not depend on Section 9-316(i)(1) [30-9A-316(9)(a)] or 9-508 [30-9A-508].

3. **Other Priority Rules.** Subsection (b) [subsection (2)] addresses the priority among security interests created by the original debtor (X Corp). By invoking the other priority rules of this subpart, as applicable, subsection (b) [subsection (2)] preserves the relative priority of security interests created by the original debtor.

Example 3: Under the facts of Example 2, SP-Y also holds a perfected-by-filing security interest in X Corp's existing and after-acquired inventory. SP-Y filed after SP-X. Inasmuch as both SP-X's and SP-Y's security interests in inventory acquired by Z Corp after it became bound would be unperfected but for the application of Section 9-508 [30-9A-508], the normal priority rules determine their relative priorities. Under the "first-to-file-or-perfect" rule of Section 9-322(a)(1) [30-9A-322(1)(a)], SP-X has priority over SP-Y.

Example 4: Under the facts of Example 3, after Z Corp became bound by X Corp's security agreement, SP-Y promptly filed a new initial financing statement against Z Corp. SP-X's security interest remains perfected only by virtue of its original filing against X Corp which "would be ineffective to perfect the security interest but for the application of Section 9-508 [30-9A-508]." Because SP-Y's security interest is perfected by the filing of a financing statement whose effectiveness does not depend on Section 9-508 [30-9A-508] or 9-316(i)(1) [30-9A-316(9)(a)], subsection (a) [subsection (1)] subordinates SP-X's security interest to SP-Y's. If both SP-X and SP-Y file a new initial financing statement against Z Corp, then the "first-to-file-or-perfect" rule of Section 9-322(a)(1) [30-9A-322(1)(a)] governs their priority inter se as well as their priority against SP-Z.

The second sentence of subsection (b) [subsection (2)] effectively limits the applicability of the first sentence to situations in which a new debtor has become bound by more than one security agreement entered into by the same original debtor. When the new debtor has become bound by security agreements entered into by different original debtors, the second sentence provides that priority is based on priority in time of the new debtor's becoming bound.

Example 5: Under the facts of Example 2, SP-W holds a perfected-by-filing security interest in W Corp's existing and after-acquired inventory. After Z Corp became bound by X Corp's security agreement in favor of SP-X, Z Corp became bound by W Corp's security agreement. Under subsection (b) [subsection (2)], SP-W's security interest in inventory acquired by Z Corp is subordinate to that of SP-X, because Z Corp became bound under SP-X's security agreement before it became bound under SP-W's security agreement. This is the result regardless of which financing statement (SP-X's or SP-W's) was filed first.

The second sentence of subsection (b) [subsection (2)] reflects the generally accepted view that priority based on the first-to-file rule is inappropriate for resolving priority disputes when the filings were made against different debtors. Like subsection (a) [subsection (1)] and the first sentence of subsection (b) [subsection (2)], however, the second sentence of subsection (b) [subsection (2)] relates only to priority conflicts among security interests that would be unperfected but for the application of Section 9-316(i)(1) [30-9A-316(9)(a)] or 9-508 [30-9A-508].

Example 6: Under the facts of Example 5, after Z Corp became bound by W Corp's security agreement, SP-W promptly filed a new initial financing statement against Z Corp. At that time, SP-X's security interest was perfected only pursuant to its original filing against X Corp which "would be ineffective to perfect the security interest but for the application of Section 9-508 [30-9A-508]." Because SP-W's security interest is perfected by the filing of a financing statement whose effectiveness does not depend on Section 9-316(i)(1) [30-9A-316(9)(a)] or 9-508 [30-9A-508], subsection (a) [subsection (1)] subordinates SP-X's security interest to SP-W's. If both SP-X and SP-W file a new initial financing statement against Z Corp, then the "first-to-file-or-perfect" rule of Section 9-322(a)(1) [30-9A-322(1)(a)] governs their priority inter se as well as their priority against SP-Z.

Compiler's Comments

2013 Amendment: Chapter 75 in (1) substituted "in collateral in which the new debtor has or acquires rights and is perfected solely" for "perfected", substituted "would be ineffective to perfect the security interest but for the application of 30-9A-316(9)(a) or 30-9A-508" for "is effective solely under 30-9A-508 in collateral in which a new debtor has or acquires rights", and at end substituted "other than by such a filed financing statement" for "by another method"; in (2) substituted current language regarding other provisions of this part and conflicting security interests for "If more than one security interest in the same collateral is subordinate under subsection (1), the other provisions of this part, as applicable, determine the priority among the subordinated security interests"; and made minor changes in style. Amendment effective July 1, 2013.

Saving Clause: Section 26, Ch. 75, L. 2013, provided: "(1) Except as otherwise provided in [sections 19 through 25] [Title 30, chapter 9A, part 8], this chapter applies to a transaction or lien within its scope, even if the transaction or lien was entered into or created before [the effective of this act] [July 1, 2013].

(2) This chapter does not affect an action, case, or proceeding commenced before [the effective date of this act] [July 1, 2013]."

30-9A-327. Priority of security interests in deposit account.

Official Comments

1. **Source.** New; derived from former Section 9-115(5) [30-9-115(5), now repealed].

2. **Scope of This Section.** This section contains the rules governing the priority of conflicting security interests in deposit accounts. It overrides conflicting priority rules. See Sections 9-322(f)(1), 9-324(a), (b), (d), (f) [30-9A-322(6)(a) and 30-9A-324(1), (2), (4), and (6)]. This section does not apply to accounts evidenced by an instrument (e.g., certain certificates of deposit), which by definition are not "deposit accounts."

3. **Control.** Under paragraph (1) [subsection (1)], security interests perfected by control (Sections 9-314, 9-104 [30-9A-314 and 30-9A-104]) take priority over those perfected otherwise, e.g., as identifiable cash proceeds under Section 9-315 [30-9A-315]. Secured parties for whom the deposit account is an integral part of the credit decision will, at a minimum, insist upon the right to immediate access to the deposit account upon the debtor's default (i.e., control). Those secured parties for whom the deposit account is less essential will not take control, thereby running the risk that the debtor will dispose of funds on deposit (either outright or for collateral purposes) after default but before the account can be frozen by court order or the secured party can obtain control.

Paragraph (2) [subsection (2)] governs the case (expected to be very rare) in which a bank enters into a Section 9-104(a)(2) [30-9A-104(1)(b)] control agreement with more than one secured party. It provides that the security interests rank according to time of obtaining control. If the bank is solvent and the control agreements are well drafted, the bank will be liable to each secured party, and the priority rule will have no practical effect.

4. **Priority of Bank.** Under paragraph (3) [subsection (3)], the security interest of the bank with which the deposit account is maintained normally takes priority over all other conflicting security interests in the deposit account, regardless of whether the deposit account constitutes the competing secured party's original collateral or its proceeds. A rule of this kind enables banks to extend credit to their depositors without the need to examine either the public record or their own records to determine whether another party might have a security interest in the deposit account.

A secured party who takes a security interest in the deposit account as original collateral can protect itself against the results of this rule in one of two ways. It can take control of the deposit account by becoming the bank's customer. Under paragraph (4) [subsection (4)], this arrangement operates to subordinate the bank's security interest. Alternatively, the secured party can obtain a subordination agreement from the bank. See Section 9-339 [30-9A-339].

A secured party who claims the deposit account as proceeds of other collateral can reduce the risk of becoming junior by obtaining the debtor's agreement to deposit proceeds into a specific cash-collateral account and obtaining the agreement of that bank to subordinate all its claims to those of the secured party. But if the debtor violates its agreement and deposits funds into a deposit account other than the cash-collateral account, the secured party risks being subordinated.

5. **Priority in Proceeds of, and Funds Transferred from, Deposit Account.** The priority afforded by this section does not extend to proceeds of a deposit account. Rather, Section 9-322(c) through (e) [30-9A-322(3) through (5)] and the provisions referred to in Section 9-322(f) [30-9A-322(6)] govern priorities in proceeds of a deposit account. Section 9-315(d) [30-9A-315(4)] addresses continuation of perfection in proceeds of deposit accounts. As to funds transferred from a deposit account that serves as collateral, see Section 9-332 [30-9A-332].

30-9A-328. Priority of security interests in investment property.

Official Comments

1. **Source.** Former Section 9-115(5) [30-9-115(5), now repealed].

2. **Scope of This Section.** This section contains the rules governing the priority of conflicting security interests in investment property. Paragraph (1) [subsection 1] states the most important general rule-that a secured party who obtains control has priority over a secured party who does not obtain control. Paragraphs (2) through (4) [subsections (2) through (4)] deal with conflicting security interests each of which is perfected by control. Paragraph (5) [subsection (5)] addresses the priority of a security interest in a certificated security which is perfected by delivery but not control. Paragraph (6) [subsection (6)] deals with the relatively unusual circumstance in which a broker, securities intermediary, or commodity intermediary has created conflicting security interests none of which is perfected by control. Paragraph (7) [subsection (7)] provides that the general priority rules of Sections 9-322 and 9-323 [30-9A-322 and 30-9A-323] apply to cases not covered by the specific rules in this section. The principal application of this residual rule is that the usual first in time of filing rule applies to conflicting security interests that are perfected only by filing. Because the control priority rule of paragraph (1) [subsection (1)] provides for the ordinary cases in which persons purchase securities on margin credit from their brokers, there is no need for special rules for purchase-money security interests. See also Section 9-103 [30-9A-103] (limiting purchase-money collateral to goods and software).

3. **General Rule: Priority of Security Interest Perfected by Control.** Under paragraph (1) [subsection (1)], a secured party who obtains control has priority over a secured party who does not obtain control. The control priority rule does not turn on either temporal sequence or

awareness of conflicting security interests. Rather, it is a structural rule, based on the principle that a lender should be able to rely on the collateral without question if the lender has taken the necessary steps to assure itself that it is in a position where it can foreclose on the collateral without further action by the debtor. The control priority rule is necessary because the perfection rules provide considerable flexibility in structuring secured financing arrangements. For example, at the "retail" level, a secured lender to an investor who wants the full measure of protection can obtain control, but the creditor may be willing to accept the greater measure of risk that follows from perfection by filing. Similarly, at the "wholesale" level, a lender to securities firms can leave the collateral with the debtor and obtain a perfected security interest under the automatic perfection rule of Section 9-309(10) [30-9A-309(10)], but a lender who wants to be entirely sure of its position will want to obtain control. The control priority rule of paragraph (1) [subsection (1)] is an essential part of this system of flexibility. It is feasible to provide more than one method of perfecting security interests only if the rules ensure that those who take the necessary steps to obtain the full measure of protection do not run the risk of subordination to those who have not taken such steps. A secured party who is unwilling to run the risk that the debtor has granted or will grant a conflicting control security interest should not make a loan without obtaining control of the collateral.

As applied to the retail level, the control priority rule means that a secured party who obtains control has priority over a conflicting security interest perfected by filing without regard to inquiry into whether the control secured party was aware of the filed security interest. Prior to the 1994 revisions to Articles 8 and 9 [Title 30, chapters 8 and 9A], Article 9 [Title 30, chapter 9A] did not permit perfection of security interests in securities by filing. Accordingly, parties who deal in securities never developed a practice of searching the UCC files before conducting securities transactions. Although filing is now a permissible method of perfection, in order to avoid disruption of existing practices in this business it is necessary to give perfection by filing a different and more limited effect for securities than for some other forms of collateral. The priority rules are not based on the assumption that parties who perfect by the usual method of obtaining control will search the files. Quite the contrary, the control priority rule is intended to ensure that, with respect to investment property, secured parties who do obtain control are entirely unaffected by filings. To state the point another way, perfection by filing is intended to affect only general creditors or other secured creditors who rely on filing. The rule that a security interest perfected by filing can be primed by a control security interest, without regard to awareness, is a consequence of the system of perfection and priority rules for investment property. These rules are designed to take account of the circumstances of the securities markets, where filing is not given the same effect as for some other forms of property. No implication is made about the effect of filing with respect to security interests in other forms of property, nor about other Article 9 [Title 30, chapter 9A] rules, e.g., Section 9-330 [30-9A-330], which govern the circumstances in which security interests in other forms of property perfected by filing can be primed by subsequent perfected security interests.

The following examples illustrate the application of the priority rule in paragraph (1) [subsection (1)]:

Example 1: Debtor borrows from Alpha and grants Alpha a security interest in a variety of collateral, including all of Debtor's investment property. At that time Debtor owns 1000 shares of XYZ Co. stock for which Debtor has a certificate. Alpha perfects by filing. Later, Debtor borrows from Beta and grants Beta a security interest in the 1000 shares of XYZ Co. stock. Debtor delivers the certificate, properly indorsed, to Beta. Alpha and Beta both have perfected security interests in the XYZ Co. stock. Beta has control, see Section 8-106(b)(1) [30-8-116(2)(a)], and hence has priority over Alpha.

Example 2: Debtor borrows from Alpha and grants Alpha a security interest in a variety of collateral, including all of Debtor's investment property. At that time Debtor owns 1000 shares of XYZ Co. stock, held through a securities account with Able & Co. Alpha perfects by filing. Later, Debtor borrows from Beta and grants Beta a security interest in the 1000 shares of XYZ Co. stock. Debtor instructs Able to have the 1000 shares transferred through the clearing corporation to Custodian Bank, to be credited to Beta's account with Custodian Bank. Alpha and Beta both have perfected security interests in the XYZ Co. stock. Beta has control, see Section 8-106(d)(1) [30-8-116(4)(a)], and hence has priority over Alpha.

Example 3: Debtor borrows from Alpha and grants Alpha a security interest in a variety of collateral, including all of Debtor's investment property. At that time Debtor owns 1000 shares of XYZ Co. stock, which is held through a securities account with Able & Co. Alpha perfects by filing. Later, Debtor borrows from Beta and grants Beta a security interest in the 1000 shares of XYZ

Co. stock. Debtor, Able, and Beta enter into an agreement under which Debtor will continue to receive dividends and distributions, and will continue to have the right to direct dispositions, but Beta will also have the right to direct dispositions and receive the proceeds. Alpha and Beta both have perfected security interests in the XYZ Co. stock (more precisely, in the Debtor's security entitlement to the financial asset consisting of the XYZ Co. stock). Beta has control, see Section 8-106(d)(2) [30-8-116(4)(b)], and hence has priority over Alpha.

Example 4: Debtor borrows from Alpha and grants Alpha a security interest in a variety of collateral, including all of Debtor's investment property. At that time Debtor owns 1000 shares of XYZ Co. stock, held through a securities account with Able & Co. Alpha perfects by filing. Debtor's agreement with Able & Co. provides that Able has a security interest in all securities carried in the account as security for any obligations of Debtor to Able. Debtor incurs obligations to Able and later defaults on the obligations to Alpha and Able. Able has control by virtue of the rule of Section 8-106(e) [30-8-116(5)] that if a customer grants a security interest to its own intermediary, the intermediary has control. Since Alpha does not have control, Able has priority over Alpha under the general control priority rule of paragraph (1) [subsection (1)].

4. **Conflicting Security Interests Perfected by Control: Priority of Securities Intermediary or Commodity Intermediary.** Paragraphs (2) through (4) [subsections (2) through (4)] govern the priority of conflicting security interests each of which is perfected by control. The following example explains the application of the rules in paragraphs (3) and (4) [subsections (3) and (4)]:

Example 5: Debtor holds securities through a securities account with Able & Co. Debtor's agreement with Able & Co. provides that Able has a security interest in all securities carried in the account as security for any obligations of Debtor to Able. Debtor borrows from Beta and grants Beta a security interest in 1000 shares of XYZ Co. stock carried in the account. Debtor, Able, and Beta enter into an agreement under which Debtor will continue to receive dividends and distributions and will continue to have the right to direct dispositions, but Beta will also have the right to direct dispositions and receive the proceeds. Debtor incurs obligations to Able and later defaults on the obligations to Beta and Able. Both Beta and Able have control, so the general control priority rule of paragraph (1) [subsection (1)] does not apply. Compare Example 4. Paragraph (3) [subsection (3)] provides that a security interest held by a securities intermediary in positions of its own customer has priority over a conflicting security interest of an external lender, so Able has priority over Beta. (Paragraph (4) [subsection (4)] contains a parallel rule for commodity intermediaries.) The agreement among Able, Beta, and Debtor could, of course, determine the relative priority of the security interests of Able and Beta, see Section 9-339 [30-9A-339], but the fact that the intermediary has agreed to act on the instructions of a secured party such as Beta does not itself imply any agreement by the intermediary to subordinate.

5. **Conflicting Security Interests Perfected by Control: Temporal Priority.** Former Section 9-115 [30-9-115, now repealed] introduced into Article 9 [Title 30, chapter 9A] the concept of conflicting security interests that rank equally. Paragraph (2) [subsection (2)] of this section governs priority in those circumstances in which more than one secured party (other than a broker, securities intermediary, or commodity intermediary) has control. It replaces the equal-priority rule for conflicting security interests in investment property with a temporal rule. For securities, both certificated and uncertificated, under paragraph (2)(A) [subsection (2)(a)] priority is based on the time that control is obtained. For security entitlements carried in securities accounts, the treatment is more complex. Paragraph (2)(B) [subsection (2)(b)] bases priority on the timing of the steps taken to achieve control. The following example illustrates the application of paragraph (2) [subsection (2)].

Example 6: Debtor borrows from Alpha and grants Alpha a security interest in a variety of collateral, including all of Debtor's investment property. At that time Debtor owns a security entitlement that includes 1000 shares of XYZ Co. stock that Debtor holds through a securities account with Able & Co. Debtor, Able, and Alpha enter into an agreement under which Debtor will continue to receive dividends and distributions, and will continue to have the right to direct dispositions, but Alpha will also have the right to direct dispositions and receive the proceeds. Later, Debtor borrows from Beta and grants Beta a security interest in all its investment property, existing and after-acquired. Debtor, Able, and Beta enter into an agreement under which Debtor will continue to receive dividends and distributions, and will continue to have the right to direct dispositions, but Beta will also have the right to direct dispositions and receive the proceeds. Alpha and Beta both have perfected-by-control security interests in the security entitlement to the XYZ Co. stock by virtue of their agreements with Able. See Sections 9-314(a), 9-106(a), 8-106(d)(2) [30-9A-314(1), 30-9A-106(1), 30-8-116(4)(b)]. Under paragraph (2)(B)(ii) [subsection (2)(b)(ii)], the priority of each security interest dates from the time of the secured party's agreement with Able. Because Alpha's agreement was first in time, Alpha has priority. This priority applies equally to security entitlements to financial assets credited to the account after the agreement was entered into.

The priority rule is analogous to "first-to-file" priority under Section 9-322 [30-9A-322] with respect to after-acquired collateral. Paragraphs (2)(B)(i) and (2)(B)(iii) [subsections (2)(b)(i) and (2)(b)(iii)] provide similar rules for security entitlements as to which control is obtained by other methods, and paragraph (2)(C) [subsection (2)(c)] provides a similar rule for commodity contracts carried in a commodity account. Section 8-510 [30-8-510] also has been revised to provide a temporal priority conforming to paragraph (2)(B) [subsection (2)(b)].

6. **Certificated Securities.** A long-standing practice has developed whereby secured parties whose collateral consists of a security evidenced by a security certificate take possession of the security certificate. If the security certificate is in bearer form, the secured party's acquisition of possession constitutes "delivery" under Section 8-301(a)(1) [30-8-331(1)(a)], and the delivery constitutes "control" under Section 8-106(a) [30-8-116(1)]. Comment 5 discusses the priority of security interests perfected by control of investment property.

If the security certificate is in registered form, the secured party will not achieve control over the security unless the security certificate contains an appropriate indorsement or is (re) registered in the secured party's name. See Section 8-106(b) [30-8-116(2)]. However, the secured party's acquisition of possession constitutes "delivery" of the security certificate under Section 8-301 [30-8-331] and serves to perfect the security interest under Section 9-313(a) [30-9A-313(1)], even if the security certificate has not been appropriately indorsed and has not been (re)registered in the secured party's name. A security interest perfected by this method has priority over a security interest perfected other than by control (e.g., by filing). See paragraph (5) [subsection (5)].

The priority rule stated in paragraph (5) [subsection (5)] may seem anomalous, in that it can afford less favorable treatment to purchasers who buy collateral outright that to those who take a security interest in it. For example, a buyer of a security certificate would cut off a security interest perfected by filing only if the buyer achieves the status of a protected purchaser under Section 8-303 [30-8-333]. The buyer would not be a protected purchaser, for example, if it does not obtain "control" under Section 8-106 [30-8-116] (e.g., if it fails to obtain a proper indorsement of the certificate) or if it had notice of an adverse claim under Section 8-105 [30-8-115]. The apparent anomaly disappears, however, when one understands the priority rule not as one intended to protect careless or guilty parties, but as one that eliminates the need to conduct a search of the public records only insofar as necessary to serve the needs of the securities markets.

7. **Secured Financing of Securities Firms.** Priority questions concerning security interests granted by brokers and securities intermediaries are governed by the general control-beats-non-control priority rule of paragraph (1) [subsection (1)], as supplemented by the special rules set out in paragraphs (2) [subsection (2)] (temporal priority-first to control), (3) [subsection (3)] (special priority for securities intermediary), and (6) [subsection (6)] (equal priority for non-control). The following examples illustrate the priority rules as applied to this setting. (In all cases it is assumed that the debtor retains sufficient other securities to satisfy all customers' claims. This section deals with the relative rights of secured lenders to a securities firm. Disputes between a secured lender and the firm's own customers are governed by Section 8-511 [30-8-511].)

Example 7: Able & Co., a securities dealer, enters into financing arrangements with two lenders, Alpha Bank and Beta Bank. In each case the agreements provide that the lender will have a security interest in the securities identified on lists provided to the lender on a daily basis, that the debtor will deliver the securities to the lender on demand, and that the debtor will not list as collateral any securities which the debtor has pledged to any other lender. Upon Able's insolvency it is discovered that Able has listed the same securities on the collateral lists provided to both Alpha and Beta. Alpha and Beta both have perfected security interests under the automatic-perfection rule of Section 9-309(10) [30-9A-309(10)]. Neither Alpha nor Beta has control. Paragraph (6) [subsection (6)] provides that the security interests of Alpha and Beta rank equally, because each of them has a non-control security interest granted by a securities firm. They share pro-rata.

Example 8: Able enters into financing arrangements, with Alpha Bank and Beta Bank as in Example 7. At some point, however, Beta decides that it is unwilling to continue to provide financing on a non-control basis. Able directs the clearing corporation where it holds its principal inventory of securities to move specified securities into Beta's account. Upon Able's insolvency it is discovered that a list of collateral provided to Alpha includes securities that had been moved to Beta's account. Both Alpha and Beta have perfected security interests; Alpha under the automatic-perfection rule of Section 9-309(10) [30-9A-309(10)], and Beta under that rule and also the perfection-by-control rule in Section 9-314(a) [30-9A-314(1)]. Beta has control but Alpha does not. Beta has priority over Alpha under paragraph (1) [subsection (1)].

Example 9: Able & Co. carries its principal inventory of securities through Clearing Corporation, which offers a "shared control" facility whereby a participant securities firm can enter into an arrangement with a lender under which the securities firm will retain the power to trade and otherwise direct dispositions of securities carried in its account, but Clearing Corporation agrees that, at any time the lender so directs, Clearing Corporation will transfer any securities from the firm's account to the lender's account or otherwise dispose of them as directed by the lender. Able enters into financing arrangements with two lenders, Alpha and Beta, each of which obtains such a control agreement from Clearing Corporation. The agreement with each lender provides that Able will designate specific securities as collateral on lists provided to the lender on a daily or other periodic basis, and that it will not pledge the same securities to different lenders. Upon Able's insolvency, it is discovered that Able has listed the same securities on the collateral lists provided to both Alpha and Beta. Both Alpha and Beta have control over the disputed securities. Paragraph (2) [subsection (2)] awards priority to whichever secured party first entered into the agreement with Clearing Corporation.

8. **Relation to Other Law.** Section 1-103 [30-1-103] provides that "unless displaced by particular provisions of this Act, the principles of law and equity . . . shall supplement its provisions." There may be circumstances in which a secured party's action in acquiring a security interest that has priority under this section constitutes conduct that is wrongful under other law. Though the possibility of such resort to other law may provide an appropriate "escape valve" for cases of egregious conduct, care must be taken to ensure that this does not impair the certainty and predictability of the priority rules. Whether a court may appropriately look to other law to impose liability upon or estop a secured party from asserting its Article 9 [Title 30, chapter 9A] priority depends on an assessment of the secured party's conduct under the standards established by such other law as well as a determination of whether the particular application of such other law is displaced by the UCC.

Some circumstances in which other law is clearly displaced by the UCC rules are readily identifiable. Common law "first in time, first in right" principles, or correlative tort liability rules such as common law conversion principles under which a purchaser may incur liability to a person with a prior property interest without regard to awareness of that claim, are necessarily displaced by the priority rules set out in this section since these rules determine the relative ranking of security interests in investment property. So too, Article 8 [Title 30, chapter 8] provides protections against adverse claims to certain purchasers of interests in investment property. In circumstances where a secured party not only has priority under Section 9-328 [30-9A-328], but also qualifies for protection against adverse claims under Section 8-303, 8-502, or 8-510 [30-8-333, 30-8-502, or 30-8-510], resort to other law would be precluded.

In determining whether it is appropriate in a particular case to look to other law, account must also be taken of the policies that underlie the commercial law rules on securities markets and security interests in securities. A principal objective of the 1994 revision of Article 8 [Title 30, chapter 8] and the provisions of Article 9 [Title 30, chapter 9A] governing investment property was to ensure that secured financing transactions can be implemented on a simple, timely, and certain basis. One of the circumstances that led to the revision was the concern that uncertainty in the application of the rules on secured transactions involving securities and other financial assets could contribute to systemic risk by impairing the ability of financial institutions to provide liquidity to the markets in times of stress. The control priority rule is designed to provide a clear and certain rule to ensure that lenders who have taken the necessary steps to establish control do not face a risk of subordination to other lenders who have not done so.

The control priority rule does not turn on an inquiry into the state of a secured party's awareness of potential conflicting claims because a rule under which a person's rights depended on that sort of after-the-fact inquiry could introduce an unacceptable measure of uncertainty. If an inquiry into awareness could provide a complete and satisfactory resolution of the problem in all cases, the priority rules of this section would have incorporated that test. The fact that they do not necessarily means that resort to other law based solely on that factor is precluded, though the question whether a control secured party induced or encouraged its financing arrangement with actual knowledge that the debtor would be violating the rights of another secured party may, in some circumstances, appropriately be treated as a factor in determining whether the control party's action is the kind of egregious conduct for which resort to other law is appropriate.

30-9A-329. Priority of security interests in letter-of-credit right.

Official Comments

1. **Source.** New; loosely modeled after former Section 9-115(5) [30-9-115(5), now repealed].

2. **General Rule.** Paragraph (1) [subsection (1)] awards priority to a secured party who perfects a security interest directly in letter-of-credit rights (i.e., one that takes an assignment of proceeds and obtains consent of the issuer or any nominated person under Section 5-114(c) [30-5-134(3)]) over another conflicting security interest (i.e., one that is perfected automatically in the letter-of-credit rights as supporting obligations under Section 9-308(d) [30-9A-308(4)]). This is consistent with international letter-of-credit practice and provides finality to payments made to recognized assignees of letter-of-credit proceeds. If an issuer or nominated person recognizes multiple security interests in a letter-of-credit right, resulting in multiple parties having control (Section 9-107 [30-9A-107]), under paragraph (2) [subsection (2)] the security interests rank according to the time of obtaining control.

3. **Drawing Rights; Transferee Beneficiaries.** Drawing under a letter of credit is personal to the beneficiary and requires the beneficiary to perform the conditions for drawing under the letter of credit. Accordingly, a beneficiary's grant of a security interest in a letter of credit includes the beneficiary's "letter-of-credit right" as defined in Section 9-102 [30-9A-102] and the right to "proceeds of [the] letter of credit" as defined in Section 5-114(a) [30-5-134(1)], but does not include the right to demand payment under the letter of credit.

Section 5-114(e) [30-5-134(5)] provides that the "[r]ights of a transferee beneficiary or nominated person are independent of the beneficiary's assignment of the proceeds of a letter of credit and are superior to the assignee's right to the proceeds." To the extent the rights of a transferee beneficiary or nominated person are independent and superior, this Article [Title 30, chapter 9A] does not apply. See Section 9-109(c) [30-9A-109(3)].

Under Article 5 [Title 30, chapter 5], there is in effect a novation upon the transfer with the issuer becoming bound on a new, independent obligation to the transferee. The rights of nominated persons and transferee beneficiaries under a letter of credit include the right to demand payment from the issuer. Under Section 5-114(e) [30-5-134(5)], their rights to payment are independent of their obligations to the beneficiary (or original beneficiary) and superior to the rights of assignees of letter-of-credit proceeds (Section 5-114(c) [30-5-134(3)]) and others claiming a security interest in the beneficiary's (or original beneficiary's) letter-of-credit rights.

A transfer of drawing rights under a transferable letter of credit establishes independent Article 5 [Title 30, chapter 5] rights in the transferee and does not create or perfect an Article 9 [Title 30, chapter 9A] security interest in the transferred drawing rights. The definition of "letter-of-credit right" in Section 9-102 [30-9A-102] excludes a beneficiary's drawing rights. The exercise of drawing rights by a transferee beneficiary may breach a contractual obligation of the transferee to the original beneficiary concerning when and how much the transferee may draw or how it may use the funds received under the letter of credit. If, for example, drawing rights are transferred to support a sale or loan from the transferee to the original beneficiary, then the transferee would be obligated to the original beneficiary under the sale or loan agreement to account for any drawing and for the use of any funds received. The transferee's obligation would be governed by the applicable law of contracts or restitution.

4. **Secured Party-Transferee Beneficiaries.** As described in Comment 3, drawing rights under letters of credit are transferred in many commercial contexts in which the transferee is not a secured party claiming a security interest in an underlying receivable supported by the letter of credit. Consequently, a transfer of a letter of credit is not a method of "perfection" of a security interest. The transferee's independent right to draw under the letter of credit and to receive and retain the value thereunder (in effect, priority) is not based on Article 9 [Title 30, chapter 9A] but on letter-of-credit law and the terms of the letter of credit. Assume, however, that a secured party does hold a security interest in a receivable that is owned by a beneficiary-debtor and supported by a transferable letter of credit. Assume further that the beneficiary-debtor causes the letter of credit to be transferred to the secured party, the secured party draws under the letter of credit, and, upon the issuer's payment to the secured party-transferee, the underlying account debtor's obligation to the original beneficiary-debtor is satisfied. In this situation, the payment to the secured party-transferee is proceeds of the receivable collected by the secured party-transferee. Consequently, the secured party-transferee would have certain duties to the debtor and third parties under Article 9 [Title 30, chapter 9A]. For example, it would be obliged to collect under the letter of credit in a commercially reasonable manner and to remit any surplus pursuant to Sections 9-607 and 9-608 [30-9A-607 and 30-9A-608].

This scenario is problematic under letter-of-credit law and practice, inasmuch as a transferee beneficiary collects in its own right arising from its own performance. Accordingly, under Section 5-114 [30-5-134], the independent and superior rights of a transferee control over any inconsistent duties under Article 9 [Title 30, chapter 9A]. A transferee beneficiary may take a transfer of drawing rights to avoid reliance on the original beneficiary's credit and collateral, and it may consider any Article 9 [Title 30, chapter 9A] rights superseded by its Article 5 [Title 30, chapter 5] rights. Moreover, it will not always be clear (i) whether a transferee beneficiary has a security interest in the underlying collateral, (ii) whether any security interest is senior to the rights of others, or (iii) whether the transferee beneficiary is aware that it holds a security interest. There will be clear cases in which the role of a transferee beneficiary as such is merely incidental to a conventional secured financing. There also will be cases in which the existence of a security interest may have little to do with the position of a transferee beneficiary as such. In dealing with these cases and less clear cases involving the possible application of Article 9 [Title 30, chapter 9A] to a nominated person or a transferee beneficiary, the right to demand payment under a letter of credit should be distinguished from letter-of-credit rights. The courts also should give appropriate consideration to the policies and provisions of Article 5 [Title 30, chapter 5] and letter-of-credit practice as well as Article 9 [Title 30, chapter 9A].

30-9A-330. Purchase of chattel paper or instrument.

Official Comments

1. **Source.** Former Section 9-308 [30-9-308, now repealed].

2. **Non-Temporal Priority.** This Article [Title 30, chapter 9A] permits a security interest in chattel paper or instruments to be perfected either by filing or by the secured party's taking possession. This section enables secured parties and other purchasers of chattel paper (both electronic and tangible) and instruments to obtain priority over earlier-perfected security interests, thereby promoting the negotiability of these types of receivables.

3. **Chattel Paper.** Subsections (a) and (b) [subsections (1) and (2)] follow former Section 9-308 [30-9-308, now repealed] in distinguishing between earlier-perfected security interests in chattel paper that is claimed merely as proceeds of inventory subject to a security interest and chattel paper that is claimed other than merely as proceeds. Like former Section 9-308 [30-9-308, now repealed], this section does not elaborate upon the phrase "merely as proceeds." For an elaboration, see PEB Commentary No. 8.

This section makes explicit the "good faith" requirement and retains the requirements of "the ordinary course of the purchaser's business" and the giving of "new value" as conditions for priority. Concerning the last, this Article [Title 30, chapter 9A] deletes former Section 9-108 [30-9-108, now repealed] and adds to Section 9-102 [30-9A-102] a completely different definition of the term "new value." Under subsection (e) [subsection (5)], the holder of a purchase-money security interest in inventory is deemed to give "new value" for chattel paper constituting the proceeds of the inventory. Accordingly, the purchase-money secured party may qualify for priority in the chattel paper under subsection (a) or (b) [subsection (1) or (2)], whichever is applicable, even if it does not make an additional advance against the chattel paper.

If a possessory security interest in tangible chattel paper or a perfected-by-control security interest in electronic chattel paper does not qualify for priority under this section, it may be subordinate to a perfected-by-filing security interest under Section 9-322(a)(1) [30-9A-322(1)(a)].

4. **Possession and Control.** To qualify for priority under subsection (a) or (b) [subsection (1) or (2)], a purchaser must "take[ ] possession of the chattel paper or obtain[ ] control of the chattel paper under Section 9-105 [30-9A-105]." When chattel paper comprises one or more tangible records and one or more electronic records, a purchaser may satisfy the possession-or-control requirement by taking possession of the tangible records under Section 9-313 [30-9A-313] and having control of the electronic records under Section 9-105 [30-9A-105]. In determining which of several related records constitutes chattel paper and thus is relevant to possession or control, the form of the records is irrelevant. Rather, the touchstone is whether possession or control of the record would afford the public notice contemplated by the possession and control requirements. For example, because possession or control of an amendment extending the term of a lease would not afford the contemplated public notice, the amendment would not constitute chattel paper regardless of whether the amendment is in tangible form and the lease is in electronic form, the amendment is electronic and the lease is tangible, the amendment and lease are both tangible, or the amendment and lease are both electronic.

Two common practices have raised particular concerns with respect to the provision requirement. First, in some cases the parties create more than one copy or counterpart of chattel paper evidencing a single secured obligation or lease. This practice raises questions as to which counterpart is the "original" and whether it is necessary for a purchaser to take possession of all counterparts in order to "take possession" of the chattel paper. Second, parties sometimes enter into a single "master" agreement. The master agreement contemplates that the parties will enter into separate "schedules" from time to time, each evidencing chattel paper. Must a purchaser of an obligation or lease evidenced by a single schedule also take possession of the master agreement as well as the schedule in order to "take possession" of the chattel paper?

The problem raised by the first practice is easily solved. The parties may in the terms of their agreement and by designation on the chattel paper identify only one counterpart as the original chattel paper for purposes of taking possession of the chattel paper. Concerns about the second practice also are easily solved by careful drafting. Each schedule should provide that it incorporates the terms of the master agreement, not the other way around. This will make it clear that each schedule is a "stand alone" document.

A secured party may wish to convert tangible chattel paper to electronic chattel paper and vice versa. The priority of a security interest in chattel paper under subsection (a) or (b) [subsection (1) or (2)] may be preserved, even if the form of the chattel paper changes. The principle implied in the preceding paragraph, i.e., that not every copy of chattel paper is relevant, applies to "control" as well as to "possession." When there are multiple copies of chattel paper, a secured party may take "possession" or obtain "control" of the chattel paper if it acts with respect to the copy or copies that are reliably identified as the copy or copies that are relevant for purposes of possession or control. This principle applies as well to chattel paper that has been converted from one form to another, even if the relevant copies are not the "original" chattel paper.

5. **Chattel Paper Claimed Merely as Proceeds.** Subsection (a) [subsection (1)] revises the rule in former Section 9-308(b) [30-9A-308(2)] to eliminate reference to what the purchaser knows. Instead, a purchaser who meets the possession or control, ordinary course, and new value requirements takes priority over a competing security interest unless the chattel paper itself indicates that it has been assigned to an identified assignee other than the purchaser. Thus subsection (a) [subsection (1)] recognizes the common practice of placing a "legend" on chattel paper to indicate that it has been assigned. This approach, under which the chattel paper purchaser who gives new value in ordinary course can rely on possession of unlegended, tangible chattel paper without any concern for other facts that it may know, comports with the expectations of both inventory and chattel paper financers.

6. **Chattel Paper Claimed Other Than Merely as Proceeds.** Subsection (b) [subsection (2)] eliminates the requirement that the purchaser take without knowledge that the "specific paper" is subject to the security interest and substitutes for it the requirement that the purchaser take "without knowledge that the purchase violates the rights of the secured party." This standard derives from the definition of "buyer in ordinary course of business" in Section 1-201(b)(9) [30-1-201(2)(j)]. The source of the purchaser's knowledge is irrelevant. Note, however, that "knowledge" means "actual knowledge." Section 1-202(b) [30-1-210(2)].

In contrast to a junior secured party in accounts, who may be required in some special circumstances to undertake a search under the "good faith" requirement, see Comment 5 to Section 9-331 [30-9A-331], a purchaser of chattel paper under this section is not required as a matter of good faith to make a search in order to determine the existence of prior security interests. There may be circumstances where the purchaser undertakes a search nevertheless, either on its own volition or because other considerations make it advisable to do so, e.g., where the purchaser also is purchasing accounts. Without more, a purchaser of chattel paper who has seen a financing statement covering the chattel paper or who knows that the chattel paper is encumbered with a security interest, does not have knowledge that its purchase violates the secured party's rights. However, if a purchaser sees a statement in a financing statement to the effect that a purchase of chattel paper from the debtor would violate the rights of the filed secured party, the purchaser would have such knowledge. Likewise, under new subsection (f) [subsection (6)], if the chattel paper itself indicates that it had been assigned to an identified secured party other than the purchaser, the purchaser would have wrongful knowledge for purposes of subsection (b) [subsection (2)], thereby preventing the purchaser from qualifying for priority under that subsection, even if the purchaser did not have actual knowledge. In the case of tangible chattel paper, the indication normally would consist of a written legend on the chattel paper. In the case of electronic chattel paper, this Article [Title 30, chapter 9A] leaves to developing market and technological practices the manner in which the chattel paper would indicate an assignment.

7. **Instruments.** Subsection (d) [subsection (4)] contains a special priority rule for instruments. Under this subsection, a purchaser of an instrument has priority over a security interest perfected by a method other than possession (e.g., by filing, temporarily under Section 9-312(e) or (g) [30-9A-312(5) or (7)], as proceeds under Section 9-315(d) [30-9A-315(4)], or automatically upon attachment under Section 9-309(4) [30-9A-309(4)] if the security interest arises out of a sale of the instrument) if the purchaser gives value and takes possession of the instrument in good faith and without knowledge that the purchase violates the rights of the secured party. Generally, to the extent subsection (d) [subsection (4)] conflicts with Section 3-306 [30-3-306], subsection (d) [subsection (4)] governs. See Section 3-102(b) [30-3-102(2)]. For example, notice of a conflicting security interest precludes a purchaser from becoming a holder in due course under Section 3-302 [30-3-202] and thereby taking free of all claims to the instrument under Section 3-306 [30-3-306]. However, a purchaser who takes even with knowledge of the security interest qualifies for priority under subsection (d) [subsection (4)] if it takes without knowledge that the purchase violates the rights of the holder of the security interest. Likewise, a purchaser qualifies for priority under subsection (d) [subsection (4)] if it takes for "value" as defined in Section 1-201 [30-1-201], even if it does not take for "value" as defined in Section 3-303 [30-3-303].

Subsection (d) [subsection (4)] is subject to Section 9-331(a) [30-9A-331(1)], which provides that Article 9 [Title 30, chapter 9A] does not limit the rights of a holder in due course under Article 3 [Title 30, chapter 3]. Thus, in the rare case in which the purchaser of an instrument qualifies for priority under subsection (d) [subsection (4)], but another person has the rights of a holder in due course of the instrument, the other person takes free of the purchaser's claim. See Section 3-306 [30-3-306].

The rule in subsection (d) [subsection (4)] is similar to the rules in subsections (a) and (b) [subsections (1) and (2)], which govern priority in chattel paper. The observations in Comment 6 concerning the requirement of good faith and the phrase "without knowledge that the purchase violates the rights of the secured party" apply equally to purchasers of instruments. However, unlike a purchaser of chattel paper, to qualify for priority under this section a purchaser of an instrument need only give "value" as defined in Section 1-201 [30-1-201]; it need not give "new value." Also, the purchaser need not purchase the instrument in the ordinary course of its business.

Subsection (d) [subsection (4)] applies to checks as well as notes. For example, to collect and retain checks that are proceeds (collections) of accounts free of a senior secured party's claim to the same checks, a junior secured party must satisfy the good-faith requirement (honesty in fact and the observance of reasonable commercial standards of fair dealing) of this subsection. This is the same good-faith requirement applicable to holders in due course. See Section 9-331 [30-9A-331], Comment 5.

8. **Priority in Proceeds of Chattel Paper.** Subsection (c) [subsection (3)] sets forth the two circumstances under which the priority afforded to a purchaser of chattel paper under subsection (a) or (b) [subsection (1) or (2)] extends also to proceeds of the chattel paper. The first is if the purchaser would have priority under the normal priority rules applicable to proceeds. The second, which the following Comments discuss in greater detail, is if the proceeds consist of the specific goods covered by the chattel paper. Former Article 9 [Title 30, chapter 9, now repealed] generally was silent as to the priority of a security interest in proceeds when a purchaser qualifies for priority under Section 9-308 [30-9A-308] (but see former Section 9-306(5)(b) [30-9-306(5)(b), now repealed, see 30-9A-315], concerning returned and repossessed goods).

9. **Priority in Returned and Repossessed Goods.** Returned and repossessed goods may constitute proceeds of chattel paper. The following Comments explain the treatment of returned and repossessed goods as proceeds of chattel paper. The analysis is consistent with that of PEB Commentary No. 5, which these Comments replace, and is based upon the following example:

Example: SP-1 has a security interest in all the inventory of a dealer in goods (Dealer); SP-1's security interest is perfected by filing. Dealer sells some of its inventory to a buyer in the ordinary course of business (BIOCOB) pursuant to a conditional sales contract (chattel paper) that does not indicate that it has been assigned to SP-1. SP-2 purchases the chattel paper from Dealer and takes possession of the paper in good faith, in the ordinary course of business, and without knowledge that the purchase violates the rights of SP-1. Subsequently, BIOCOB returns the goods to Dealer because they are defective. Alternatively, Dealer acquires possession of the goods following BIOCOB's default.

10. Assignment of Non-Lease Chattel Paper.

a. **Loan by SP-2 to Dealer Secured by Chattel Paper (or Functional Equivalent Pursuant to Recourse Arrangement).**

(1) **Returned Goods.** If BIOCOB returns the goods to Dealer for repairs, Dealer is merely a bailee and acquires thereby no meaningful rights in the goods to which SP-1's security interest could attach. (Although SP-1's security interest could attach to Dealer's interest as a bailee, that interest is not likely to be of any particular value to SP-1.) Dealer is the owner of the chattel paper (i.e., the owner of a right to payment secured by a security interest in the goods); SP-2 has a security interest in the chattel paper, as does SP-1 (as proceeds of the goods under Section 9-315 [30-9A-315]). Under Section 9-330 [30-9A-330], SP-2's security interest in the chattel paper is senior to that of SP-1. SP-2 enjoys this priority regardless of whether, or when, SP-2 filed a financing statement covering the chattel paper. Because chattel paper and goods represent different types of collateral, Dealer does not have any meaningful interest in goods to which either SP-1's or SP-2's security interest could attach in order to secure Dealer's obligations to either creditor. See Section 9-102 [30-9A-102] (defining "chattel paper" and "goods").

Now assume that BIOCOB returns the goods to Dealer under circumstances whereby Dealer once again becomes the owner of the goods. This would be the case, for example, if the goods were defective and BIOCOB was entitled to reject or revoke acceptance of the goods. See Sections 2-602 [30-2-602] (rejection), 2-608 [30-2-608] (revocation of acceptance). Unless BIOCOB has waived its defenses as against assignees of the chattel paper, SP-1's and SP-2's rights against BIOCOB would be subject to BIOCOB's claims and defenses. See Sections 9-403, 9-404 [30-9A-403 and 30-9A-404]. SP-1's security interest would attach again because the returned goods would be proceeds of the chattel paper. Dealer's acquisition of the goods easily can be characterized as "proceeds" consisting of an "in kind" collection on or distribution on account of the chattel paper. See Section 9-102 [30-9A-102] (definition of "proceeds"). Assuming that SP-1's security interest is perfected by filing against the goods and that the filing is made in the same office where a filing would be made against the chattel paper, SP-1's security interest in the goods would remain perfected beyond the 20-day period of automatic perfection. See Section 9-315(e) [30-9A-315(5)].

Because Dealer's newly reacquired interest in the goods is proceeds of the chattel paper, SP-2's security interest also would attach in the goods as proceeds. If SP-2 had perfected its security interest in the chattel paper by filing (again, assuming that filing against the chattel paper was made in the same office where a filing would be made against the goods), SP-2's security interest in the reacquired goods would be perfected beyond 20 days. See Section 9-315(e) [30-9A-315(5)]. However, if SP-2 had relied only on its possession of the chattel paper for perfection and had not filed against the chattel paper or the goods, SP-2's security interest would be unperfected after the 20-day period. See Section 9-315(e) [30-9A-315(5)]. Nevertheless, SP-2's unperfected security interest in the goods would be senior to SP-1's security interest under Section 9-330(c) [30-9A-330(3)]. The result in this priority contest is not affected by SP-2's acquiescence or non-acquiescence in the return of the goods to Dealer.

(2) **Repossessed Goods.** As explained above, Dealer owns the chattel paper covering the goods, subject to security interests in favor of SP-1 and SP-2. In Article 9 [Title 30, chapter 9A] parlance, Dealer has an interest in chattel paper, not goods. If Dealer, SP-1, or SP-2 repossesses the goods upon BIOCOB's default, whether the repossession is rightful or wrongful as among Dealer, SP-1, or SP-2, Dealer's interest will not change. The location of goods and the party who possesses them does not affect the fact that Dealer's interest is in chattel paper, not goods. The goods continue to be owned by BIOCOB. SP-1's security interest in the goods does not attach until such time as Dealer reacquires an interest (other than a bare possessory interest) in the goods. For example, Dealer might buy the goods at a foreclosure sale from SP-2 (whose security interest in the chattel paper is senior to that of SP-1); that disposition would cut off BIOCOB's rights in the goods. Section 9-617 [30-9A-617].

In many cases the matter would end upon sale of the goods to Dealer at a foreclosure sale and there would be no priority contest between SP-1 and SP-2; Dealer would be unlikely to buy the goods under circumstances whereby SP-2 would retain its security interest. There can be exceptions, however. For example, Dealer may be obliged to purchase the goods from SP-2 and SP-2 may be obliged to convey the goods to Dealer, but Dealer may fail to pay SP-2. Or, one could imagine that SP-2, like SP-1, has a general security interest in the inventory of Dealer. In the latter case, SP-2 should not receive the benefit of any special priority rule, since its interest in no way derives from priority under Section 9-330 [30-9A-330]. In the former case, SP-2's security interest in the goods reacquired by Dealer is senior to SP-1's security interest under Section 9-330 [30-9A-330].

b. **Dealer's Outright Sale of Chattel Paper to SP-2.** Article 9 [Title 30, chapter 9A] also applies to a transaction whereby SP-2 buys the chattel paper in an outright sale transaction without recourse against Dealer. Sections 1-201(37), 9-109(a) [30-1-201(37), 30-9A-109(1)]. Although Dealer does not, in such a transaction, retain any residual ownership interest in the chattel paper, the chattel paper constitutes proceeds of the goods to which SP-1's security interest will attach and continue following the sale of the goods. Section 9-315(a) [30-9A-315(1)]. Even though Dealer has not retained any interest in the chattel paper, as discussed above BIOCOB subsequently may return the goods to Dealer under circumstances whereby Dealer reacquires an interest in the goods. The priority contest between SP-1 and SP-2 will be resolved as discussed above; Section 9-330 [30-9A-330] makes no distinction among purchasers of chattel paper on the basis of whether the purchaser is an outright buyer of chattel paper or one whose security interest secures an obligation of Dealer.

11. **Assignment of Lease Chattel Paper.** As defined in Section 9-102 [30-9A-102], "chattel paper" includes not only writings that evidence security interests in specific goods but also those that evidence true leases of goods.

The analysis with respect to lease chattel paper is similar to that set forth above with respect to non-lease chattel paper. It is complicated, however, by the fact that, unlike the case of chattel paper arising out of a sale, Dealer retains a residual interest in the goods. See Section 2A-103(1)(q) [30-2A-103(1)(q)] (defining "lessor's residual interest"); In re Leasing Consultants, Inc., 486 F.2d 367 (2d Cir. 1973) (lessor's residual interest under true lease is an interest in goods and is a separate type of collateral from lessor's interest in the lease). If Dealer leases goods to a "lessee in ordinary course of business" (LIOCOB), then LIOCOB takes its interest under the lease (i.e., its "leasehold interest") free of the security interest of SP-1. See Sections 2A-307(3), 2A-103(1)(m) [30-2A-307(3), 30-2A-103(1)(m)] (defining "leasehold interest"), (1)(o) [30-2A-103(1)(o)] (defining "lessee in ordinary course of business"). SP-1 would, however, retain its security interest in the residual interest. In addition, SP-1 would acquire an interest in the lease chattel paper as proceeds. If Dealer then assigns the lease chattel paper to SP-2, Section 9-330 [30-9A-330] gives SP-2 priority over SP-1 with respect to the chattel paper, but not with respect to the residual interest in the goods. Consequently, assignees of lease chattel paper typically take a security interest in and file against the lessor's residual interest in goods, expecting their priority in the goods to be governed by the first-to-file-or-perfect rule of Section 9-322 [30-9A-322].

If the goods are returned to Dealer, other than upon expiration of the lease term, then the security interests of both SP-1 and SP-2 normally would attach to the goods as proceeds of the chattel paper. (If the goods are returned to Dealer at the expiration of the lease term and the lessee has made all payments due under the lease, however, then Dealer no longer has any rights under the chattel paper. Dealer's interest in the goods consists solely of its residual interest, as to which SP-2 has no claim.) This would be the case, for example, when the lessee rescinds the lease or when the lessor recovers possession in the exercise of its remedies under Article 2A [Title 30, chapter 2A]. See, e.g., Section 2A-525 [30-2A-525]. If SP-2 enjoyed priority in the chattel paper under Section 9-330 [30-9A-330], then SP-2 likewise would enjoy priority in the returned goods as proceeds. This does not mean that SP-2 necessarily is entitled to the entire value of the returned goods. The value of the goods represents the sum of the present value of (i) the value of their use for the term of the lease and (ii) the value of the residual interest. SP-2 has priority in the former, but SP-1 ordinarily would have priority in the latter. Thus, an allocation of a portion of the value of the goods to each component may be necessary. Where, as here, one secured party has a security interest in the lessor's residual interest and another has a priority security interest in the chattel paper, it may be advisable for the conflicting secured parties to establish a method for making such an allocation and otherwise to determine their relative rights in returned goods by agreement.

30-9A-331. Priority of rights of purchasers of instruments, documents, and securities under other chapters — priority of interests in financial assets and security entitlements under chapter 8.

Official Comments

1. **Source.** Former Section 9-309 [30-9-309, now repealed].

2. **"Priority."** In some provisions, this Article [Title 30, chapter 9A] distinguishes between claimants that take collateral free of a security interest (in the sense that the security interest no longer encumbers the collateral) and those that take an interest in the collateral that is senior to a surviving security interest. See, e.g., Section 9-317 [30-9A-317]. Whether a holder or purchaser referred to in this section takes free or is senior to a security interest depends on whether the

purchaser is a buyer of the collateral or takes a security interest in it. The term "priority" is meant to encompass both scenarios, as it does in Section 9-330 [30-9A-330].

3. **Rights Acquired by Purchasers.** The rights to which this section refers are set forth in Sections 3-305 and 3-306 [30-3-505 and 30-3-306] (holder in due course), 7-502 [30-7-502] (holder to whom a negotiable document of title has been duly negotiated), and 8-303 [30-8-333] (protected purchaser). The holders and purchasers referred to in this section do not always take priority over a security interest. See, e.g., Section 7-503 [30-7-503] (affording paramount rights to certain owners and secured parties as against holder to whom a negotiable document of title has been duly negotiated). Accordingly, this section adds the clause, "to the extent provided in Articles 3, 7, and 8 [Title 30, chapters 3, 7, and 8]" to former Section 9-309 [30-9-309, now repealed].

4. **Financial Assets and Security Entitlements.** New subsection (b) [subsection (2)] provides explicit protection for those who deal with financial assets and security entitlements and who are immunized from liability under Article 8 [Title 30, chapter 8]. See, e.g., Sections 8-502, 8-503(e), 8-510, 8-511 [30-8-502, 30-8-503(5), 30-8-510, 30-8-511]. The new subsection makes explicit in Article 9 [Title 30, chapter 9A] what is implicit in former Article 9 [Title 30, chapter 9, now repealed] and explicit in several provisions of Article 8 [Title 30, chapter 8]. It does not change the law.

5. **Collections by Junior Secured Party.** Under this section, a secured party with a junior security interest in receivables (accounts, chattel paper, promissory notes, or payment intangibles) may collect and retain the proceeds of those receivables free of the claim of a senior secured party to the same receivables, if the junior secured party is a holder in due course of the proceeds. In order to qualify as a holder in due course, the junior must satisfy the requirements of Section 3-302 [30-3-302], which include taking in "good faith." This means that the junior not only must act "honestly" but also must observe "reasonable commercial standards of fair dealing" under the particular circumstances. See Section 9-102(a) [30-9A-102(1)]. Although "good faith" does not impose a general duty of inquiry, e.g., a search of the records in filing offices, there may be circumstances in which "reasonable commercial standards of fair dealing" would require such a search.

Consider, for example, a junior secured party in the business of financing or buying accounts who fails to undertake a search to determine the existence of prior security interests. Because a search, under the usages of trade of that business, would enable it to know or learn upon reasonable inquiry that collecting the accounts violated the rights of a senior secured party, the junior may fail to meet the good-faith standard. See Utility Contractors Financial Services, Inc. v. Amsouth Bank, NA, 985 F.2d 1554 (11th Cir. 1993). Likewise, a junior secured party who collects accounts when it knows or should know under the particular circumstances that doing so would violate the rights of a senior secured party, because the debtor had agreed not to grant a junior security interest in, or sell, the accounts, may not meet the good-faith test. Thus, if a junior secured party conducted or should have conducted a search and a financing statement filed on behalf of the senior secured party states such a restriction, the junior's collection would not meet the good-faith standard. On the other hand, if there was a course of performance between the senior secured party and the debtor which placed no such restrictions on the debtor and allowed the debtor to collect and use the proceeds without any restrictions, the junior secured party may then satisfy the requirements for being a holder in due course. This would be more likely in those circumstances where the junior secured party was providing additional financing to the debtor on an on-going basis by lending against or buying the accounts and had no notice of any restrictions against doing so. Generally, the senior secured party would not be prejudiced because the practical effect of such payment to the junior secured party is little different than if the debtor itself had made the collections and subsequently paid the secured party from the debtor's general funds. Absent collusion, the junior secured party would take the funds free of the senior security interests. See Section 9-332 [30-9A-332]. In contrast, the senior secured party is likely to be prejudiced if the debtor is going out of business and the junior secured party collects the accounts by notifying the account debtors to make payments directly to the junior. Those collections may not be consistent with "reasonable commercial standards of fair dealing."

Whether the junior secured party qualifies as a holder in due course is fact-sensitive and should be decided on a case-by-case basis in the light of those circumstances. Decisions such as Financial Management Services Inc. v. Familian, 905 P.2d 506 (Ariz. App. Div. 1995) (finding holder in due course status) could be determined differently under this application of the good-faith requirement.

The concepts addressed in this Comment are also applicable to junior secured parties as purchasers of instruments under Section 9-330(d) [30-9A-330(4)]. See Section 9-330 [30-9A-330], Comment 7.

Compiler's Comments

2001 Amendment: Chapter 179 near end of (2) substituted "a claim" for "an adverse claim". Amendment effective July 1, 2001.

30-9A-332. Transfer of money — transfer of funds from deposit account.

Official Comments

1. **Source.** New.

2. **Scope of This Section.** This section affords broad protection to transferees who take funds from a deposit account and to those who take money. The term "transferee" is not defined; however, the debtor itself is not a transferee. Thus this section does not cover the case in which a debtor withdraws money (currency) from its deposit account or the case in which a bank debits an encumbered account and credits another account it maintains for the debtor.

A transfer of funds from a deposit account, to which subsection (b) [subsection (2)] applies, normally will be made by check, by funds transfer, or by debiting the debtor's deposit account and crediting another depositor's account.

Example 1: Debtor maintains a deposit account with Bank A. The deposit account is subject to a perfected security interest in favor of Lender. Debtor draws a check on the account, payable to Payee. Inasmuch as the check is not the proceeds of the deposit account (it is an order to pay funds from the deposit account), Lender's security interest in the deposit account does not give rise to a security interest in the check. Payee deposits the check into its own deposit account, and Bank A pays it. Unless Payee acted in collusion with Debtor in violating Lender's rights, Payee takes the funds (the credits running in favor of Payee) free of Lender's security interest. This is true regardless of whether Payee is a holder in due course of the check and even if Payee gave no value for the check.

Example 2: Debtor maintains a deposit account with Bank A. The deposit account is subject to a perfected security interest in favor of Lender. At Bank B's suggestion, Debtor moves the funds from the account at Bank A to Debtor's deposit account with Bank B. Unless Bank B acted in collusion with Debtor in violating Lender's rights, Bank B takes the funds (the credits running in favor of Bank B) free from Lender's security interest. See subsection (b) [subsection (2)]. However, inasmuch as the deposit account maintained with Bank B constitutes the proceeds of the deposit account at Bank A, Lender's security interest would attach to that account as proceeds. See Section 9-315 [30-9A-315].

Subsection (b) [subsection (2)] also would apply if, in the example, Bank A debited Debtor's deposit account in exchange for the issuance of Bank A's cashier's check. Lender's security interest would attach to the cashier's check as proceeds of the deposit account, and the rules applicable to instruments would govern any competing claims to the cashier's check. See, e.g., Sections 3-306, 9-322, 9-330, 9-331 [30-3-306, 30-9A-322, 30-9A-330, and 30-9A-331].

If Debtor withdraws money (currency) from an encumbered deposit account and transfers the money to a third party, then subsection (a) [subsection (1)], to the extent not displaced by federal law relating to money, applies. It contains the same rule as subsection (b) [subsection (2)].

Subsection (b) [subsection (2)] applies to transfers of funds from a deposit account; it does not apply to transfers of the deposit account itself or of an interest therein. For example, this section does not apply to the creation of a security interest in a deposit account. Competing claims to the deposit account itself are dealt with by other Article 9 [Title 30, chapter 9A] priority rules. See Sections 9-317(a), 9-327, 9-340, 9-341 [30-9A-317(1), 30-9A-327, 30-9A-340, and 30-9A-341]. Similarly, a corporate merger normally would not result in a transfer of funds from a deposit account. Rather, it might result in a transfer of the deposit account itself. If so, the normal rules applicable to transferred collateral would apply; this section would not.

3. **Policy.** Broad protection for transferees helps to ensure that security interests in deposit accounts do not impair the free flow of funds. It also minimizes the likelihood that a secured party will enjoy a claim to whatever the transferee purchases with the funds. Rules concerning recovery of payments traditionally have placed a high value on finality. The opportunity to upset a completed transaction, or even to place a completed transaction in jeopardy by bringing suit against the transferee of funds, should be severely limited. Although the giving of value usually is a prerequisite for receiving the ability to take free from third-party claims, where payments are concerned the law is even more protective. Thus, Section 3-418(c) [see 30-3-425] provides that, even where the law of restitution otherwise would permit recovery of funds

paid by mistake, no recovery may be had from a person "who in good faith changed position in reliance on the payment." Rather than adopt this standard, this section eliminates all reliance requirements whatsoever. Payments made by mistake are relatively rare, but payments of funds from encumbered deposit accounts (e.g., deposit accounts containing collections from accounts receivable) occur with great regularity. In most cases, unlike payment by mistake, no one would object to these payments. In the vast proportion of cases, the transferee probably would be able to show a change of position in reliance on the payment. This section does not put the transferee to the burden of having to make this proof.

4. **"Bad Actors."** To deal with the question of the "bad actor," this section borrows "collusion" language from Article 8 [Title 30, chapter 8]. See, e.g., Sections 8-115, 8-503(e) [30-8-115, 30-8-503(5)]. This is the most protective (i.e., least stringent) of the various standards now found in the UCC. Compare, e.g., Section 1-201(b)(9) [30-1-201(2)(j)] ("without knowledge that the sale violates the rights of another person"); Section 1-201(b)(20) [30-1-201(2)(u)] ("honesty in fact and the observance of reasonable commercial standards of fair dealing"); Section 3-302(a)(2)(v) [30-3-302(1)(b)(v)] ("without notice of any claim").

5. **Transferee Who Does Not Take Free.** This section sets forth the circumstances under which certain transferees of money or funds take free of security interests. It does not determine the rights of a transferee who does not take free of a security interest.

Example 3: The facts are as in Example 2, but, in wrongfully moving the funds from the deposit account at Bank A to Debtor's deposit account with Bank B, Debtor acts in collusion with Bank B. Bank B does not take the funds free of Lender's security interest under this section. If Debtor grants a security interest to Bank B, Section 9-327 [30-9A-327] governs the relative priorities of Lender and Bank B. Under Section 9-327(3) [30-9A-327(3)], Bank B's security interest in the Bank B deposit account is senior to Lender's security interest in the deposit account as proceeds. However, Bank B's senior security interest does not protect Bank B against any liability to Lender that might arise from Bank B's wrongful conduct.

30-9A-333. Priority of certain liens arising by operation of law.

Official Comments

1. **Source.** Former Section 9-310 [30-9-310, now repealed].

2. **"Possessory Liens."** This section governs the relative priority of security interests arising under this Article [Title 30, chapter 9A] and "possessory liens," i.e., common-law and statutory liens whose effectiveness depends on the lienor's possession of goods with respect to which the lienor provided services or furnished materials in the ordinary course of its business. As under former Section 9-310 [30-9-310, now repealed], the possessory lien has priority over a security interest unless the possessory lien is created by a statute that expressly provides otherwise. If the statute creating the possessory lien is silent as to its priority relative to a security interest, this section provides a rule of interpretation that the possessory lien takes priority, even if the statute has been construed judicially to make the possessory lien subordinate.

30-9A-334. Priority of security interests in fixtures and crops.

Official Comments

1. **Source.** Former Section 9-313 [30-9-313, now repealed].

2. **Scope of This Section.** This section contains rules governing the priority of security interests in fixtures and crops as against persons who claim an interest in real property. Priority contests with other Article 9 [Title 30, chapter 9A] security interests are governed by the other priority rules of this Article [Title 30, chapter 9A]. The provisions with respect to fixtures follow those of former Section 9-313 [30-9-313, now repealed]. However, they have been rewritten to conform to Section 2A-309 [30-2A-309] and to prevailing style conventions. Subsections (i) and (j) [subsections (9) and (10)], which apply to crops, are new.

3. **Security Interests in Fixtures.** Certain goods that are the subject of personal-property (chattel) financing become so affixed or otherwise so related to real property that they become part of the real property. These goods are called "fixtures." See Section 9-102 [30-9A-102] (definition of "fixtures"). Some fixtures retain their personal-property nature: a security interest under this Article [Title 30, chapter 9A] may be created in fixtures and may continue in goods that become fixtures. See subsection (a) [subsection (1)]. However, if the goods are ordinary building materials incorporated into an improvement on land, no security interest in them exists. Rather, the priority of claims to the building materials are determined by the law governing claims to real property. (Of course, the fact that no security interest exists in ordinary building materials incorporated into an improvement on land does not prejudice any rights the secured party may

have against the debtor or any other person who violated the secured party's rights by wrongfully incorporating the goods into real property.)

Thus, this section recognizes three categories of goods: (1) those that retain their chattel character entirely and are not part of the real property; (2) ordinary building materials that have become an integral part of the real property and cannot retain their chattel character for purposes of finance; and (3) an intermediate class that has become real property for certain purposes, but as to which chattel financing may be preserved.

To achieve priority under certain provisions of this section, a security interest must be perfected by making a "fixture filing" (defined in Section 9-102 [30-9A-102]) in the real-property records. Because the question whether goods have become fixtures often is a difficult one under applicable real-property law, a secured party may make a fixture filing as a precaution. Courts should not infer from a fixture filing that the secured party concedes that the goods are or will become fixtures.

4. **Priority in Fixtures: General.** In considering priority problems under this section, one must first determine whether real-property claimants per se have an interest in the crops or fixtures as part of real property. If not, it is immaterial, so far as concerns real property parties as such, whether a security interest arising under this Article [Title 30, chapter 9A] is perfected or unperfected. In no event does a real-property claimant (e.g., owner or mortgagee) acquire an interest in a "pure" chattel just because a security interest therein is unperfected. If on the other hand real-property law gives real-property parties an interest in the goods, a conflict arises and this section states the priorities.

5. **Priority in Fixtures: Residual Rule.** Subsection (c) [subsection (3)] states the residual priority rule, which applies only if one of the other rules does not: A security interest in fixtures is subordinate to a conflicting interest of an encumbrancer or owner of the related real property other than the debtor.

6. **Priority in Fixtures: First to File or Record.** Subsection (e)(1) [subsection (5)(a)], which follows former Section 9-313(4)(b) [30-9-313(4)(b), now repealed], contains the usual priority rule of conveyancing, that is, the first to file or record prevails. In order to achieve priority under this rule, however, the security interest must be perfected by a "fixture filing" (defined in Section 9-102 [30-9A-102]), i.e., a filing for record in the real property records and indexed therein, so that it will be found in a real-property search.. The condition in subsection (e)(1)(B) [subsection (5)(a)(ii)], that the security interest must have had priority over any conflicting interest of a predecessor in title of the conflicting encumbrancer or owner, appears to limit to the first-in-time principle. However, this apparent limitation is nothing other than an expression of the usual rule that a person must be entitled to transfer what he has. Thus, if the fixture security interest is subordinate to a mortgage, it is subordinate to an interest of an assignee of the mortgage, even though the assignment is a later recorded instrument. Similarly if the fixture security interest is subordinate to the rights of an owner, it is subordinate to a subsequent grantee of the owner and likewise subordinate to a subsequent mortgagee of the owner.

7. **Priority in Fixtures: Purchase-Money Security Interests.** Subsection (d) [subsection (4)], which follows former Section 9-313(4)(a) [30-9-313(4)(a), now repealed], contains the principal exception to the first-to-file-or-record rule of subsection (e)(1) [subsection (5)(a)]. It affords priority to purchase-money security interests in fixtures as against prior recorded real-property interests, provided that the purchase-money security interest is filed as a fixture filing in the real-property records before the goods become fixtures or within 20 days thereafter. This priority corresponds to the purchase-money priority under Section 9-324(a) [30-9A-324(1)]. (Like other 10-day periods in former Article 9 [Title 30, chapter 9, now repealed], the 10-day period in this section has been changed to 20 days.)

It should be emphasized that this purchase-money priority with the 20-day grace period for filing is limited to rights against real-property interests that arise before the goods become fixtures. There is no such priority with the 20-day grace period as against real-property interests that arise subsequently. The fixture security interest can defeat subsequent real-property interests only if it is filed first and prevails under the usual conveyancing rule in subsection (e)(1) [subsection (5)(a)] or one of the other rules in this section.

8. **Priority in Fixtures: Readily Removable Goods.** Subsection (e)(2) [subsection (5)(b)], which derives from Section 2A-309 [30-2A-309] and former Section 9-313(4)(d) [30-9-313(4)(d), now repealed], contains another exception to the usual first-to-file-or-perfect rule. It affords priority to the holders of security interests in certain types of readily removable goods-factory and office machines, equipment that is not primarily used or leased for use in the operation of the real property, and (as discussed below) certain replacements of domestic appliances. This rule

is made necessary by the confusion in the law as to whether certain machinery, equipment, and appliances become fixtures. It protects a secured party who, perhaps in the mistaken belief that the readily removable goods will not become fixtures, makes a UCC filing (or otherwise perfects under this Article [Title 30, chapter 9A]) rather than making a fixture filing.

Frequently, under applicable law, goods of the type described in subsection (e)(2) [subsection (5)(b)] will not be considered to have become part of the real property. In those cases, the fixture security interest does not conflict with a real-property interest, and resort to this section is unnecessary. However, if the goods have become part of the real property, subsection (e)(2) [subsection (5)(b)] enables a fixture secured party to take priority over a conflicting real-property interest if the fixture security interest is perfected by a fixture filing or by any other method permitted by this Article [Title 30, chapter 9A]. If perfection is by fixture filing, the fixture security interest would have priority over subsequently recorded real-property interests under subsection (e)(1) [subsection (5)(a)] and, if the fixture security interest is a purchase-money security interest (a likely scenario), it would also have priority over most real property interests under the purchase-money priority of subsection (d) [subsection (4)]. Note, however, that unlike the purchase-money priority rule in subsection (d) [subsection (4)], the priority rules in subsection (e) [subsection (5)] override the priority given to a construction mortgage under subsection (h) [subsection (8)].

The rule in subsection (e)(2) [subsection (5)(b)] is limited to readily removable replacements of domestic appliances. It does not apply to original installations. Moreover, it is limited to appliances that are "consumer goods" (defined in Section 9-102 [30-9A-102]) in the hands of the debtor. The principal effect of the rule is to make clear that a secured party financing occasional replacements of domestic appliances in noncommercial, owner-occupied contexts need not concern itself with real-property descriptions or records; indeed, for a purchase-money replacement of consumer goods, perfection without any filing will be possible. See Section 9-309(1) [30-9A-309(1)].

9. **Priority in Fixtures: Judicial Liens.** Subsection (e)(3) [subsection (5)(c)], which follows former Section 9-313(4)(d) [30-9-313(4)(d), now repealed], adopts a first-in-time rule applicable to conflicts between a fixture security interest and a lien on the real property obtained by legal or equitable proceedings. Such a lien is subordinate to an earlier-perfected security interest, regardless of the method by which the security interest was perfected. Judgment creditors generally are not reliance creditors who search real-property records. Accordingly, a perfected fixture security interest takes priority over a subsequent judgment lien or other lien obtained by legal or equitable proceedings, even if no evidence of the security interest appears in the relevant real-property records. Subsection (e)(3) [subsection (5)(c)] thus protects a perfected fixture security interest from avoidance by a trustee in bankruptcy under Bankruptcy Code Section 544(a), regardless of the method of perfection.

10. **Priority in Fixtures: Manufactured Homes.** A manufactured home may become a fixture. New subsection (e)(4) [subsection (5)(d)] contains a special rule granting priority to certain security interests created in a "manufactured home" as part of a "manufactured-home transaction" (both defined in Section 9-102 [30-9A-102]). Under this rule, a security interest in a manufactured home that becomes a fixture has priority over a conflicting interest of an encumbrancer or owner of the real property if the security interest is perfected under a certificate-of-title statute (see Section 9-311 [30-9A-311]). Subsection (e)(4) [subsection (5)(d)] is only one of the priority rules applicable to security interests in a manufactured home that becomes a fixture. Thus, a security interest in a manufactured home which does not qualify for priority under this subsection may qualify under another.

11. **Priority in Fixtures: Construction Mortgages.** The purchase-money priority presents a difficult problem in relation to construction mortgages. The latter ordinarily will have been recorded even before the commencement of delivery of materials to the job, and therefore would take priority over fixture security interests were it not for the purchase-money priority. However, having recorded first, the holder of a construction mortgage reasonably expects to have first priority in the improvement built using the mortgagee's advances. Subsection (g) [subsection (7)] expressly gives priority to the construction mortgage recorded before the filing of the purchase-money security interest in fixtures. A refinancing of a construction mortgage has the same priority as the construction mortgage itself. The phrase "an obligation incurred for the construction of an improvement" covers both optional advances and advances pursuant to commitment. Both types of advances have the same priority under subsection (g) [subsection (7)].

The priority under this subsection applies only to goods that become fixtures during the construction period leading to the completion of the improvement. The construction priority will not apply to additions to the building made long after completion of the improvement, even if the additions are financed by the real-property mortgagee under an open-end clause of the construction mortgage. In such case, subsections (d), (e), and (f) [subsections (4), (5), and (6)] govern.

Although this subsection affords a construction mortgage priority over a purchase-money security interest that otherwise would have priority under subsection (d) [subsection (4)], the subsection is subject to the priority rules in subsections (e) and (f) [subsections (5) and (6)]. Thus, a construction mortgage may be junior to a fixture security interest perfected by a fixture filing before the construction mortgage was recorded. See subsection (e)(1) [subsection (5)(a)].

12. **Crops.** Growing crops are "goods" in which a security interest may be created and perfected under this Article [Title 30, chapter 9A]. In some jurisdictions, a mortgage of real property may cover crops, as well. In the event that crops are encumbered by both a mortgage and an Article 9 [Title 30, chapter 9A] security interest, subsection (i) [subsection (9)] provides that the security interest has priority. States whose real-property law provides otherwise should either amend that law directly or override it by enacting subsection (j) [subsection (10)].

30-9A-335. Accessions.

Official Comments

1. **Source.** Former Section 9-314 [30-9-314, now repealed].

2. **"Accession."** This section applies to an "accession," as defined in Section 9-102 [30-9A-102], regardless of the cost or difficulty of removing the accession from the other goods, and regardless of whether the original goods have come to form an integral part of the other goods. This section does not apply to goods whose identity has been lost. Goods of that kind are "commingled goods" governed by Section 9-336 [30-9A-336]. Neither this section nor the following one addresses the case of collateral that changes form without the addition of other goods.

3. **"Accession" vs. "Other Goods."** This section distinguishes among the "accession," the "other goods," and the "whole." The last term refers to the combination of the "accession" and the "other goods." If one person's collateral becomes physically united with another person's collateral, each is an "accession."

Example 1: SP-1 holds a security interest in the debtor's tractors (which are not subject to a certificate-of-title statute), and SP-2 holds a security interest in a particular tractor engine. The engine is installed in a tractor. From the perspective of SP-1, the tractor becomes an "accession" and the engine is the "other goods." From the perspective of SP-2, the engine is the "accession" and the tractor is the "other goods." The completed tractor-tractor cum engine-constitutes the "whole."

4. **Scope.** This section governs only a few issues concerning accessions. Subsection (a) [subsection (1)] contains rules governing continuation of a security interest in an accession. Subsection (b) [subsection (2)] contains a rule governing continued perfection of a security interest in goods that become an accession. Subsection (d) [subsection (4)] contains a special priority rule governing accessions that become part of a whole covered by a certificate of title. Subsections (e) and (f) [subsections (5) and (6)] govern enforcement of a security interest in an accession.

5. **Matters Left to Other Provisions of this Article [Title 30, chapter 9A]: Attachment and Perfection.** Other provisions of this Article [Title 30, chapter 9A] often govern accession-related issues. For example, this section does not address whether a secured party acquires a security interest in the whole if its collateral becomes an accession. Normally this will turn on the description of the collateral in the security agreement.

Example 2: Debtor owns a computer subject to a perfected security interest in favor of SP-1. Debtor acquires memory and installs it in the computer. Whether SP-1's security interest attaches to the memory depends on whether the security agreement covers it.

Similarly, this section does not determine whether perfection against collateral that becomes an accession is effective to perfect a security interest in the whole. Other provisions of this Article [Title 30, chapter 9A], including the requirements for indicating the collateral covered by a financing statement, resolve that question.

6. **Matters Left to Other Provisions of this Article [Title 30, chapter 9A]: Priority.** With one exception, concerning goods covered by a certificate of title (see subsection (d) [subsection (4)]), the other provisions of this Part, including the rules governing purchase-money security interests, determine the priority of most security interests in an accession, including the relative priority of a security interest in an accession and a security interest in the whole. See subsection (c) [subsection (3)].

Example 3: Debtor owns an office computer subject to a security interest in favor of SP-1. Debtor acquires memory and grants a perfected security interest in the memory to SP-2. Debtor installs the memory in the computer, at which time (one assumes) SP-1's security interest attaches to the memory. The first-to-file-or-perfect rule of Section 9-322 [30-9A-322] governs priority in the memory. If, however, SP-2's security interest is a purchase-money security interest, Section 9-324(a) [30-9A-324(1)] would afford priority in the memory to SP-2, regardless of which security interest was perfected first.

7. **Goods Covered by Certificate of Title.** This section does govern the priority of a security interest in an accession that is or becomes part of a whole that is subject to a security interest perfected by compliance with a certificate-of-title statute. Subsection (d) [subsection (4)] provides that a security interest in the whole, perfected by compliance with a certificate-of-title statute, takes priority over a security interest in the accession. It enables a secured party to rely upon a certificate of title without having to check the UCC files to determine whether any components of the collateral may be encumbered. The subsection imposes a corresponding risk upon those who finance goods that may become part of goods covered by a certificate of title. In doing so, it reverses the priority that appeared reasonable to most pre-UCC courts.

Example 4: Debtor owns an automobile subject to a security interest in favor of SP-1. The security interest is perfected by notation on the certificate of title. Debtor buys tires subject to a perfected-by-filing purchase-money security interest in favor of SP-2 and mounts the tires on the automobile's wheels. If the security interest in the automobile attaches to the tires, then SP-1 acquires priority over SP-2. The same result would obtain if SP-1's security interest attached to the automobile and was perfected after the tires had been mounted on the wheels.

Case Notes

CASES DECIDED PRIOR TO 1999 REVISION

Tires Not Accessions: Paccar leased trucks to MPT. MPT entered into an agreement to buy tires from Les Schwab on credit. When MPT defaulted on its purchase agreement, Paccar argued that it had a superior interest to Les Schwab in the tires on the basis that the tires were accessions. The Supreme Court, after examining decisions of other jurisdictions, determined that the tires were not accessions because they could easily be removed from the trucks with no damage to the trucks. Paccar Financial Corp. v. Les Schwab Tire Centers of Mont., Inc., 277 M 171, 920 P2d 977, 53 St. Rep. 652 (1996).

30-9A-336. Commingled goods.

Official Comments

1. **Source.** Former Section 9-315 [30-9-315, now repealed].

2. **"Commingled Goods."** Subsection (a) [subsection (1)] defines "commingled goods." It is meant to include not only goods whose identity is lost through manufacturing or production (e.g., flour that has become part of baked goods) but also goods whose identity is lost by commingling with other goods from which they cannot be distinguished (e.g., ball bearings).

3. **Consequences of Becoming "Commingled Goods."** By definition, the identity of the original collateral cannot be determined once the original collateral becomes commingled goods. Consequently, the security interest in the specific original collateral alone is lost once the collateral becomes commingled goods, and no security interest in the original collateral can be created thereafter except as a part of the resulting product or mass. See subsection (b) [subsection (2)].

Once collateral becomes commingled goods, the secured party's security interest is transferred from the original collateral to the product or mass. See subsection (c) [subsection (3)]. If the security interest in the original collateral was perfected, the security interest in the product or mass is a perfected security interest. See subsection (d) [subsection (4)]. This perfection continues until lapse.

4. **Priority of Perfected Security Interests That Attach Under This Section.** This section governs the priority of competing security interests in a product or mass only when both security interests arise under this section. In that case, if both security interests are perfected by operation of this section (see subsections (c) and (d) [subsections (3) and (4)]), then the security interests rank equally, in proportion to the value of the collateral at the time it became commingled goods. See subsection (f)(2) [subsection (6)(b)].

Example 1: SP-1 has a perfected security interest in Debtor's eggs, which have a value of $300 and secure a debt of $400, and SP-2 has a perfected security interest in Debtor's flour, which has a value of $500 and secures a debt of $600. Debtor uses the flour and eggs to make cakes, which have a value of $1000. The two security interests rank equally and share in the ratio of

3:5. Applying this ratio to the entire value of the product, SP-1 would be entitled to $375 (i.e., 3/8 x $1000), and SP-2 would be entitled to $625 (i.e., 5/8 x $1000).

Example 2: Assume the facts of Example 1, except that SP-1's collateral, worth $300, secures a debt of $200. Recall that, if the cake is worth $1000, then applying the ratio of 3:5 would entitle SP-1 to $375 and SP-2 to $625. However, SP-1 is not entitled to collect from the product more than it is owed. Accordingly, SP-1's share would be only $200, SP-2 would receive the remaining value, up to the amount it is owed ($600).

Example 3: Assume that the cakes in the previous examples have a value of only $600. Again, the parties share in the ratio of 3:5. If, as in Example 1, SP-1 is owed $400, then SP-1 is entitled to $225 (i.e., 3/8 x $600), and SP-2 is entitled to $375 (i.e., 5/8 x $600). Debtor receives nothing. If, however, as in Example 2, SP-1 is owed only $200, then SP-2 receives $400.

The results in the foregoing examples remain the same, regardless of whether SP-1 or SP-2 (or each) has a purchase-money security interest.

5. **Perfection: Unperfected Security Interests.** The rule explained in the preceding Comment applies only when both security interests in original collateral are perfected when the goods become commingled goods. If a security interest in original collateral is unperfected at the time the collateral becomes commingled goods, subsection (f)(1) [subsection (6)(a)] applies.

Example 4: SP-1 has a perfected security interest in the debtor's eggs, and SP-2 has an unperfected security interest in the debtor's flour. Debtor uses the flour and eggs to make cakes. Under subsection (c) [subsection (3)], both security interests attach to the cakes. But since SP-1's security interest was perfected at the time of commingling and SP-2's was not, only SP-1's security interest in the cakes is perfected. See subsection (d) [subsection (4)]. Under subsection (f)(1) and Section 9-322(a)(2) [subsection (6)(a) and 30-9A-322(1)(b)], SP-1's perfected security interest has priority over SP-2's unperfected security interest. If both security interests are unperfected, the rule of Section 9-322(a)(3) [30-9A-322(1)(c)] would apply.

6. **Multiple Security Interests.** On occasion, a single input may be encumbered by more than one security interest. In those cases, the multiple secured parties should be treated like a single secured party for purposes of determining their collective share under subsection (f)(2) [subsection (6)(b)]. The normal priority rules would determine how that share would be allocated between them. Consider the following example, which is a variation on Example 1 above:

Example 5: SP-1A has a perfected, first-priority security interest in Debtor's eggs. SP-1B has a perfected, second-priority security interest in the same collateral. The eggs have a value of $300. Debtor owes $200 to SP-1A and $200 to SP-1B. SP-2 has a perfected security interest in Debtor's flour, which has a value of $500 and secures a debt of $600. Debtor uses the flour and eggs to make cakes, which have a value of $1000.

For purposes of subsection (f)(2) [subsection (6)(b)], SP-1A and SP-1B should be treated like a single secured party. The collective security interest would rank equally with that of SP-2. Thus, the secured parties would share in the ratio of 3 (for SP-1A and SP-1B combined) to 5 (for SP-2). Applying this ratio to the entire value of the product, SP-1A and SP-1B in the aggregate would be entitled to $375 (i.e., 3/8 x $1000), and SP-2 would be entitled to $625 (i.e., 5/8 x $1000).

SP-1A and SP-1B would share the $300 in accordance with their priority, as established under other rules. Inasmuch as SP-1A has first priority, it would receive $200, and SP-1B would receive $100.

7. **Priority of Security Interests That Attach Other Than by Operation of This Section.** Under subsection (e) [subsection (5)], the normal priority rules determine the priority of a security interest that attaches to the product or mass other than by operation of this section. For example, assume that SP-1 has a perfected security interest in Debtor's existing and after-acquired baked goods, and SP-2 has a perfected security interest in Debtor's flour. When the flour is processed into cakes, subsections (c) and (d) [subsections (3) and (4)] provide that SP-2 acquires a perfected security interest in the cakes. If SP-1 filed against the baked goods before SP-2 filed against the flour, then SP-1 will enjoy priority in the cakes. See Section 9-322 [30-9A-322] (first-to-file-or-perfect). But if SP-2 filed against the flour before SP-1 filed against the baked goods, then SP-2 will enjoy priority in the cakes to the extent of its security interest.

Compiler's Comments

2001 Amendment: Chapter 179 in (6)(b) after "proportion to" inserted "the". Amendment effective July 1, 2001.

30-9A-337. Priority of security interests in goods covered by certificate of title.

Official Comments

1. **Source.** Derived from former Section 9-103(2)(d) [30-9-103(2)(d), now repealed].

2. **Protection for Buyers and Secured Parties.** This section affords protection to certain good-faith purchasers for value who are likely to have relied on a "clean" certificate of title, i.e., one that neither shows that the goods are subject to a particular security interest nor contains a statement that they may be subject to security interests not shown on the certificate. Under this section, a buyer can take free of, and the holder of a conflicting security interest can acquire priority over, a security interest that is perfected by any method under the law of another jurisdiction. The fact that the security interest has been reperfected by possession under Section 9-313 [30-9A-313] does not of itself disqualify the holder of a conflicting security interest from protection under paragraph (2) [subsection (2)].

30-9A-338. Priority of security interest or agricultural lien perfected by filed financing statement providing certain incorrect information.

Official Comments

1. **Source.** New.

2. **Effect of Incorrect Information in Financing Statement.** Section 9-520(a) [30-9A-520(1)] requires the filing office to reject financing statements that do not contain information concerning the debtor as specified in Section 9-516(b)(5) [30-9A-516(2)(e)]. An error in this information does not render the financing statement ineffective. On rare occasions, a subsequent purchaser of the collateral (i.e., a buyer or secured party) may rely on the misinformation to its detriment. This section subordinates a security interest or agricultural lien perfected by an effective, but flawed, financing statement to the rights of a buyer or holder of a perfected security interest to the extent that, in reasonable reliance on the incorrect information, the purchaser gives value and, in the case of tangible collateral, receives delivery of the collateral. A purchaser who has not made itself aware of the information in the filing office with respect to the debtor cannot act in "reasonable reliance" upon incorrect information.

3. **Relationship to Section 9-507 [30-9A-507].** This section applies to financing statements that contain information that is incorrect at the time of filing and imposes a small risk of subordination on the filer. In contrast, Section 9-507 [30-9A-507] deals with financing statements containing information that is correct at the time of filing but which becomes incorrect later. Except as provided in Section 9-507 [30-9A-507] with respect to changes in the name that is sufficient as the name of the debtor under Section 9-503(a) [30-9A-503(1)], an otherwise effective financing statement does not become ineffective if the information contained in it becomes inaccurate.

Compiler's Comments

2005 Amendment: Chapter 575 in (2) in two places inserted "tangible". Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-9A-339. Priority subject to subordination.

Official Comments

1. **Source.** Former Section 9-316 [30-9-316, now repealed].

2. **Subordination by Agreement.** The preceding sections deal elaborately with questions of priority. This section makes it entirely clear that a person entitled to priority may effectively agree to subordinate its claim. Only the person entitled to priority may make such an agreement: a person's rights cannot be adversely affected by an agreement to which the person is not a party.

30-9A-340. Effectiveness of right of recoupment or setoff against deposit account.

Official Comments

1. **Source.** New; subsection (b) [subsection (2)] is based on a nonuniform Illinois amendment.

2. **Set-off vs. Security Interest.** This section resolves the conflict between a security interest in a deposit account and the bank's rights of recoupment and set-off.

Subsection (a) [subsection (1)] states the general rule and provides that the bank may effectively exercise rights of recoupment and set-off against the secured party. Subsection (c) [subsection (3)] contains an exception: if the secured party has control under Section 9-104(a)(3) [30-9A-104(1)(c)] (i.e., if it has become the bank's customer), then any set-off exercised by the bank against a debt owed by the debtor (as opposed to a debt owed to the bank by the secured party) is ineffective. The bank may, however, exercise its recoupment rights effectively. This result is consistent with the priority rule in Section 9-327(4) [30-9A-327(4)], under which the security interest of a bank in a deposit account is subordinate to that of a secured party who has control under Section 9-104(a)(3) [30-9A-104(1)(c)].

This section deals with rights of set-off and recoupment that a bank may have under other law. It does not create a right of set-off or recoupment, nor is it intended to override any limitations or restrictions that other law imposes on the exercise of those rights.

3. **Preservation of Set-Off Right.** Subsection (b) [subsection (2)] makes clear that a bank may hold both a right of set-off against, and an Article 9 [Title 30, chapter 9A] security interest in, the same deposit account. By holding a security interest in a deposit account, a bank does not impair any right of set-off it would otherwise enjoy. This subsection does not pertain to accounts evidenced by an instrument (e.g., certain certificates of deposit), which are excluded from the definition of "deposit accounts."

30-9A-341. Bank's rights and duties with respect to deposit account.

Official Comments

1. **Source.** New.
2. **Free Flow of Funds.** This section is designed to prevent security interests in deposit accounts from impeding the free flow of funds through the payment system. Subject to two exceptions, it leaves the bank's rights and duties with respect to the deposit account and the funds on deposit unaffected by the creation or perfection of a security interest or by the bank's knowledge of the security interest. In addition, the section permits the bank to ignore the instructions of the secured party unless it had agreed to honor them or unless other law provides to the contrary. A secured party who wishes to deprive the debtor of access to funds on deposit or to appropriate those funds for itself needs to obtain the agreement of the bank, utilize the judicial process, or comply with procedures set forth in other law. Section 4-303(a) [30-4-303(1)], concerning the effect of notice on a bank's right and duty to pay items, is not to the contrary. That section addresses only whether an otherwise effective notice comes too late; it does not determine whether a timely notice is otherwise effective.
3. **Operation of Rule.** The general rule of this section is subject to Section 9-340(c) [30-9A-340(3)], under which a bank's right of set-off may not be exercised against a deposit account in the secured party's name if the right is based on a claim against the debtor. This result reflects current law in many jurisdictions and does not appear to have unduly disrupted banking practices or the payments system. The more important function of this section, which is not impaired by Section 9-340 [30-9A-340], is the bank's right to follow the debtor's (customer's) instructions (e.g., by honoring checks, permitting withdrawals, etc.) until such time as the depository institution is served with judicial process or receives instructions with respect to the funds on deposit from a secured party who has control over the deposit account.
4. **Liability of Bank.** This Article [Title 30, chapter 9A] does not determine whether a bank that pays out funds from an encumbered deposit is liable to the holder of a security interest. Although the fact that a secured party has control over the deposit account and the manner by which control was achieved may be relevant to the imposition of liability, whatever rule applies generally when a bank pays out funds in which a third party has an interest would determine liability to a secured party. Often, this rule is found in a non-UCC adverse claim statute.
5. **Certificates of Deposit.** This section does not address the obligations of banks that issue instruments evidencing deposits (e.g., certain certificates of deposit).

30-9A-342. Bank's right to refuse to enter into or disclose existence of control agreement.

Official Comments

1. **Source.** New; derived from Section 8-106(g) [30-8-116].
2. **Protection for Bank.** This section protects banks from the need to enter into agreements against their will and from the need to respond to inquiries from persons other than their customers.

Part 4
Rights of Third Parties

Part Compiler's Comments

Saving Clause: Section 169, Ch. 305, L. 1999, provided: "(1) Except as otherwise provided in [sections 164 through 169] [sections 162 through 167—30-9A-703 through 30-9A-706, 30-9A-708, 30-9A-709], [this act] applies to a transaction or lien within its scope, even if the transaction or lien was entered into or created before [this act] takes effect.

(2) Except as otherwise provided in subsection (3) and [sections 164 through 169] [sections 162 through 167—30-9A-703 through 30-9A-706, 30-9A-708, 30-9A-709]:

(a) transactions and liens that were not governed by [former chapter 9, now repealed] were validly entered into or created before [this act] takes effect and would be subject to [this act] if they had been entered into or created after [this act] takes effect, and the rights, duties, and interests flowing from those transactions and liens remain valid after [this act] takes effect; and

(b) the transactions and liens may be terminated, completed, consummated, or enforced as required or permitted by [this act] or by the law that otherwise would apply if [this act] did not take effect.

(3) [This act] does not affect an action, case, or proceeding commenced before [this act] takes effect."

Part Case Notes

CASES DECIDED PRIOR TO 1999 REVISION

Good Faith Filing — Effective Against Persons With Knowledge: In a case decided before the 1985 amendments to 30-9-401 (now repealed, see 30-9A-501), a bank that filed its security agreement in livestock in the wrong county did not have a perfected security interest in the livestock but did take precedence over another secured party because the filing was made in good faith and the other secured party had actual knowledge of the security interest. First Nat'l Bank of Glasgow v. First Sec. Bank of Mont., 222 M 118, 721 P2d 1270, 43 St. Rep. 1105 (1986).

Business Equipment for Lease: A trencher held by a leasing business falls into none of the categories for which filing is not required. Since it is business equipment for lease, the perfection of a security interest in the trencher required filing with the Secretary of State. Between two rival security interests, one filed with the Secretary of State on June 19, 1978, and one filed initially with a County Clerk and Recorder on December 13, 1979, and subsequently filed with the Secretary of State on March 13, 1981, the former prevailed. Taylor Rental Corp. v. First Citizens Bank, 539 F. Supp. 228, 39 St. Rep. 985 (D.C. Mont. 1982).

Knowledge of Financing Statement — Unidentified Bank Loan: A national leasing company perfected a security interest in after-acquired inventory of its franchisee. Subsequently, a bank incorrectly filed a security interest on the franchisee's trencher that it had financed. The leasing company's knowledge of an unidentified bank loan did not imply it had knowledge of the bank's security interest. Even if it did, the leasing company's security interest would still be prior to the bank's security interest. Taylor Rental Corp. v. First Citizens Bank, 539 F. Supp. 228, 39 St. Rep. 985 (D.C. Mont. 1982).

Knowledge of Financing Statement — Confidential Computer Journal Records: A national leasing company provided a computerized accounting service to its franchisees. The information provided to the accounting service was confidential and unavailable to the leasing company without consent of the franchisee. A journal entry of an unidentified bank loan was not evidence of the leasing company's knowledge of a bank's security agreement. Taylor Rental Corp. v. First Citizens Bank, 539 F. Supp. 228, 39 St. Rep. 985 (D.C. Mont. 1982).

Security Interest on Livestock: Security interest listing "all livestock" was perfected upon filing of financing statement with County Clerk (prior to 1985 amendment). Failure to adequately describe cattle in notice of security agreement to Livestock Commission would bar superior lien only in action against livestock market for conversion. Batey Land & Livestock Co. v. Nixon, 172 M 99, 560 P2d 1334 (1977).

Forestry and Logging: Forestry and logging are not farming for the purposes of 30-9-401 (now repealed, see 30-9A-501); filing with the Secretary of State is necessary to perfect a security interest on equipment used for that purpose. Belgrade St. Bank v. Elder, 157 M 1, 482 P2d 135 (1971).

30-9A-401. Alienability of debtor's rights.

Official Comments

1. **Source.** Former Section 9-311 [30-9-311, now repealed].

2. **Scope of This Part.** This Part [Title 30, chapter 9A, part 4] deals with several issues affecting third parties (i.e., parties other than the debtor and the secured party). These issues are not addressed in Part 3, Subpart 3 [30-9A-317 through 30-9A-339], which deals with priorities. This Part [Title 30, chapter 9A, part 4] primarily addresses the rights and duties of account debtors and other persons obligated on collateral who are not, themselves, parties to a secured transaction.

3. **Governing Law.** There was some uncertainty under former Article 9 [Title 30, chapter 9, now repealed] as to which jurisdiction's law (usually, which jurisdiction's version of Article 9 [Title 30, chapter 9A]) applied to the matters that this Part [Title 30, chapter 9A, part 4] addresses. Part 3, Subpart 1 [30-9A-301 through 30-9A-307], does not determine the law governing these matters because they do not relate to perfection, the effect of perfection or nonperfection, or priority. However, it might be inappropriate for a designation of applicable law by a debtor and secured party under Section 1-301 [30-1-105, now repealed, but see 30-1-301] to control the law applicable to an independent transaction or relationship between the debtor and an account debtor.

Consider an example under Section 9-408 [30-9A-408].

Example 1: State X has adopted this Article [Title 30, chapter 9A]; former Article 9 [Title 30, chapter 9, now repealed] is the law of State Y. A general intangible (e.g., a franchise agreement) between a debtor-franchisee, D, and an account debtor-franchisor, AD, is governed by the law of State Y. D grants to SP a security interest in its rights under the franchise agreement. The franchise agreement contains a term prohibiting D's assignment of its rights under the agreement. D and SP agree that their secured transaction is governed by the law of State X. Under State X's Section 9-408 [30-9A-408], the restriction on D's assignment is ineffective to prevent the creation, attachment, or perfection of SP's security interest. State Y's former Section 9-318(4) [30-9-318(4), now repealed, see 30-9A-404 through 30-9A-406], however, does not address restrictions on the creation of security interests in general intangibles other than general intangibles for money due or to become due. Accordingly, it does not address restrictions on the assignment to SP of D's rights under the franchise agreement. The non-Article-9 [non-Title 30, chapter 9, now repealed] law of State Y, which does address restrictions, provides that the prohibition on assignment is effective.

This Article [Title 30, chapter 9A] does not provide a specific answer to the question of which State's law applies to the restriction on assignment in the example. However, assuming that under non-UCC choice-of-law principles the effectiveness of the restriction would be governed by the law of State Y, which governs the franchise agreement, the fact that State X's Article 9 [Title 30, chapter 9A] governs the secured transaction between SP and D would not override the otherwise applicable law governing the agreement. Of course, to the extent that jurisdictions eventually adopt identical versions of this Article [Title 30, chapter 9A] and courts interpret it consistently, the inability to identify the applicable law in circumstances such as those in the example may be inconsequential.

4. **Inalienability Under Other Law.** Subsection (a) [subsection (1)] addresses the question whether property necessarily is transferable by virtue of its inclusion (i.e., its eligibility as collateral) within the scope of Article 9 [Title 30, chapter 9A]. It gives a negative answer, subject to the identified exceptions. The substance of subsection (a) [subsection (1)] was implicit under former Article 9 [Title 30, chapter 9, now repealed].

5. **Negative Pledge Covenant.** Subsection (b) [subsection (2)] is an exception to the general rule in subsection (a) [subsection (1)]. It makes clear that in secured transactions under this Article [Title 30, chapter 9A] the debtor has rights in collateral (whether legal title or equitable) which it can transfer and which its creditors can reach. It is best explained with an example.

Example 2: A debtor, D, grants to SP a security interest to secure a debt in excess of the value of the collateral. D agrees with SP that it will not create a subsequent security interest in the collateral and that any security interest purportedly granted in violation of the agreement will be void. Subsequently, in violation of its agreement with SP, D purports to grant a security interest in the same collateral to another secured party. Subsection (b) [subsection (2)] validates D's creation of the subsequent (prohibited) security interest, which might even achieve priority over the earlier security interest. See Comment 7. However, unlike some other provisions of this Part, such as Section 9-406 [30-9A-406], subsection (b) [subsection (2)] does not provide that the agreement restricting assignment itself is "ineffective." Consequently, the debtor's breach may create a default.

6. **Rights of Lien Creditors.** Difficult problems may arise with respect to attachment, levy, and other judicial procedures under which a debtor's creditors may reach collateral subject

to a security interest. For example, an obligation may be secured by collateral worth many times the amount of the obligation. If a lien creditor has caused all or a portion of the collateral to be seized under judicial process, it may be difficult to determine the amount of the debtor's "equity" in the collateral that has been seized. The section leaves resolution of this problem to the courts. The doctrine of marshaling may be appropriate.

7. **Sale of Receivables.** If a debtor sells an account, chattel paper, payment intangible, or promissory note outright, as against the buyer the debtor has no remaining rights to transfer. If, however, the buyer fails to perfect its interest, then solely insofar as the rights of certain third parties are concerned, the debtor is deemed to retain its rights and title. See Section 9-318 [30-9A-318]. The debtor has the power to convey these rights to a subsequent purchaser. If the subsequent purchaser (buyer or secured lender) perfects its interest, it will achieve priority over the earlier, unperfected purchaser. See Section 9-322(a)(1) [30-9A-322(1)(a)].

Case Notes

CASES DECIDED PRIOR TO 1999 REVISION

Transfer of Collateral — Security Interest Follows: The plaintiff's father had the right to transfer to plaintiff his interest in property securing loans by the defendant's bank to the father where the security instrument was perfected and the father was not in default; but the creditor, without knowledge of the transfer and under an agreement containing a "dragnet clause", not having received the proceeds, could consider such a transfer a default. The security interest followed the collateral though the transfer occurred under 30-9-311 (now repealed, see this section). Sturdevant v. First Security Bank, 186 M 91, 606 P2d 525 (1980).

30-9A-402. Secured party not obligated on contract of debtor.

Official Comments

1. **Source.** Former Section 9-317 [30-9-317, now repealed].

2. **Nonliability of Secured Party.** This section, like former Section 9-317 [30-9-317, now repealed], rejects theories on which a secured party might be held liable on a debtor's contracts or in tort merely because a security interest exists or because the debtor is entitled to dispose of or use collateral. This section expands former Section 9-317 [30-9-317, now repealed] to cover agricultural liens.

Case Notes

CASES DECIDED PRIOR TO 1999 REVISION

Oral Notice Sufficient: Plaintiff entered numerous financing arrangements with Tri-Mont. Plaintiff had blanket security interests in Tri-Mont's after-acquired assets. Defendant also financed acquisitions of inventory for Tri-Mont. Defendant filed a purchase money security interest in certain property. Although there was no formal agreement between the parties, they routinely contacted one another prior to financing an item. Upon Tri-Mont's filing a bankruptcy petition, a dispute arose as to whether the defendant's security interest had been properly noticed to plaintiff, thereby giving priority to defendant's interest. Under 30-9-312 (now repealed, see 30-9A-322 through 30-9A-324), prior to perfecting a purchase money security interest, notice must be given to known secured parties. Plaintiff contended this notice had to be in writing. It was held that under the definitions of "notice" and "notifies" in 30-1-201, notice may be given orally, as was the case here. The defendant's oral notification to plaintiff was sufficient to put plaintiff on notice of its intent to perfect a purchase money security interest. Credit Alliance Corp. v. First Nat'l Bank of Missoula, 40 St. Rep. 2095 (Bankr. 9th Cir. 1983) (apparently not reported in Federal Supplement). See also First Bank of Billings v. Feterl Mfg. Co., 47 Bankr. 419, 42 St. Rep. 382 (Bankr. 9th Cir. 1985).

Security Interest in Inventory — Subsidiary Corporation Transfers to Parent Corporation: A subsidiary corporation owed money to plaintiff under a contract by which plaintiff sold his business and took a security interest in the subsidiary's inventory to cover the balance due on the purchase price. The subsidiary's parent corporation later guaranteed a bank's loan to the subsidiary. The subsidiary defaulted on the loan, the parent paid it upon request of the bank, and the parent took over from the bank a security interest in the subsidiary's inventory, which the bank was given upon granting the loan. This security interest, both in the hands of the bank and in the hands of the parent, was secondary to plaintiff's security interest, which plaintiff had perfected. The subsidiary corporation then sold its entire inventory and placed the proceeds of the sale in the parent corporation's account. The argument that the parent corporation was not liable to plaintiff for the remainder of the purchase price of plaintiff's business because plaintiff knew of and did not object to the sale of the inventory by the subsidiary and thus waived his security interest could not stand. The parent corporation was simply a secured creditor of the subsidiary with a security interest inferior to plaintiff's. Whether or not plaintiff waived his security interest in the subsidiary's inventory has no bearing on plaintiff's right to the proceeds of the sale by the subsidiary of the subsidiary's inventory, as against competing creditors such as the parent corporation. The plaintiff had priority, to the extent of his security interest, in the proceeds of the sale of the inventory whether or not he consented to the sale. Any consent by plaintiff to the sale affected only his rights as against the purchaser of the inventory, barring him from obtaining possession from the purchaser. As against the parent corporation, the plaintiff's security interest took precedence over the parent corporation's security interest. The same person owned the parent and the subsidiary, and the parent had in fact liquidated the subsidiary and deposited the proceeds in the parent's account. This was very close to a fraudulent transaction in that plaintiff's security interest was violated. Therefore, the parent corporation was secondarily liable to the plaintiff for the balance due on the purchase of his business, the subsidiary being primarily liable. Rudio v. Yellowstone Merchandising Corp., 200 M 537, 652 P2d 1163, 39 St. Rep. 1923 (1982).

Business Equipment for Lease: A trencher held by a leasing business falls into none of the categories for which filing is not required. Since it is business equipment for lease, the perfection of a security interest in the trencher required filing with the Secretary of State. Between two rival security interests, one filed with the Secretary of State on June 19, 1978, and one filed initially with a County Clerk and Recorder on December 13, 1979, and subsequently filed with the Secretary of State on March 13, 1981, the former prevailed. Taylor Rental Corp. v. First Citizens Bank, 539 F. Supp. 228, 39 St. Rep. 985 (D.C. Mont. 1982).

Security Interest in Collateral: Where a tractor was sold to a third party in violation of plaintiff's security agreement within the 4-month grace period allowed by Article 9, defendant took the tractor "subject to" plaintiff's security interest. Exch. Bank of Osceola v. Jarrett, 180 M 33, 588 P2d 1006 (1979).

30-9A-403. Agreement not to assert defense against assignee.

Official Comments

1. **Source.** Former Section 9-206 [30-9-206, now repealed].

2. **Scope and Purpose.** Subsection (b) [subsection (2)], like former Section 9-206 [30-9-206, now repealed], generally validates an agreement between an account debtor and an assignor that the account debtor will not assert against an assignee claims and defenses that it may have against the assignor. These agreements are typical in installment sale agreements and leases. However, this section expands former Section 9-206 [30-9-206, now repealed] to apply to all account debtors; it is not limited to account debtors that have bought or leased goods. This section applies only to the obligations of an "account debtor," as defined in Section 9-102 [30-9A-102]. Thus, it does not determine the circumstances under which and the extent to which a person who is obligated on a negotiable instrument is disabled from asserting claims and defenses. Rather, Article 3 [Title 30, chapter 3] must be consulted. See, e.g., Sections 3-305, 3-306 [30-3-305, 30-3-306]. Article 3 [Title 30, chapter 3] governs even when the negotiable instrument constitutes part of chattel paper. See Section 9-102 [30-9A-102] (an obligor on a negotiable instrument constituting part of chattel paper is not an "account debtor").

3. **Conditions of Validation; Relationship to Article 3 [Title 30, chapter 3].** Subsection (b) [subsection (2)] validates an account debtor's agreement only if the assignee takes an assignment for value, in good faith, and without notice of conflicting claims to the property assigned or of certain claims or defenses of the assignor. Like former Section 9-206 [30-9-206, now repealed], this section is designed to put the assignee in a position that is no better and no worse than that of a holder in due course of an negotiable instrument under Article 3 [Title 30, chapter 3]. However, former Section 9-206 [30-9-206, now repealed] left open certain issues, e.g., whether the section incorporated the special Article 3 [Title 30, chapter 3] definition of "value" in Section 3-303 [30-3-303] or the generally applicable definition in Section 1-201(44) [30-1-201(44)]. Subsection (a) [subsection (1)] addresses this question; it provides that "value" has the meaning specified in Section 3-303(a) [30-3-303(1)]. Similarly, subsection (c) [subsection (3)] provides that subsection (b) [subsection (2)] does not validate an agreement with respect to defenses that could be asserted against a holder in due course under Section 9-305(b) [30-9A-305(2)] (the so-called "real" defenses). In 1990, the definition of "holder in due course" (Section 3-302 [30-3-302]) and the articulation of the rights of a holder in due course (Sections 3-305 and 3-306 [30-3-305, 30-3-306])

were revised substantially. This section tracks more closely the rules of Sections 3-302, 3-305, and 3-306 [30-3-302, 30-3-305, and 30-3-306].

4. **Relationship to Terms of Assigned Property.** Former Section 9-206(2) [30-9-206(2), now repealed], concerning warranties accompanying the sale of goods, has been deleted as unnecessary. This Article [Title 30, chapter 9A] does not regulate the terms of the account, chattel paper, or general intangible that is assigned, except insofar as the account, chattel paper, or general intangible itself creates a security interest (as often is the case with chattel paper). Thus, Article 2 [Title 30, chapter 2], and not this Article [Title 30, chapter 9A], determines whether a seller of goods makes or effectively disclaims warranties, even if the sale is secured. Similarly, other law, and not this Article [Title 30, chapter 9A], determines the effectiveness of an account debtor's undertaking to pay notwithstanding, and not to assert, any defenses or claims against an assignor-e.g., a "hell-or-high-water" provision in the underlying agreement that is assigned. If other law gives effect to this undertaking, then, under principles of nemo dat, the undertaking would be enforceable by the assignee (secured party). If other law prevents the assignor from enforcing the undertaking, this section nevertheless might permit the assignee to do so. The right of the assignee to enforce would depend upon whether, under the particular facts, the account debtor's undertaking fairly could be construed as an agreement that falls within the scope of this section and whether the assignee meets the requirements of this section.

5. **Relationship to Federal Trade Commission Rule.** Subsection (d) [subsection (4)] is new. It applies to rights evidenced by a record that is required to contain, but does not contain, the notice set forth in Federal Trade Commission Rule 433, 16 C.F.R. Part 433 (the "Holder-in-Due-Course Regulations"). Under this subsection, an assignee of such a record takes subject to the consumer account debtor's claims and defenses to the same extent as it would have if the writing had contained the required notice. Thus, subsection (d) [subsection (4)] effectively renders waiver-of-defense clauses ineffective in the transactions with consumers to which it applies.

6. **Relationship to Other Law.** Like former Section 9-206(1) [30-9-206(1), now repealed], this section takes no position on the enforceability of waivers of claims and defenses by consumer account debtors, leaving that question to other law. However, the reference to "law other than this article [this chapter] " in subsection (e) [subsection (5)] encompasses administrative rules and regulations; the reference in former Section 9-206(1) [30-9-206(1), now repealed] that it replaces ("statute or decision") arguably did not.

This section does not displace other law that gives effect to a non-consumer account debtor's agreement not to assert defenses against an assignee, even if the agreement would not qualify under subsection (b) [subsection (2)]. See subsection (f) [subsection (6)]. It validates, but does not invalidate, agreements made by a non-consumer account debtor. This section also does not displace other law to the extent that the other law permits an assignee, who takes an assignment with notice of a claim of a property or possessory right, a defense, or a claim in recoupment, to enforce an account debtor's agreement not to assert claims and defenses against the assignor (e.g., a "hell-or-high-water" agreement). See Comment 4. It also does not displace an assignee's right to assert that an account debtor is estopped from asserting a claim or defense. Nor does this section displace other law with respect to waivers of potential future claims and defenses that are the subject of an agreement between the account debtor and the assignee. Finally, it does not displace Section 1-107 [30-1-107], concerning waiver of a breach that allegedly already has occurred.

Case Notes

CASES DECIDED PRIOR TO 1999 REVISION

Assignee Obligated on Contract Claims: Defendant was entitled to receive from plaintiff the value of a combine trade-in awarded on counterclaim, over and above being absolved from making payments on the contract sued on by plaintiff assignee, because the facts and circumstances surrounding plaintiff's acceptance of the contract obligated it to perform the contract upon assignor's failure to do so and subjected it to assignor's indebtedness arising out of the contract. Plaintiff could not avail itself of the protection under 30-9-206 (now repealed, see this section). Massey-Ferguson Credit Corp. v. Brown, 173 M 253, 567 P2d 440 (1977), followed in Topco, Inc. v. St., 275 M 352, 912 P2d 805, 53 St. Rep. 175 (1996).

When Seller's Breach of Oral Contract Is a Valid Defense Against Seller's Assignee: Where assignee's agent was present during seller's oral promise to make repairs to buyer, assignee cannot be considered among those whose protection is contemplated by 30-9-206 (now repealed, see this section) as the assignee did not take assignment without notice of a claim or defense.

Massey-Ferguson Credit Corp. v. Brown, 169 M 396, 547 P2d 846 (1976), distinguished with regard to a lack of implied assumption of contractual liabilities in real estate transactions in Davey v. Nessan, 252 M 397, 830 P2d 92, 49 St. Rep. 294 (1992).

30-9A-404. Rights acquired by assignee — claim and defenses against assignee.

Official Comments

1. **Source.** Former Section 9-318(1) [30-9-318(1), now repealed].

2. **Purpose; Rights of Assignee in General.** Subsection (a) [subsection (1)], like former Section 9-318(1) [30-9-318(1), now repealed], provides that an assignee generally takes an assignment subject to defenses and claims of an account debtor. Under subsection (a)(1) [subsection (1)(a)], if the account debtor's defenses on an assigned claim arise from the transaction that gave rise to the contract with the assignor, it makes no difference whether the defense or claim accrues before or after the account debtor is notified of the assignment. Under subsection (a)(2) [subsection (1)(b)], the assignee takes subject to other defenses or claims only if they accrue before the account debtor has been notified of the assignment. Of course, an account debtor may waive its right to assert defenses or claims against an assignee under Section 9-403 [30-9A-403] or other applicable law. Subsection (a) [subsection (1)] tracks Section 3-305(a)(3) [30-9A-305(1)(c)] more closely than its predecessor.

3. **Limitation on Affirmative Claims.** Subsection (b) [subsection (2)] is new. It limits the claim that the account debtor may assert against an assignee. Borrowing from Section 3-305(a)(3) [30-9A-305(1)(c)] and cases construing former Section 9-318 [30-9-318, now repealed], subsection (b) [subsection (2)] generally does not afford the account debtor the right to an affirmative recovery from an assignee.

4. **Consumer Account Debtors; Relationship to Federal Trade Commission Rule.** Subsections (c) and (d) [subsections (3) and (4)] also are new. Subsection (c) [subsection (3)] makes clear that the rules of this section are subject to other law establishing special rules for consumer account debtors. An "account debtor who is an individual" as used in subsection (c) [subsection (3)] includes individuals who are jointly or jointly and severally obligated. Subsection (d) [subsection (4)] applies to rights evidenced by a record that is required to contain, but does not contain, the notice set forth in Federal Trade Commission Rule 433, 16 C.F.R. Part 433 (the "Holder-in-Due-Course Regulations"). Under subsection (d) [subsection (4)], a consumer account debtor has the same right to an affirmative recovery from an assignee of such a record as the consumer would have had against the assignee had the record contained the required notice.

5. **Scope; Application to "Account Debtor."** This section deals only with the rights and duties of "account debtors"-and for the most part only with account debtors on accounts, chattel paper, and payment intangibles. Subsection (e) [subsection (5)] provides that the obligation of an insurer with respect to a health-care-insurance receivable is governed by other law. References in this section to an "account debtor" include account debtors on collateral that is proceeds. Neither this section nor any other provision of this Article [Title 30, chapter 9A], including Sections 9-408 and 9-409 [30-9A-408 and 30-9A-409], provides analogous regulation of the rights and duties of other obligors on collateral, such as the maker of a negotiable instrument (governed by Article 3 [Title 30, chapter 3]), the issuer of or nominated person under a letter of credit (governed by Article 5 [Title 30, chapter 5]), or the issuer of a security (governed by Article 8 [Title 30, chapter 8]). Article 9 [Title 30, chapter 9A] leaves those rights and duties untouched; however, Section 9-409 [30-9A-409] deals with the special case of letters of credit. When chattel paper is composed in part of a negotiable instrument, the obligor on the instrument is not an "account debtor," and Article 3 [Title 30, chapter 3] governs the rights of the assignee of the chattel paper with respect to the issues that this section addresses. See, e.g., Section 3-601 [30-3-601] (dealing with discharge of an obligation to pay a negotiable instrument).

Case Notes

Inadequate Notice of Assignment — Escrow Agent Not Liable for Failure to Disburse Funds to Party With No Escrow Rights: Brandts invested in a condominium development corporation, loaning $20,000 to the corporation president. The promissory note exchanged for the loan provided that Brandts would be repaid with interest upon sale of a condominium to a family trust. Sande acted as escrow agent for the closing of the real estate sale and purchase transaction. The corporation president had instructed the title company to repay Brandts upon closing, but later rescinded that instruction, so funds from the purchase of the condominium were disbursed to the corporation and to various creditors instead of to Brandts. When the corporation was later sold, Brandts signed an agreement releasing and discharging their claims against the corporation. Nearly 2 years later, Brandts sued Sande and the title company for negligently and wrongfully applying $20,000 from the escrow account. The District Court summarily dismissed the suit and ordered sanctions against Brandts for filing a frivolous complaint. The court determined that there was neither a valid assignment nor legal notice of an assignment of Brandts' interest in the funds from the closing, so Sande owed no legal duty to Brandts. However, Brandts never asserted an irrevocable interest in the closing proceeds either prior to or during the time that the funds were in Sande's possession, nor did they execute a written assignment to ensure that the repayment instruction would not be rescinded. Under Montana law, an escrow agent or other account debtor must have adequate notice of an assignment before an assignee can hold the agent liable for wrongful payment. The promissory note did not reasonably identify the rights assigned and was thus ineffective. Brandts did not dispute that they were not a party to the escrow agreement, and because Sande had no notice of an assignment of the closing proceeds, he was not liable under an assignment theory. Sande simply fulfilled his fiduciary duty by strictly following the instructions of the principles to the escrow account, which did not assign any funds to Brandts. Summary dismissal was affirmed on grounds that Sande owed no legal duty to Brandts. Brandt v. Sande, 2000 MT 98, 299 M 256, 1 P3d 929, 57 St. Rep. 400 (2000), distinguishing Merchants & Miners Nat'l Bank v. Barnes, 18 M 335, 45 P 218 (1896).

New Agreement and Termination of Escrow by Account Debtor and Assignor: The purpose for the provision requiring notice that payment is to be made to the assignee is to allow for commercial situations where accounts are used as collateral to secure a loan repayment. Borrower in this case retained right to collect account, and assignee's right of collection would ripen only upon default of borrower. Subject to this "indirect collection" situation, the account debtor could not be expected to pay assignee until he had been instructed. The payor and payee in this case could make a new agreement and terminate the escrow account as long as third parties did not intervene. First Fidelity Bank v. Matthews, 214 M 323, 692 P2d 1255, 41 St. Rep. 2502 (1984).

Intent of Section: Plaintiff purchased a truck from defendant under a retail installment sales contract that was subsequently assigned to Ford Motor Credit Company. Plaintiff had problems with the truck that could not be adequately repaired and left the truck with defendant. Plaintiff then filed suit against defendant and the credit company for rescission. Shortly after filing an answer, the credit company reassigned the contract to defendant and moved for summary judgment, which was granted. Plaintiff appealed, alleging that the assignment of the retail installment sales contract imposed full contract liability on the assignee of certain rights under the contract. The court relied on other courts' interpretation of section 9-318 of the U.C.C. (30-9-318, MCA, now repealed, see 30-9A-404 through 30-9A-406). The court held that the intent of 30-9-318 (now repealed, see 30-9A-404 through 30-9A-406) was to allow an account debtor to assert contractual defenses as a setoff. The provisions were not intended, generally, to place the assignee of a contract in the position of being held a guarantor of a product in place of the assignor. The summary judgment was affirmed. Cuchine v. H.O. Bell, Inc., 210 M 312, 682 P2d 723, 41 St. Rep. 1074 (1984).

Assignee Obligated on Contract Claims: Defendant was entitled to receive from plaintiff the value of a combine trade-in awarded on counterclaim, over and above being absolved from making payments on the contract sued on by plaintiff assignee, because the facts and circumstances surrounding plaintiff's acceptance of the contract obligated it to perform the contract upon assignor's failure to do so and subjected it to assignor's indebtedness arising out of the contract. Plaintiff could not avail itself of the protection under 30-9-206 (now repealed, see 30-9A-403). Massey-Ferguson Credit Corp. v. Brown, 173 M 253, 567 P2d 440 (1977), followed in Topco, Inc. v. St., 275 M 352, 912 P2d 805, 53 St. Rep. 175 (1996), and distinguished, with regard to a lack of implied assumption of contractual liabilities in real estate transactions, in Davey v. Nessan, 252 M 397, 830 P2d 92, 49 St. Rep. 294 (1992).

30-9A-405. Modification of assigned contract.

Official Comments

1. **Source.** Former Section 9-318(2) [30-9-318(2), now repealed].

2. **Modification of Assigned Contract.** The ability of account debtors and assignors to modify assigned contracts can be important, especially in the case of government contracts and complex contractual arrangements (e.g., construction contracts) with respect to which modifications are customary. Subsections (a) and (b) [subsections (1) and (2)] provide that good-faith modifications of assigned contracts are binding against an assignee to the extent that (i) the right to payment has not been fully earned or (ii) the right to payment has been earned and notification of the assignment has not been given to the account debtor. Former Section 9-318(2) [30-9-318(2), now repealed] did not validate modifications of fully-performed contracts

under any circumstances, whether or not notification of the assignment had been given to the account debtor. Subsection (a) [subsection (1)] protects the interests of assignees by (i) limiting the effectiveness of modifications to those made in good faith, (ii) affording the assignee with corresponding rights under the contract as modified, and (iii) recognizing that the modification may be a breach of the assignor's agreement with the assignee.

3. **Consumer Account Debtors.** Subsection (c) [subsection (3)] is new. It makes clear that the rules of this section are subject to other law establishing special rules for consumer account debtors.

4. **Account Debtors on Health-Care-Insurance Receivables.** Subsection (d) [subsection (4)] also is new. It provides that this section does not apply to an assignment of a heath-care-insurance receivable. The obligation of an insurer with respect to a health-care-insurance receivable is governed by other law.

30-9A-406. Discharge of account debtor — notification of assignment — identification and proof of assignment — restrictions on assignment of accounts, chattel paper, payment intangibles, and promissory notes ineffective.

Official Comments

1. **Source.** Former Section 9-318(3), (4) [30-9-318(3), (4), now repealed].

2. **Account Debtor's Right to Pay Assignor Until Notification.** Subsection (a) [subsection (1)] provides the general rule concerning an account debtor's right to pay the assignor until the account debtor receives appropriate notification. The revision makes clear that once the account debtor receives the notification, the account debtor cannot discharge its obligation by paying the assignor. It also makes explicit that payment to the assignor before notification, or payment to the assignee after notification, discharges the obligation. No change in meaning from former Section 9-318 [30-9-318, now repealed] is intended. Nothing in this section conditions the effectiveness of a notification on the identity of the person who gives it. An account debtor that doubts whether the right to payment has been assigned may avail itself of the procedures in subsection (c) [subsection (3)]. See Comment 4.

An effective notification under subsection (a) [subsection (1)] must be authenticated. This requirement normally could be satisfied by sending notification on the notifying person's letterhead or on a form on which the notifying person's name appears. In each case the printed name would be a symbol adopted by the notifying person for the purpose of identifying the person and adopting the notification. See Section 9-102 [30-9A-102] (defining "authenticate").

Subsection (a) [subsection (1)] applies only to account debtors on accounts, chattel paper, and payment intangibles. (Section 9-102 [30-9A-102] defines the term "account debtor" more broadly, to include those obligated on all general intangibles.) Although subsection (a) [subsection (1)] is more precise than its predecessor, it probably does not change the rule that applied under former Article 9 [Title 30, chapter 9, now repealed]. Former Section 9-318(3) [30-9-318(3), now repealed] referred to the account debtor's obligation to "pay," indicating that the subsection was limited to account debtors on accounts, chattel paper, and other payment obligations.

3. **Limitations on Effectiveness of Notification.** Subsection (b) [subsection (2)] contains some special rules concerning the effectiveness of a notification under subsection (a) [subsection (1)].

Subsection (b)(1) [subsection (2)(a)] tracks former Section 9-318(3) [30-9-318(3), now repealed] by making ineffective a notification that does not reasonably identify the rights assigned. A reasonable identification need not identify the right to payment with specificity, but what is reasonable also is not left to the arbitrary decision of the account debtor. If an account debtor has doubt as to the adequacy of a notification, it may not be safe in disregarding the notification unless it notifies the assignee with reasonable promptness as to the respects in which the account debtor considers the notification defective.

Subsection (b)(2) [subsection (2)(b)], which is new, applies only to sales of payment intangibles. It makes a notification ineffective to the extent that other law gives effect to an agreement between an account debtor and a seller of a payment intangible that limits the account debtor's duty to pay a person other than the seller. Payment intangibles are substantially less fungible than accounts and chattel paper. In some (e.g., commercial bank loans), account debtors customarily and legitimately expect that they will not be required to pay any person other than the financial institution that has advanced funds.

It has become common in financing transactions to assign interests in a single obligation to more than one assignee. Requiring an account debtor that owes a single obligation to make multiple payments to multiple assignees would be unnecessarily burdensome. Thus, under subsection (b)(3) [subsection (2)(c)], an account debtor that is notified to pay an assignee less than the full amount of any installment or other periodic payment has the option to treat the notification as ineffective, ignore the notice, and discharge the assigned obligation by paying the assignor. Some account debtors may not realize that the law affords them the right to ignore certain notices of assignment with impunity. By making the notification ineffective at the account debtor's option, subsection (b)(3) [subsection (2)(c)] permits an account debtor to pay the assignee in accordance with the notice and thereby to satisfy its obligation pro tanto. Under subsection (g) [subsection (7)], the rights and duties created by subsection (b)(3) [subsection (2)(c)] cannot be waived or varied.

4. **Proof of Assignment.** Subsection (c) [subsection (3)] links payment with discharge, as in subsection (a) [subsection (1)]. It follows former Section 9-318(3) [30-9-318(3), now repealed] in referring to the right of the account debtor to pay the assignor if the requested proof of assignment is not seasonably forthcoming. Even if the proof is not forthcoming, the notification of assignment would remain effective, so that, in the absence of reasonable proof of the assignment, the account debtor could discharge the obligation by paying either the assignee or the assignor. Of course, if the assignee did not in fact receive an assignment, the account debtor cannot discharge its obligation by paying a putative assignee who is a stranger. The observations in Comment 3 concerning the reasonableness of an identification of a right to payment also apply here. An account debtor that questions the adequacy of proof submitted by an assignor would be well advised to promptly inform the assignor of the defects.

An account debtor may face another problem if its obligation becomes due while the account debtor is awaiting reasonable proof of the assignment that it has requested from the assignee. This section does not excuse the account debtor from timely compliance with its obligations. Consequently, an account debtor that has received a notification of assignment and who has requested reasonable proof of the assignment may discharge its obligation by paying the assignor at the time (or even earlier if reasonably necessary to avoid risk of default) when a payment is due, even if the account debtor has not yet received a response to its request for proof. On the other hand, after requesting reasonable proof of the assignment, an account debtor may not discharge its obligation by paying the assignor substantially in advance of the time that the payment is due unless the assignee has failed to provide the proof seasonably.

5. **Contractual Restrictions on Assignment.** Former Section 9-318(4) [30-9-318(4), now repealed] rendered ineffective an agreement between an account debtor and an assignor which prohibited assignment of an account (whether outright or to secure an obligation) or prohibited a security assignment of a general intangible for the payment of money due or to become due. Subsection (d) [subsection (4)] essentially follows former Section 9-318(4) [30-9-318(4), now repealed], but expands the rule of free assignability to chattel paper (subject to Sections 2A-303 and 9-407 [30-2A-303 and 30-9A-407]) and promissory notes and explicitly overrides both restrictions and prohibitions of assignment. The policies underlying the ineffectiveness of contractual restrictions under this section build on common-law developments that essentially have eliminated legal restrictions on assignments of rights to payment as security and other assignments of rights to payment such as accounts and chattel paper. Any that might linger for accounts and chattel paper are addressed by new subsection (f) [subsection (6)]. See Comment 6.

Former Section 9-318(4) [30-9-318(4), now repealed] did not apply to a sale of a payment intangible (as described in the former provision, "a general intangible for money due or to become due") but did apply to an assignment of a payment intangible for security. Subsection (e) [subsection (5)] continues this approach and also makes subsection (d) [subsection (4)] inapplicable to sales of promissory notes. Section 9-408 [30-9A-408] addresses anti-assignment clauses with respect to sales of payment intangibles and promissory notes.

Like former Section 9-318(4) [30-9-318(4), now repealed], subsection (d) [subsection (4)] provides that anti-assignment clauses are "ineffective." The quoted term means that the clause is of no effect whatsoever; the clause does not prevent the assignment from taking effect between the parties and the prohibited assignment does not constitute a default under the agreement between the account debtor and assignor. However, subsection (d) [subsection (4)] does not override terms that do not directly prohibit, restrict, or require consent to an assignment but which might, nonetheless, present a practical impairment of the assignment. Properly read, however, subsection (d) [subsection (4)] reaches only covenants that prohibit, restrict, or require consents to assignments; it does not override all terms that might "impair" an assignment in fact.

Example: Buyer enters into an agreement with Seller to buy equipment that Seller is to manufacture according to Buyer's specifications. Buyer agrees to make a series of prepayments during the construction process. In return, Seller agrees to set aside the prepaid funds in a special account and to use the funds solely for the manufacture of the designated equipment. Seller also agrees that it will not assign any of its rights under the sale agreement with Buyer. Nevertheless, Seller grants to Secured Party a security interest in its accounts. Seller's anti-assignment agreement is ineffective under subsection (d) [subsection (4)]; its agreement concerning the use of prepaid funds, which is not a restriction or prohibition on assignment, is not. However, if Secured Party notifies Buyer to make all future payments directly to Secured Party, Buyer will be obliged to do so under subsection (a) [subsection (1)] if it wishes the payments to discharge its obligation. Unless Secured Party releases the funds to Seller so that Seller can comply with its use-of-funds covenant, Seller will be in breach of that covenant. In the example, there appears to be a plausible business purpose for the use-of-funds covenant. However, a court may conclude that a covenant with no business purpose other than imposing an impediment to an assignment actually is a direct restriction that is rendered ineffective by subsection (d) [subsection (4)].

6. **Legal Restrictions on Assignment.** Former Section 9-318(4) [30-9-318(4), now repealed], like subsection (d) [subsection (4)] of this section, addressed only contractual restrictions on assignment. The former section was grounded on the reality that legal, as opposed to contractual, restrictions on assignments of rights to payment had largely disappeared. New subsection (f) [subsection (6)] codifies this principle of free assignability for accounts and chattel paper. For the most part the discussion of contractual restrictions in Comment 5 applies as well to legal restrictions rendered ineffective under subsection (f) [subsection (6)].

7. **Multiple Assignments.** This section, like former Section 9-318 [30-9-318, now repealed], is not a complete codification of the law of assignments of rights to payment. In particular, it is silent concerning many of the ramifications for an account debtor in cases of multiple assignments of the same right. For example, an assignor might assign the same receivable to multiple assignees (which assignments could be either inadvertent or wrongful). Or, the assignor could assign the receivable to assignee-1, which then might re-assign it to assignee-2, and so forth. The rights and duties of an account debtor in the face of multiple assignments and in other circumstances not resolved in the statutory text are left to the common-law rules. See, e.g., Restatement (2d), Contracts §§ 338(3), 339. The failure of former Article 9 [Title 30, chapter 9, now repealed] to codify these rules does not appear to have caused problems.

8. **Consumer Account Debtors.** Subsection (h) [subsection (8)] is new. It makes clear that the rules of this section are subject to other law establishing special rules for consumer account debtors.

9. **Account Debtors on Health-Care-Insurance Receivables.** Subsection (i) [subsection (9)] also is new. The obligation of an insurer with respect to a health-care-insurance receivable is governed by other law. Section 9-408 [30-9A-408] addresses contractual and legal restrictions on the assignment of a health-care-insurance receivable.

Compiler's Comments

2013 Amendment: Chapter 75 deleted former (5)(a) that read: "(a) the assignment or transfer or the creation, attachment, perfection, or enforcement of a security interest in:

(i) a claim or right to receive compensation for injuries or sickness as described in 26 U.S.C. 104(a)(2); or

(ii) a claim or right to receive benefits under a special needs trust as described in 42 U.S.C. 1396p(d)(4)" and after "promissory note" inserted provision regarding other than a sale pursuant to a disposition or acceptance of collateral; and made minor changes in style. Amendment effective July 1, 2013.

Saving Clause: Section 26, Ch. 75, L. 2013, provided: "(1) Except as otherwise provided in [sections 19 through 25] [Title 30, chapter 9A, part 8], this chapter applies to a transaction or lien within its scope, even if the transaction or lien was entered into or created before [the effective of this act] [July 1, 2013].

(2) This chapter does not affect an action, case, or proceeding commenced before [the effective date of this act] [July 1, 2013]."

2001 Amendment: Chapter 179 in catchline substituted "restrictions on assignment of accounts, chattel paper, payment intangibles, and promissory notes" for "term prohibiting assignment"; in (2)(c)(i) substituted "payment intangible" for "general intangible"; in (4)(b) before "creation" inserted "assignment or transfer or the"; inserted (5)(a) concerning assignment or transfer or creation, attachment, perfection, or enforcement of certain security interests; inserted (6) concerning rule of law, statute, or regulation concerning consent; and made minor changes in style. Amendment effective July 1, 2001.

30-9A-407. Restrictions on creation or enforcement of security interest in leasehold interest or in lessor's residual interest.

Official Comments

1. **Source.** Section 2A-303 [30-2A-303].

2. **Restrictions on Assignment Generally Ineffective.** Under subsection (a) [subsection (1)], as under former Section 2A-303(3) [30-2A-303(3)], a term in a lease agreement which prohibits or restricts the creation of a security interest generally is ineffective. This reflects the general policy of Section 9-406(d) [30-9A-406(4)] and former Section 9-318(4) [30-9-318(4), now repealed, see 30-9A-406]. This section has been conformed in several respects to analogous provisions in Sections 9-406, 9-408, and 9-409 [30-9A-406, 30-9A-408, and 30-9A-409], including the substitution of "ineffective" for "not enforceable" and the substitution of "assignment or transfer of, or the creation, attachment, perfection, or enforcement of a security interest" for "creation or enforcement of a security interest."

3. **Exceptions for Certain Transfers and Delegations.** Subsection (b) [subsection (2)] provides exceptions to the general ineffectiveness of restrictions under subsection (a) [subsection (1)]. A term that otherwise is ineffective under subsection (a)(2) [subsection (1)(b)] is effective to the extent that a lessee transfers its right to possession and use of goods or if either party delegates material performance of the lease contract in violation of the term. However, under subsection (c) [subsection (3)], as under former Section 2A-303(3) [30-2A-303(3)], a lessor's creation of a security interest in its interest in a lease contract or its residual interest in the leased goods is not a material impairment under Section 2A-303(4) [30-2A-303(4)] (former Section 2A-303(5) [30-2A-303(5)]), absent an actual delegation of the lessor's material performance. The terms of the lease contract determine whether the lessor, in fact, has any remaining obligations to perform. If it does, it is then necessary to determine whether there has been an actual delegation of "material performance." See Section 2A-303 [30-2A-303], Comments 3 and 4.

Compiler's Comments

2001 Amendment: Chapter 179 in (1)(a) before "creation" inserted "assignment or transfer of, or the"; in (1)(b) before "creation" inserted "assignment or transfer or the"; and made minor changes in style. Amendment effective July 1, 2001.

30-9A-408. Restrictions on assignment of promissory notes, health-care-insurance receivables, and certain general intangibles ineffective.

Official Comments

1. **Source.** New.

2. **Free Assignability.** This section makes ineffective any attempt to restrict the assignment of a general intangible, health-care-insurance receivable, or promissory note, whether the restriction appears in the terms of a promissory note or the agreement between an account debtor and a debtor (subsection (a) [subsection (1)]) or in a rule of law, including a statute or governmental rule or regulation (subsection (c) [subsection (3)]). This result allows the creation, attachment, and perfection of a security interest in a general intangible, such as an agreement for the nonexclusive license of software, as well as sales of certain receivables, such as a health-care-insurance receivable (which is an "account"), payment intangible, or promissory note, without giving rise to a default or breach by the assignor or from triggering a remedy of the account debtor or person obligated on a promissory note. This enhances the ability of certain debtors to obtain credit. On the other hand, subsection (d) [subsection (4)] protects the other party-the "account debtor" on a general intangible or the person obligated on a promissory note-from adverse effects arising from the security interest. It leaves the account debtor's or obligated person's rights and obligations unaffected in all material respects if a restriction rendered ineffective by subsection (a) or (c) [subsection (1) or (3)] would be effective under law other than Article 9 [Title 30, chapter 9A].

Example 1: A term of an agreement for the nonexclusive license of computer software prohibits the licensee from assigning any of its rights as licensee with respect to the software. The agreement also provides that an attempt to assign rights in violation of the restriction is a default entitling the licensor to terminate the license agreement. The licensee, as debtor, grants to a secured party a security interest in its rights under the license and in the computers in which it is installed. Under this section, the term prohibiting assignment and providing for a default upon an attempted assignment is ineffective to prevent the creation, attachment, or perfection of the security interest or entitle the licensor to terminate the license agreement. However, under subsection (d) [subsection (4)], the secured party (absent the licensor's agreement) is not entitled to enforce the license or to use, assign, or otherwise enjoy the benefits of the licensed software, and the licensor need not recognize (or pay any attention to) the secured party. Even if the secured party takes possession of the computers on the debtor's default, the debtor would remain free to remove the software from the computer, load it on another computer, and continue to use it, if the license so permits. If the debtor does not remove the software, other law may require the secured party to remove it before disposing of the computer. Disposition of the software with the computer could violate an effective prohibition on enforcement of the security interest. See subsection (d) [subsection (4)].

3. **Nature of Debtor's Interest.** Neither this section nor any other provision of this Article [Title 30, chapter 9A] determines whether a debtor has a property interest. The definition of the term "security interest" provides that it is an "interest in personal property." See Section 1-201(b)(35) [30-1-201(2)(jj)]. Ordinarily, a debtor can create a security interest in collateral only if it has "rights in the collateral." See Section 9-203(b) [30-9A-203(2)]. Other law determines whether a debtor has a property interest ("rights in the collateral") and the nature of that interest. For example, the nonexclusive license addressed in Example 1 may not create any property interest whatsoever in the intellectual property (e.g., copyright) that underlies the license and that effectively enables the licensor to grant the license. The debtor's property interest may be confined solely to its interest in the promises made by the licensor in the license agreement (e.g., a promise not to sue the debtor for its use of the software).

4. **Scope: Sales of Payment Intangibles and Other General Intangibles; Assignments Unaffected by this Section.** Subsections (a) and (c) [subsections (1) and (3)] render ineffective restrictions on assignments only "to the extent" that the assignments restrict the "creation, attachment, or perfection of a security interest," including sales of payment intangibles and promissory notes. This section does not render ineffective a restriction on an assignment that does not create a security interest. For example, if the debtor in Comment 2, Example 1 purported to assign the license to another entity that would use the computer software itself, other law would govern the effectiveness of the anti-assignment provisions.

Subsection (a) [subsection (1)] applies to a security interest in payment intangibles only if the security interest arises out of sale of the payment intangibles. Contractual restrictions directed to security interests in payment intangibles which secure an obligation are subject to Section 9-406(d) [30-9A-406(4)]. Subsection (a) [subsection (1)] also deals with sales of promissory notes which also create security interests. See Section 9-109(a) [30-9A-109(1)]. Subsection (c) [subsection (3)] deals with all security interests in payment intangibles or promissory notes, whether or not arising out of a sale.

Subsection (a) [subsection (1)] does not render ineffective any term, and subsection (c) [subsection (3)] does not render ineffective any law, statute or regulation, that restricts outright sales of general intangibles other than payment intangibles. They deal only with restrictions on security interests. The only sales of general intangibles that create security interests are sales of payment intangibles.

5. **Terminology: "Account Debtor"; "Person Obligated on a Promissory Note."** This section uses the term "account debtor" as it is defined in Section 9-102 [30-9A-102]. The term refers to the party, other than the debtor, to a general intangible, including a permit, license, franchise, or the like, and the person obligated on a health-care-insurance receivable, which is a type of account. The definition of "account debtor" does not limit the term to persons who are obligated to pay under a general intangible. Rather, the term includes all persons who are obligated on a general intangible, including those who are obligated to render performance in exchange for payment. In some cases, e.g., the creation of a security interest in a franchisee's rights under a franchise agreement, the principal payment obligation may be owed by the debtor (franchisee) to the account debtor (franchisor). This section also refers to a "person obligated on a promissory note," inasmuch as those persons do not fall within the definition of "account debtor."

Example 2: A licensor and licensee enter into an agreement for the nonexclusive license of computer software. The licensee's interest in the license agreement is a general intangible. If the licensee grants to a secured party a security interest in its rights under the license agreement, the licensee is the debtor and the licensor is the account debtor. On the other hand, if the licensor grants to a secured party a security interest in its right to payment (an account) under the license agreement, the licensor is the debtor and the licensee is the account debtor. (This section applies to the security interest in the general intangible but not to the security interest in the account, which is not a health-care-insurance receivable.)

6. **Effects on Account Debtors and Persons Obligated on Promissory Notes.** Subsections (a) and (c) [subsections (1) and (3)] affect two classes of persons. These subsections affect account debtors on general intangibles and health-care-insurance receivables and persons

obligated on promissory notes. Subsection (c) [subsection (3)] also affects governmental entities that enact or determine rules of law. However, subsection (d) [subsection (4)] ensures that these affected persons are not affected adversely. That provision removes any burdens or adverse effects on these persons for which any rational basis could exist to restrict the effectiveness of an assignment or to exercise any remedies. For this reason, the effects of subsections (a) and (c) [subsections (1) and (3)] are immaterial insofar as those persons are concerned.

Subsection (a) [subsection (1)] does not override terms that do not directly prohibit, restrict, or require consent to an assignment but which might, nonetheless, present a practical impairment of the assignment. Properly read, however, this section, like Section 9-406(d) [30-9A-406(4)], reaches only covenants that prohibit, restrict, or require consents to assignments; it does not override all terms that might "impair" an assignment in fact.

Example 3: A licensor and licensee enter into an agreement for the nonexclusive license of valuable business software. The license agreement includes terms (i) prohibiting the licensee from assigning its rights under the license, (ii) prohibiting the licensee from disclosing to anyone certain information relating to the software and the licensor, and (iii) deeming prohibited assignments and prohibited disclosures to be defaults. The licensee wishes to obtain financing and, in exchange, is willing to grant a security interest in its rights under the license agreement. The secured party, reasonably, refuses to extend credit unless the licensee discloses the information that it is prohibited from disclosing under the license agreement. The secured party cannot determine the value of the proposed collateral in the absence of this information. Under this section, the terms of the license prohibiting the assignment (grant of the security interest) and making the assignment a default are ineffective. However, the nondisclosure covenant is not a term that prohibits the assignment or creation of a security interest in the license. Consequently, the nondisclosure term is enforceable even though the practical effect is to restrict the licensee's ability to use its rights under the license agreement as collateral. The nondisclosure term also would be effective in the factual setting of Comment 2, Example 1. If the secured party's possession of the computers loaded with software would put it in a position to discover confidential information that the debtor was prohibited from disclosing, the licensor should be entitled to enforce its rights against the secured party. Moreover, the licensor could have required the debtor to obtain the secured party's agreement that (i) it would immediately return all copies of software loaded on the computers and that (ii) it would not examine or otherwise acquire any information contained in the software. This section does not prevent an account debtor from protecting by agreement its independent interests that are unrelated to the "creation, attachment, or perfection" of a security interest. In Example 1, moreover, the secured party is not in possession of copies of software by virtue of its security interest or in connection with enforcing its security interest in the debtor's license of the software. Its possession is incidental to its possession of the computers, in which it has a security interest. Enforcing against the secured party a restriction relating to the software in no way interferes with its security interest in the computers.

7. **Effect in Assignor's Bankruptcy.** This section could have a substantial effect if the assignor enters bankruptcy. Roughly speaking, Bankruptcy Code Section 552 invalidates security interests in property acquired after a bankruptcy petition is filed, except to the extent that the postpetition property constitutes proceeds of prepetition collateral.

Example 4: A debtor is the owner of a cable television franchise that, under applicable law, cannot be assigned without the consent of the municipal franchisor. A lender wishes to extend credit to the debtor, provided that the credit is secured by the debtor's "going business" value. To secure the loan, the debtor grants a security interest in all its existing and after-acquired property. The franchise represents the principal value of the business. The municipality refuses to consent to any assignment for collateral purposes. If other law were given effect, the security interest in the franchise would not attach; and if the debtor were to enter bankruptcy and sell the business, the secured party would receive but a fraction of the business's value. Under this section, however, the security interest would attach to the franchise. As a result, the security interest would attach to the proceeds of any sale of the franchise while a bankruptcy is pending. However, this section would protect the interests of the municipality by preventing the secured party from enforcing its security interest to the detriment of the municipality.

8. **Effect Outside of Bankruptcy.** The principal effects of this section will take place outside of bankruptcy. Compared to the relatively few debtors that enter bankruptcy, there are many more that do not. By making available previously unavailable property as collateral, this section should enable debtors to obtain additional credit. For purposes of determining whether to extend credit, under some circumstances a secured party may ascribe value to the collateral to which its security interest has attached, even if this section precludes the secured party from

enforcing the security interest without the agreement of the account debtor or person obligated on the promissory note. This may be the case where the secured party sees a likelihood of obtaining that agreement in the future. This may also be the case where the secured party anticipates that the collateral will give rise to a type of proceeds as to which this section would not apply.

Example 5: Under the facts of Example 4, the debtor does not enter bankruptcy. Perhaps in exchange for a fee, the municipality agrees that the debtor may transfer the franchise to a buyer. As consideration for the transfer, the debtor receives from the buyer its check for part of the purchase price and its promissory note for the balance. The security interest attaches to the check and promissory note as proceeds. See Section 9-315(a)(2) [30-9A-315(1)(b)]. This section does not apply to the security interest in the check, which is not a promissory note, health-care-insurance receivable, or general intangible. Nor does it apply to the security interest in the promissory note, inasmuch as it was not sold to the secured party.

9. **Contrary Federal Law.** This section does not override federal law to the contrary. However, it does reflect an important policy judgment that should provide a template for future federal law reforms.

Compiler's Comments

2013 Amendment: Chapter 75 in (2) after "promissory note" inserted provision regarding other than a sale pursuant to a disposition or acceptance of collateral. Amendment effective July 1, 2013.

Saving Clause: Section 26, Ch. 75, L. 2013, provided: "(1) Except as otherwise provided in [sections 19 through 25] [Title 30, chapter 9A, part 8], this chapter applies to a transaction or lien within its scope, even if the transaction or lien was entered into or created before [the effective of this act] [July 1, 2013].

(2) This chapter does not affect an action, case, or proceeding commenced before [the effective date of this act] [July 1, 2013]."

2001 Amendment: Chapter 179 in (1)(b) and (3)(b) before "creation" inserted "assignment or transfer or the"; inserted (5) excluding certain assignments or transfers or the creation, attachment, or perfection of a security interest from the application of subsections (1) and (3); and made minor changes in style. Amendment effective July 1, 2001.

30-9A-409. Restrictions on assignment of letter-of-credit rights ineffective.

Official Comments

1. **Source.** New.

2. **Purpose and Relevance.** This section, patterned on Section 9-408 [30-9A-408], limits the effectiveness of attempts to restrict the creation, attachment, or perfection of a security interest in letter-of-credit rights, whether the restriction appears in the letter of credit or a rule of law, custom, or practice applicable to the letter of credit. It protects the creation, attachment, and perfection of a security interest while preventing these events from giving rise to a default or breach by the assignor or from triggering a remedy or defense of the issuer or other person obligated on a letter of credit. Letter-of-credit rights are a type of supporting obligation. See Section 9-102 [30-9A-102]. Under Sections 9-203 and 9-308 [30-9A-203 and 30-9A-308], a security interest in a supporting obligation attaches and is perfected automatically if the security interest in the supported obligation attaches and is perfected. See Section 9-107 [30-9A-107], Comment 5. The automatic attachment and perfection under Article 9 [Title 30, chapter 9A] would be anomalous or misleading if, under other law (e.g., Article 5 [Title 30, chapter 5]), a restriction on transfer or assignment were effective to block attachment and perfection.

3. **Relationship to Letter-of-Credit Law.** Although restrictions on an assignment of a letter of credit are ineffective to prevent creation, attachment, and perfection of a security interest, subsection (b) [subsection (2)] protects the issuer and other parties from any adverse effects of the security interest by preserving letter-of-credit law and practice that limits the right of a beneficiary to transfer its right to draw or otherwise demand performance (Section 5-112 [see 30-8-128]) and limits the obligation of an issuer or nominated person to recognize a beneficiary's assignment of letter-of-credit proceeds (Section 5-114 [30-5-134]). Thus, this section's treatment of letter-of-credit rights differs from this Article's [Title 30, chapter 9A] treatment of instruments and investment property. Moreover, under Section 9-109(c)(4) [30-9A-109(3)(d)], this Article [Title 30, chapter 9A] does not apply to the extent that the rights of a transferee beneficiary or nominated person are independent and superior under Section 5-114 [30-5-134], thereby preserving the "independence principle" of letter-of-credit law.

Compiler's Comments

2001 Amendment: Chapter 179 near beginning of (1)(b) before "creation" inserted "assignment or the". Amendment effective July 1, 2001.

30-9A-420. Removal of improper or fraudulent liens — notice to secured party and debtor.

Compiler's Comments

2007 Amendment: Chapter 69 in catchline at end inserted "notice to secured party and debtor"; and in (1) at end inserted "and the debtor". Amendment effective October 1, 2007.

Part 5

Filing

Part Compiler's Comments

Saving Clause: Section 169, Ch. 305, L. 1999, provided: "(1) Except as otherwise provided in [sections 164 through 169] [sections 162 through 167—30-9A-703 through 30-9A-706, 30-9A-708, and 30-9A-709], [this act] applies to a transaction or lien within its scope, even if the transaction or lien was entered into or created before [this act] takes effect.

(2) Except as otherwise provided in subsection (3) and [sections 164 through 169] [sections 162 through 167—30-9A-703 through 30-9A-706, 30-9A-708, and 30-9A-709]:

(a) transactions and liens that were not governed by [former chapter 9, now repealed] were validly entered into or created before [this act] takes effect and would be subject to [this act] if they had been entered into or created after [this act] takes effect, and the rights, duties, and interests flowing from those transactions and liens remain valid after [this act] takes effect; and

(b) the transactions and liens may be terminated, completed, consummated, or enforced as required or permitted by [this act] or by the law that otherwise would apply if [this act] did not take effect.

(3) [This act] does not affect an action, case, or proceeding commenced before [this act] takes effect."

Part Administrative Rules

Title 44, chapter 6, ARM Secretary of State — Uniform Commercial Code.

30-9A-501. Filing office.

Official Comments

1. **Source.** Derived from former Section 9-401 [30-9-401, now repealed].

2. **Where to File.** Subsection (a) [subsection (1)] indicates where in a given State a financing statement is to be filed. Former Article 9 [Title 30, chapter 9, now repealed] afforded each State three alternative approaches, depending on the extent to which the State desires central filing (usually with the Secretary of State), local filing (usually with a county office), or both. As Comment 1 to former Section 9-401 [30-9-401, now repealed] observed, "The principal advantage of state-wide filing is ease of access to the credit information which the files exist to provide. Consider for example the national distributor who wishes to have current information about the credit standing of the thousands of persons he sells to on credit. The more completely the files are centralized on a state-wide basis, the easier and cheaper it becomes to procure credit information; the more the files are scattered in local filing units, the more burdensome and costly." Local filing increases the net costs of secured transactions also by increasing uncertainty and the number of required filings. Any benefit that local filing may have had in the 1950's is now insubstantial. Accordingly, this Article [Title 30, chapter 9A] dictates central filing for most situations, while retaining local filing for real-estate-related collateral and special filing provisions for transmitting utilities.

3. **Minerals and Timber.** Under subsection (a)(1) [subsection (1)(a)], a filing in the office where a record of a mortgage on the related real property would be filed will perfect a security interest in as-extracted collateral. Inasmuch as the security interest does not attach until extraction, the filing continues to be effective after extraction. A different result occurs with respect to timber to be cut, however. Unlike as-extracted collateral, standing timber may be goods before it is cut. See Section 9-102 [30-9A-102] (defining "goods"). Once cut, however, it is no longer timber to be cut, and the filing in the real-property-mortgage office ceases to be effective. The timber then becomes ordinary goods, and filing in the office specified in subsection (a)(2) [subsection (1)(b)] is necessary for perfection. Note also that after the timber is cut the law of the debtor's location, not the location of the timber, governs perfection under Section 9-301 [30-9A-301].

4. **Fixtures.** There are two ways in which a secured party may file a financing statement to perfect a security interest in goods that are or are to become fixtures. It may file in the Article 9 [Title 30, chapter 9A] records, as with most other goods. See subsection (a)(2) [subsection (1)(b)]. Or it may file the financing statement as a "fixture filing," defined in Section 9-102 [30-9A-102], in the office in which a record of a mortgage on the related real property would be filed. See subsection (a)(1)(B) [subsection (1)(a)(ii)].

5. **Transmitting Utilities.** The usual filing rules do not apply well for a transmitting utility (defined in Section 9-102 [30-9A-102]). Many pre-UCC statutes provided special filing rules for railroads and in some cases for other public utilities, to avoid the requirements for filing with legal descriptions in every county in which such debtors had property. Former Section 9-401(5) [30-9-401(5), now repealed] recreated and broadened these provisions, and subsection (b) [subsection (2)] follows this approach. The nature of the debtor will inform persons searching the record as to where to make a search.

A given State's subsection (b) [subsection (2)] applies only if the local law of that State governs perfection. As to most collateral, perfection by filing is governed by the law of the jurisdiction in which the debtor is located. See Section 9-301(1) [30-9A-301(1)]. However, the law of the jurisdiction in which goods that are or become fixtures are located governs perfection by filing a fixture filing. See Section 9-301(3)(A) [30-9A-301(3)(a)]. As a consequence, filing in the filing office of more than one State may be necessary to perfect a security interest in fixtures collateral of a transmitting utility by filing a fixture filing. See Section 9-301 [30-9A-301], Comment 5.b.

Compiler's Comments

2007 Amendment: Chapter 44 in (3) after "institution" substituted "is required to" for "must". Amendment effective October 1, 2007.

2005 Amendment: Chapter 207 inserted (3) requiring that an effective financing statement, as defined in 7 U.S.C. 1631, be filed in the office of the secretary of state. Amendment effective October 1, 2005.

Administrative Rules

ARM 44.6.105 Uniform Commercial Code fees.

ARM 44.6.109 Format requirements for filing effective financing statement lien under Federal Food Security Act of 1985.

Case Notes

Applicability of Local Law When Perfecting Agricultural Liens: In a dispute over priority of an agricultural lien versus a security interest in the same profits from agricultural products, plaintiff who held a security interest asserted that defendant who held an agricultural lien did not satisfy the requirements of the Uniform Commercial Code (U.C.C.) regarding perfection because defendant's lien was not perfected in North Dakota where the farm products were located, as required by 30-9A-302, at the time that the dispute arose. However, agricultural liens follow the location of the farm products, not the location of the debtor, and when defendant's lien was created, the products in question were located in Montana. Therefore, Montana's local law was the local law designated by the U.C.C. to govern perfection of the lien. Defendant properly filed the lien in Montana and therefore did not violate the U.C.C. in perfecting the lien. Stockman Bank of Mont. v. Mon-Kota, Inc., 2008 MT 74, 342 M 115, 180 P3d 1125 (2008).

30-9A-502. Contents of financing statement — mortgage as financing statement — time of filing financing statement.

Official Comments

1. **Source.** Former Section 9-402(1), (5), (6) [30-9-402(1), (5), (6), now repealed].

2. **"Notice Filing."** This section adopts the system of "notice filing." What is required to be filed is not, as under pre-UCC chattel mortgage and conditional sales acts, the security agreement itself, but only a simple record providing a limited amount of information (financing statement). The financing statement may be filed before the security interest attaches or thereafter. See subsection (d) [subsection (4)]. See also Section 9-308(a) [30-9A-308(1)] (contemplating situations in which a financing statement is filed before a security interest attaches).

The notice itself indicates merely that a person may have a security interest in the collateral indicated. Further inquiry from the parties concerned will be necessary to disclose the complete state of affairs. Section 9-210 [30-9A-210] provides a statutory procedure under which the secured party, at the debtor's request, may be required to make disclosure. However, in many cases, information may be forthcoming without the need to resort to the formalities of that section.

Notice filing has proved to be of great use in financing transactions involving inventory, accounts, and chattel paper, because it obviates the necessity of refiling on each of a series of transactions in a continuing arrangement under which the collateral changes from day to day. However, even in the case of filings that do not necessarily involve a series of transactions (e.g., a loan secured by a single item of equipment), a financing statement is effective to encompass transactions under a security agreement not in existence and not contemplated at the time the notice was filed, if the indication of collateral in the financing statement is sufficient to cover the collateral concerned. Similarly, a financing statement is effective to cover after-acquired property of the type indicated and to perfect with respect to future advances under security agreements, regardless of whether after-acquired property or future advances are mentioned in the financing statement and even if not in the contemplation of the parties at the time the financing statement was authorized to be filed.

3. **Debtor's Signature; Required Authorization.** Subsection (a) [subsection (1)] sets forth the simple formal requirements for an effective financing statement. These requirements are: (1) the debtor's name; (2) the name of a secured party or representative of the secured party; and (3) an indication of the collateral.

Whereas former Section 9-402(1) [30-9-402(1), now repealed] required the debtor's signature to appear on a financing statement, this Article [Title 30, chapter 9A] contains no signature requirement. The elimination of the signature requirement facilitates paperless filing. (However, as PEB Commentary No. 15 indicates, a paperless financing statement was sufficient under former Article 9 [Title 30, chapter 9, now repealed].) Elimination of the signature requirement also makes the exceptions provided by former Section 9-402(2) [30-9-402(2), now repealed] unnecessary.

The fact that this Article [Title 30, chapter 9A] does not require that an authenticating symbol be contained in the public record does not mean that all filings are authorized. Rather, Section 9-509(a) [30-9A-509(1)] entitles a person to file an initial financing statement, an amendment that adds collateral, or an amendment that adds a debtor only if the debtor authorizes the filing, and Section 9-509(d) [30-9A-509(4)] entitles a person other than the debtor to file a termination statement only if the secured party of record authorizes the filing. Of course, a filing has legal effect only to the extent it is authorized. See Section 9-510 [30-9A-510].

Law other than this Article [Title 30, chapter 9A], including the law with respect to ratification of past acts, generally determines whether a person has the requisite authority to file a record under this Article [Title 30, chapter 9A]. See Section 1-103 [30-1-103]. However, under Section 9-509(b) [30-9A-509(2)], the debtor's authentication of (or becoming bound by) a security agreement ipso facto constitutes the debtor's authorization of the filing of a financing statement covering the collateral described in the security agreement. The secured party need not obtain a separate authorization.

Section 9-625 [30-9A-625] provides a remedy for unauthorized filings. Making an unauthorized filing also may give rise to civil or criminal liability under other law. In addition, this Article [Title 30, chapter 9A] contains provisions that assist in the discovery of unauthorized filings and the amelioration of their practical effect. For example, Section 9-518 [30-9A-518] provides a procedure whereby a person may add to the public record a statement to the effect that a financing statement indexed under the person's name was wrongfully filed, and Section 9-509(d) [30-9A-509(4)] entitles any person to file a termination statement if the secured party of record fails to comply with its obligation to file or send one to the debtor, the debtor authorizes the filing, and the termination statement so indicates. However, the filing office is neither obligated nor permitted to inquire into issues of authorization. See Section 9-520(a) [30-9A-520(1)].

4. **Certain Other Requirements.** Subsection (a) [subsection (1)] deletes other provisions of former Section 9-402(1) [30-9-402(1), now repealed] because they seems unwise (real-property description for financing statements covering crops), unnecessary (adequacy of copies of financing statements), or both (copy of security agreement as financing statement). In addition, the filing office must reject a financing statement lacking certain other information formerly required as a condition of perfection (e.g., an address for the debtor or secured party). See Sections 9-516(b), 9-520(a) [30-9A-516(2) and 30-9A-520(1)]. However, if the filing office accepts the record, it is effective nevertheless. See Section 9-520(c) [30-9A-520(3)].

5. **Real-Property-Related Filings.** Subsection (b) [subsection (2)] contains the requirements for financing statements filed as fixture filings and financing statements covering timber to be cut or minerals and minerals-related accounts constituting as-extracted collateral. A description of the related real property must be sufficient to reasonably identify it. See Section 9-108 [30-9A-108]. This formulation rejects the view that the real property description must be by

metes and bounds, or otherwise conforming to traditional real-property practice in conveyancing, but, of course, the incorporation of such a description by reference to the recording data of a deed, mortgage or other instrument containing the description should suffice under the most stringent standards. The proper test is that a description of real property must be sufficient so that the financing statement will fit into the real-property search system and be found by a real-property searcher. Under the optional language in subsection (b)(3) [subsection (2)(c)], the test of adequacy of the description is whether it would be adequate in a record of a mortgage of the real property. As suggested in the Legislative Note, more detail may be required if there is a tract indexing system or a land registration system.

If the debtor does not have an interest of record in the real property, a real-property-related financing statement must show the name of a record owner, and Section 9-519(d) [30-9A-519(4)] requires the financing statement to be indexed in the name of that owner. This requirement also enables financing statements covering as-extracted collateral or timber to be cut and financing statements filed as fixture filings to fit into the real-property search system.

6. **Record of Mortgage Effective as Financing Statement.** Subsection (c) [subsection (3)] explains when a record of a mortgage is effective as a financing statement filed as a fixture filing or to cover timber to be cut or as-extracted collateral. Use of the term "record of a mortgage" recognizes that in some systems the record actually filed is not the record pursuant to which a mortgage is created. Moreover, "mortgage" is defined in Section 9-102 [30-9A-102] as an "interest in real property," not as the record that creates or evidences the mortgage or the record that is filed in the public recording systems. A record creating a mortgage may also create a security interest with respect to fixtures (or other goods) in conformity with this Article [Title 30, chapter 9A]. A single agreement creating a mortgage on real property and a security interest in chattels is common and useful for certain purposes. Under subsection (c) [subsection (3)], the recording of the record evidencing a mortgage (if it satisfies the requirements for a financing statement) constitutes the filing of a financing statement as to the fixtures (but not, of course, as to other goods). Section 9-515(g) [30-9A-515(7)] makes the usual five-year maximum life for financing statements inapplicable to mortgages that operate as fixture filings under Section 9-502(c) [30-9A-502(3)]. Such mortgages are effective for the duration of the real-property recording.

Of course, if a combined mortgage covers chattels that are not fixtures, a regular financing statement filing is necessary with respect to the chattels, and subsection (c) [subsection (3)] is inapplicable. Likewise, a financing statement filed as a "fixture filing"is not effective to perfect a security interest in personal property other than fixtures.

In some cases it may be difficult to determine whether goods are or will become fixtures. Nothing in this Part prohibits the filing of a "precautionary" fixture filing, which would provide protection in the event goods are determined to be fixtures. The fact of filing should not be a factor in the determining whether goods are fixtures. Cf. Section 9-505(b) [30-9A-505(2)].

Compiler's Comments

2013 Amendment: Chapter 75 in (3)(c)(i) substituted "the record need not indicate" for "other than an indication"; inserted (3)(c)(ii) regarding the name of a debtor; and made minor changes in style. Amendment effective July 1, 2013.

Saving Clause: Section 26, Ch. 75, L. 2013, provided: "(1) Except as otherwise provided in [sections 19 through 25] [Title 30, chapter 9A, part 8], this chapter applies to a transaction or lien within its scope, even if the transaction or lien was entered into or created before [the effective of this act] [July 1, 2013].

(2) This chapter does not affect an action, case, or proceeding commenced before [the effective date of this act] [July 1, 2013]."

Optional Additions — Alternative A: Pursuant to the Legislative Note, the language "for record" in subsection (2)(b) and "sufficient to give constructive notice of a mortgage under the law of this state if the description were contained in a record of the mortgage of the real property" in subsection (2)(c) are optional additions under the Uniform Commercial Code. Furthermore, the amendments enacted in 2013 to this section were adopted because Montana chose to adopt Alternative A of the 2010 Uniform Commercial Code amendments to Section 9-503 [30-9A-503].

Administrative Rules

ARM 44.6.109 Format requirements for filing effective financing statement lien under Federal Food Security Act of 1985.

ARM 44.6.110 Definitions and format requirements for filing of Title 71 lien.

ARM 44.6.113 Definitions and requirements for online filing.

Case Notes

CASES DECIDED AFTER 1999 REVISION

Interaction of Agricultural Lien Law and Uniform Commercial Code on Secured Transactions — Filing of Agricultural Lien Adequate to Fulfill Financing Statement Requirements of Uniform Commercial Code: Agricultural liens are not security interests, and only the parts of Article 9 of the Uniform Commercial Code (U.C.C.) that expressly refer to agricultural liens, rather than those that refer only to security interests, apply to agricultural liens. Merely because collateral consists of farm products does not automatically turn an agricultural lien into a security interest. The attachment rules of Article 9 do not apply to agricultural liens; rather, agricultural liens attach according to the rules in the statutes that created agricultural liens. Similarly, 71-3-902 clearly delineates the procedure for perfecting an agricultural lien. This case presented a potential conflict regarding lien priority in that 71-3-904 grants agricultural liens a superpriority status that is not dependent on being the first to file, while 30-9A-322 states that an agricultural lien has priority over a conflicting security interest on the same collateral if the lien is perfected pursuant to 30-9A-310 of the U.C.C. Thus, agricultural lienors must satisfy the perfection requirements of 30-9A-310 in addition to the perfection requirements of 71-3-902, and by doing so, the lienors will be insulated from the U.C.C. first-in-time rule and retain the superpriority status pursuant to 71-3-904. However, because agricultural liens require the same and more information as a U.C.C. filing and both filings are documented in the same database, the filing of an agricultural lien with the Secretary of State also satisfied the financing statement requirements of the U.C.C., and a duplicate filing of a U.C.C. financing statement is not required. Stockman Bank of Mont. v. Mon-Kota, Inc., 2008 MT 74, 342 M 115, 180 P3d 1125 (2008).

CASES DECIDED PRIOR TO 1999 REVISION

Statement of Location in Security Agreement — Limiting Factor: A security agreement in livestock and their progeny which contained an after-acquired property clause and which described the livestock as being located "20 miles East of Jordan on premises owned by: James J. Murnion" is limited to livestock located on the described premises. This security agreement did not give the secured party a prior perfected security interest in the debtor's cattle that were purchased with a later loan from another bank and pastured in another location. First Nat'l Bank of Glasgow v. First Sec. Bank of Mont., 222 M 118, 721 P2d 1270, 43 St. Rep. 1105 (1986).

Effect of Noncompliance: Where financing statement described the real property to which fixtures were to be attached, but did not describe the fixtures themselves, it was erroneous but the error did not convert the statement into a mortgage, nor did it purport to claim an interest in real property by virtue of 30-9-104(j) (30-9-104(10), now repealed, see 30-9A-109). First Sec. Bank of Bozeman v. Tholkes, 169 M 422, 547 P2d 1328 (1976).

30-9A-503. Name of debtor and secured party.

Official Comments

1. **Source.** Subsections (a)(4)(A), (b), and (c) [subsections (1)(d)(i), (2), and (3)] derive from former Section 9-402(7) [30-9-402(7), now repealed]; otherwise, new.

2. **Debtor's Name.** The requirement that a financing statement provide the debtor's name is particularly important. Financing statements are indexed under the name of the debtor, and those who wish to find financing statements search for them under the debtor's name. Subsection (a) [subsection (1)] explains what the debtor's name is for purposes of a financing statement.

a. Registered Organizations. As a general matter, if the debtor is a "registered organization" (defined in Section 9-102 [30-9A-102] so as to ordinarily include corporations, limited partnerships, and limited liability companies, and statutory trusts), then the debtor's name is the name shown on the "public organic record" of the debtor's "jurisdiction of organization" (both also defined in Section 9-102 [30-9A-102]).

b. Collateral Held in a Trust. When a financing statement covers collateral that is held in a trust that is a registered organization, subsection (a)(1) [subsection (1)(a)] governs the name of the debtor. If, however, the collateral is held in a trust that is not a registered organization, subsection (a)(3) [subsection (1)(c)] applies. (As used in this Article [Title 30, chapter 9A], collateral "held in a trust" includes collateral as to which the trust is the debtor as well as collateral as to which the trustee is the debtor.) This subsection adopts a convention that generally results in the name of the trust or the name of the trust's settlor being provided as the name of the debtor on the financing statement, even if, as typically is the case with common-law trusts, the "debtor" (defined in Section 9-102 [30-9A-102]) is a trustee acting with respect to the collateral. This convention provides more accurate information and eases the burden for searchers, who otherwise would have difficulty with respect to debtor trustees that are large financial institutions.

More specifically, if a trust's organic record specifies a name for the trust, subsection (a)(3) [subsection (1)(c)] requires the financing statement to provide, as the name of the debtor, the name for the trust specified in the organic record. In addition, the financing statement must indicate, in a separate part of the financing statement, that the collateral is held in a trust.

If the organic record of the trust does not specify a name for the trust, the name required for the financing statement is the name of the settlor or, in the case of a testamentary trust, the testator, in each case as determined under subsection (h) [subsection (8)]. In addition, the financing statement must provide sufficient additional information to distinguish the trust from other trusts having one or more of the same settlors or the same testator. In many cases an indication of the date on which the trust was settled will satisfy this requirement. If neither the name nor the additional information indicates that the collateral is held in a trust, the financing statement must indicate that fact, but not as part of the debtor's name.

Neither the indication that the collateral is held in a trust nor the additional information that distinguishes the trust from other trusts having one or more of the same settlors or the same testator is part of the debtor's name. Nevertheless, a financing statement that fails to provide, in a separate part of the financing statement, any required indication or additional information does not sufficiently provide the name of the debtor under Sections 9-502(a) [30-9A-502(1)] and 9-503(a)(3) [30-9A-503(1)(c)], does not "substantially satisfy[ ] the requirements" of Part 5 within the meaning of Section 9-506(a) [30-9A-506(1)], and so is ineffective.

c. Collateral Administered by a Personal Representative. Subsection (a)(2) [subsection (1)(b)] deals with collateral that is being administered by an executor, administrator, or other personal representative of a decedent. Even if, as often is the case, the representative is the "debtor" (defined in Section 9-102 [30-9A-102]), the financing statement must provide the name of the decedent as the name of the debtor. Subsection (f) [subsection (6)] provides a safe harbor, under which the name of the decedent indicated on the order appointing the personal representative issued by the court having jurisdiction over the collateral is sufficient as the name of the decedent. If the order indicates more than one name for the decedent, the first name in the list qualifies under subsection (f) [subsection (6)]; however, other names in the list also may qualify as the "name of the decedent" within the meaning of subsection (a)(2) [subsection (1)(b)]. In addition to providing the name of the decedent, the financing statement must indicate, in a separate part of the financing statement, that the collateral is being administered by a personal representative. Although the indication is not part of the debtor's name, a financing statement that fails to provide the indication does not sufficiently provide the name of the debtor under Sections 9-502(a) [30-9A-502(1)] and 9-503(a)(2) [30-9A-503(1)(b)], does not "substantially satisfy[ ] the requirements" of Part 5 within the meaning of Section 9-506(a) [30-9A-506(1)], and so is ineffective.

d. Individuals. This Article provides alternative approaches towards the requirement for providing the name of a debtor who is an individual.

Alternative A. Alternative A distinguishes between two groups of individual debtors. For debtors holding an unexpired driver's license issued by the State where the financing statement is filed (ordinarily the State where the debtor maintains the debtor's principal residence), Alternative A requires that a financing statement provide the name indicated on the license. When a debtor does not hold an unexpired driver's license issued by the relevant State, the requirement can be satisfied in either of two ways. A financing statement is sufficient if it provides the "individual name" of the debtor. Alternatively, a financing statement is sufficient if it provides the debtor's surname (i.e., family name) and first personal name (i.e., first name other than the surname).

Alternative B. Alternative B provides three ways in which a financing statement may sufficiently provide the name of an individual who is a debtor. The "individual name" of the debtor is sufficient, as is the debtor's surname and first personal name. If the individual holds an unexpired driver's license issued by the State where the financing statement is filed (ordinarily the State of the debtor's principal residence), the name indicated on the driver's license also is sufficient.

Name indicated on the driver's license. A financing statement does not "provide the name of the individual which is indicated" on the debtor's driver's license unless the name it provides is the same as the name indicated on the license. This is the case even if the name indicated on the debtor's driver's license contains an error.

Example 1: Debtor, an individual whose principal residence is in Illinois, grants a security interest to SP in certain business equipment. SP files a financing statement with the Illinois filing office. The financing statement provides the name appearing on Debtor's Illinois driver's license, "Joseph Allan Jones." Regardless of which Alternative is in effect in Illinois, this filing would be sufficient under Illinois' Section 9-503(a) [equivalent to 30-9A-503(3)], even if Debtor's correct middle name is Alan, not Allan.

A filing against "Joseph A. Jones" or "Joseph Jones" would not "provide the name of the individual which is indicated" on the debtor's driver's license. However, these filings might be sufficient if Alternative A is in effect in Illinois and Jones has no current (i.e., unexpired) Illinois driver's license, or if Illinois has enacted Alternative B.

Determining the name that should be provided on the financing statement must not be done mechanically. The order in which the components of an individual's name appear on a driver's license differs among the States. Had the debtor in Example 1 obtained a driver's license from a different State, the license might have indicated the name as "Jones Joseph Allan." Regardless of the order on the driver's license, the debtor's surname must be provided in the part of the financing statement designated for the surname.

Alternatives A and B both refer to a license issued by "this State." Perfection of a security interest by filing ordinarily is determined by the law of the jurisdiction in which the debtor is located. See Section 9-301(1) [30-9A-301(1)]. (Exceptions to the general rule are found in Section 9-301(3) and (4) [30-9A-301(3) and (4)], concerning fixture filings, timber to be cut, and as-extracted collateral.) A debtor who is an individual ordinarily is located at the individual's principal residence. See Section 9-307(b) [30-9A-307(2)]. (An exception appears in Section 9-307(c) [30-9A-307(3)].) Thus, a given State's Section 9-503 [30-9A-503] ordinarily will apply during any period when the debtor's principal residence is located in that State, even if during that time the debtor holds or acquires a driver's license from another State.

When a debtor's principal residence changes, the location of the debtor under Section 9-307 [30-9A-307] also changes and perfection by filing ordinarily will be governed by the law of the debtor's new location. As a consequence of the application of that jurisdiction's Section 9-316 [30-9A-316], a security interest that is perfected by filing under the law of the debtor's former location will remain perfected for four months after the relocation, and thereafter if the secured party perfects under the law of the debtor's new location. Likewise, a financing statement filed in the former location may be effective to perfect a security interest that attaches after the debtor relocates. See Section 9-316(h) [30-9A-316(8)].

Individual name of the debtor. Article 9 [Title 30, chapter 9A] does not determine the "individual name" of a debtor. Nor does it determine which element or elements in a debtor's name constitute the surname. In some cases, determining the "individual name" of a debtor may be difficult, as may determining the debtor's surname. This is because in the case of individuals, unlike registered organizations, there is no public organic record to which reference can be made and from which the name and its components can be definitively determined.

Names can take many forms in the United States. For example, whereas a surname is often colloquially referred to as a "last name," the sequence in which the elements of a name are presented is not determinative. In some cultures, the surname appears first, while in others it may appear in a location that is neither first nor last. In addition, some surnames are composed of multiple elements that, taken together, constitute a single surname. These elements may or may not be separated by a space or connected by a hyphen, "i," or "y." In other instances, some or all of the same elements may not be part of the surname. In some cases, a debtor's entire name might be composed of only a single element, which should be provided in the part of the financing statement designated for the surname.

In disputes as to whether a financing statement sufficiently provides the "individual name" of a debtor, a court should refer to any non-UCC law concerning names. However, case law about names may have developed in contexts that implicate policies different from those of Article 9 [Title 30, chapter 9A]. A court considering an individual's name for purposes of determining the sufficiency of a financing statement is not necessarily bound by cases that were decided in other contexts and for other purposes.

Individuals are asked to provide their names on official documents such as tax returns and bankruptcy petitions. An individual may provide a particular name on an official document in response to instructions relating to the document rather than because the name is actually the individual's name. Accordingly, a court should not assume that the name an individual provides on an official document necessarily constitutes the "individual name" for purposes of the sufficiency of the debtor's name on a financing statement. Likewise, a court should not assume that the name as presented on an individual's birth certificate is necessarily the individual's current name.

In applying non-UCC law for purposes of determining the sufficiency of a debtor's name on a financing statement, a court should give effect to the instruction in Section 1-103(a)(1) [30-1-102(1)] that the UCC "must be liberally construed and applied to promote its underlying purposes and policies," which include simplifying and clarifying the law governing commercial transactions. Thus, determination of a debtor's name in the context of the Article 9 [Title 30, chapter 9A] filing system must take into account the needs of both filers and searchers. Filers need a simple and predictable system in which they can have a reasonable degree of confidence that, without undue burden, they can determine a name that will be sufficient so as to permit their financing statements to be effective. Likewise, searchers need a simple and predictable system in which they can have a reasonable degree of confidence that, without undue burden, they will discover all financing statements pertaining to the debtor in question. The court also should take into account the purpose of the UCC to make the law uniform among the various jurisdictions. See Section 1-103(a)(3) [30-1-102(1)(c)].

Of course, once an individual debtor's name has been determined to be sufficient for purposes of Section 9-503 [30-9A-503], a financing statement that provides a variation of that name, such as a "nickname" that does not constitute the debtor's name, does not sufficiently provide the name of the debtor under this section. Cf. Section 9-503(c) [30-9A-503(3)] (a financing statement providing only a debtor's trade name is not sufficient).

If there is any doubt about an individual debtor's name, a secured party may choose to file one or more financing statements that provide a number of possible names for the debtor and a searcher may similarly choose to search under a number of possible names.

Note that, even if the name provided in an initial financing statement is correct, the filing office nevertheless must reject the financing statement if it does not identify an individual debtor's surname (e.g., if it is not clear whether the debtor's surname is Perry or Mason). See Section 9-516(b)(3)(C) [30-9A-516(2)(c)(iii)].

3. **Secured Party's Name.** New subsection (d) [subsection (4)] makes clear that when the secured party is a representative, a financing statement is sufficient if it names the secured party, whether or not it indicates any representative capacity. Similarly, a financing statement that names a representative of the secured party is sufficient, even if it does not indicate the representative capacity.

Example: Debtor creates a security interest in favor of Bank X, Bank Y, and Bank Z, but not to their representative, the collateral agent (Bank A). The collateral agent is not itself a secured party. See Section 9-102 [30-9A-102]. Under Sections 9-502(a) and 9-503(d) [30-9A-502(1) and 30-9A-503(4)], however, a financing statement is effective if it names as secured party Bank A and not the actual secured parties, even if it omits Bank A's representative capacity. Each person whose name is provided in an initial financing statement as the name of the secured party or representative of the secured party is a secured party of record. See Section 9-511 [30-9A-511].

4. **Multiple Names.** Subsection (e) [subsection (5)] makes explicit what is implicit under former Article 9 [Title 30, chapter 9, now repealed]: a financing statement may provide the name of more than one debtor and secured party. See Section 1-106 [30-1-102(2)(a)] (words in the singular include the plural). With respect to records relating to more than one debtor, see Section 9-520(d) [30-9A-520(4)]. With respect to financing statements providing the name of more than one secured party, see Sections 9-509(e) and 9-510(b) [30-9A-509(5) and 30-9A-510(2)].

Compiler's Comments

2013 Amendment: Chapter 75 in (1)(a) at beginning inserted exception clause, inserted "or the collateral is held in a trust that is a registered organization", substituted "name that is stated to be the registered organization's name on the public organic record most recently filed with or issued or enacted by the registered organization's" for "name of the debtor indicated on the public record of the debtor's", and substituted "purports to state, amend, or restate the registered organization's name" for "shows the debtor to have been organized"; in (1)(b) at beginning inserted exception clause, substituted "collateral is being administered by the personal representative of a decedent" for "debtor is a decedent's estate", inserted "as the name of the debtor", substituted "in a separate part of the financing statement, indicates that the collateral is being administered by a personal representative" for "indicates that the debtor is an estate"; in (1)(c) substituted current language regarding collateral held in a trust that is not a registered organization for former language that read: "if the debtor is a trust or a trustee acting with respect to property held in trust, only if the financing statement:

(i) provides the name, if any, specified for the trust in its organic documents or, if no name is specified, provides the name of the settlor and additional information sufficient to distinguish the debtor from other trusts having one or more of the same settlors; and

(ii) indicates, in the debtor's name or otherwise, that the debtor is a trust or is a trustee acting with respect to property held in trust"; inserted (1)(d) and (1)(e) regarding driver's license, state identification card, tribal identification card, and the lack of identification; in (1)(f)(i) substituted "the financing statement" for "it" and after "provides the" deleted "individual or"; in (1)(f)(ii) after "comprising the debtor" inserted provision regarding name being sufficient if the person named were the debtor; inserted (6) and (7) regarding a court order and multiple identifications; inserted (8) providing definition; and made minor changes in style. Amendment effective July 1, 2013.

Saving Clause: Section 26, Ch. 75, L. 2013, provided: "(1) Except as otherwise provided in [sections 19 through 25] [Title 30, chapter 9A, part 8], this chapter applies to a transaction or lien within its scope, even if the transaction or lien was entered into or created before [the effective of this act] [July 1, 2013].

(2) This chapter does not affect an action, case, or proceeding commenced before [the effective date of this act] [July 1, 2013]."

Alternative A — Deviation From Uniform Act: The National Conference of Commissioners on Uniform State Laws proposed two alternative sets of amendments to the Uniform Commercial Code relating to the names of individual debtors under this section. Montana enacted "Alternative A", which affected subsections (a) and (g) [(1) and (7)]. This alternative also affected Section 9-502 [30-9A-502]. In addition to these changes, Montana chose to include state identification cards and tribal identification cards in addition to driver's licenses under this section. The Legislative Note to the section encourages states to identify other alternatives to driver's licenses issued by the same state agency but did not contemplate tribal identification cards issued by tribal authorities.

30-9A-504. Indication of collateral.

Official Comments

1. **Source.** Former Section 9-402(1) [30-9-402(1), now repealed].

2. **Indication of Collateral.** To comply with Section 9-502(a) [30-9A-502(1)], a financing statement must "indicate" the collateral it covers. This section explains what suffices for an indication.

Paragraph (1) [subsection (1)] provides that a "description" of the collateral (as the term is explained in Section 9-108 [30-9A-108]) suffices as an indication for purposes of the sufficiency of a financing statement.

Debtors sometimes create a security interest in all, or substantially all, of their assets. To accommodate this practice, paragraph (2) [subsection (2)] expands the class of sufficient collateral references to embrace "an indication that the financing statement covers all assets or all personal property." If the property in question belongs to the debtor and is personal property, any searcher will know that the property is covered by the financing statement. Of course, regardless of its breadth, a financing statement has no effect with respect to property indicated but to which a security interest has not attached. Note that a broad statement of this kind (e.g., "all debtor's personal property") would not be a sufficient "description" for purposes of a security agreement. See Sections 9-203(b)(3)(A), 9-108 [30-9A-203(2)(c)(i) and 30-9A-108]. It follows that a somewhat narrower description than "all assets," e.g., "all assets other than automobiles," is sufficient for purposes of this section, even if it does not suffice for purposes of a security agreement.

30-9A-505. Filing and compliance with other statutes and treaties for consignments, leases, bailments, and other transactions.

Official Comments

1. **Source.** Former Section 9-408 [now repealed].

2. **Precautionary Filing.** Occasionally, doubts arise concerning whether a transaction creates a relationship to which this Article [Title 30, chapter 9A] or its filing provisions apply. For example, questions may arise over whether a "lease" of equipment in fact creates a security interest or whether the "sale" of payment intangibles in fact secures an obligation, thereby requiring action to perfect the security interest. This section, which derives from former Section 9-408 [now repealed], affords the option of filing of a financing statement with appropriate changes of terminology but without affecting the substantive question of classification of the transaction.

3. **Changes from Former Section 9-408 [now repealed].** This section expands the rule of former Section 9-408 [30-9A-408] to embrace more generally other bailments and transactions, as well as sales transactions, primarily sales of payment intangibles and promissory notes. It provides the same benefits for compliance with a statute or treaty described in Section 9-311(a) [30-9A-311(1)] that former Section 9-408 [now repealed] provided for filing, in connection with the use of terms such as "lessor," "consignor," etc. The references to "owner" and "registered owner"

are intended to address, for example, the situation where a putative lessor is the registered owner of an automobile covered by a certificate of title and the transaction is determined to create a security interest. Although this section provides that the security interest is perfected, the relevant certificate-of-title statute may expressly provide to the contrary or may be ambiguous. If so, it may be necessary or advisable to amend the certificate-of-title statute to ensure that perfection of the security interest will be achieved.

As did former Section 1-201 [30-1-201], former Article 9 [Title 30, chapter 9, now repealed] referred to transactions, including leases and consignments, "intended as security." This misleading phrase created the erroneous impression that the parties to a transaction can dictate how the law will classify it (e.g., as a bailment or as a security interest) and thus affect the rights of third parties. This Article [Title 30, chapter 9A] deletes the phrase wherever it appears. Subsection (b) [subsection (2)] expresses the principle more precisely by referring to a security interest that "secures an obligation."

4. **Consignments.** Although a "true" consignment is a bailment, the filing and priority provisions of former Article 9 [Title 30, chapter 9, now repealed] applied to "true" consignments. See former Sections 2-326(3), 9-114 [30-2-326(3), 30-9-114, now repealed]. A consignment "intended as security" created a security interest that was in all respects subject to former Article 9 [Title 30, chapter 9, now repealed]. This Article [Title 30, chapter 9A] subsumes most true consignments under the rubric of "security interest." See Sections 9-102 [30-9A-102] (definition of "consignment"), 9-109(a)(4) [30-9A-109(1)(d)], 1-201(b)(35) [30-1-201(2)(jj)] (definition of "security interest"). Nevertheless, it maintains the distinction between a (true) "consignment," as to which only certain aspects of Article 9 [Title 30, chapter 9A] apply, and a so-called consignment that actually "secures an obligation," to which Article 9 [Title 30, chapter 9A] applies in full. The revisions to this section reflect the change in terminology.

30-9A-506. Effect of errors or omissions.

Official Comments

1. **Source.** Former Section 9-402(8) [30-9-402(8), now repealed].

2. **Errors.** Like former Section 9-402(8) [30-9-402(8), now repealed], subsection (a) [subsection (1)] is in line with the policy of this Article [Title 30, chapter 9A] to simplify formal requisites and filing requirements. It is designed to discourage the fanatical and impossibly refined reading of statutory requirements in which courts occasionally have indulged themselves. Subsection (a) [subsection (1)] provides the standard applicable to indications of collateral. Subsections (b) and (c) [subsections (2) and (3)], which are new, concern the effectiveness of financing statements in which the debtor's name is incorrect. Subsection (b) [subsection (2)] contains the general rule: a financing statement that fails sufficiently to provide the debtor's name in accordance with Section 9-503(a) [30-9A-503(1)] is seriously misleading as a matter of law. Subsection (c) [subsection (3)] provides an exception: If the financing statement nevertheless would be discovered in a search under the debtor's correct name, using the filing office's standard search logic, if any, then as a matter of law the incorrect name does not make the financing statement seriously misleading. A financing statement that is seriously misleading under this section is ineffective even if it is disclosed by (i) using a search logic other than that of the filing office to search the official records, or (ii) using the filing office's standard search logic to search a data base other than that of the filing office. For purposes of subsection (c) [subsection (3)], any name that satisfies Section 9-503(a) [30-9A-503(1)] at the time of the search is a "correct name."

This section and Section 9-503 [30-9A-503] balance the interests of filers and searchers. Searchers are not expected to ascertain nicknames, trade names, and the like by which the debtor may be known and then search under each of them. Rather, it is the secured party's responsibility to provide the name of the debtor sufficiently in a filed financing statement. Subsection (c) [subsection (3)] sets forth the only situation in which a financing statement that fails sufficiently to provide the name of the debtor is not seriously misleading. As stated in subsection (b) [subsection (2)], if the name of the debtor provided on a financing statement is insufficient and subsection (c) [subsection (3)] is not satisfied, the financing statement is seriously misleading. Such a financing statement is ineffective even if the debtor is known in some contexts by the name provided on the financing statement and even if searchers know or have reason to know that the name provided on the financing statement refers to the debtor. Any suggestion to the contrary in a judicial opinion is incorrect.

To satisfy the requirements of Section 9-503(a)(2) [30-9A-503(1)(b)], a financing statement must indicate that the collateral is being administered by a personal representative. To satisfy the requirements of Section 9-503(a)(3) [30-9A-503(1)(c)], a financing statement must indicate that the collateral is held in a trust and provide additional information that distinguishes the trust from certain other trusts. The indications and additional information are not part of the debtor's name. Nevertheless, a financing statement that fails to provide an indication or the additional information when required does not sufficiently provide the name of the debtor under Sections 9-502(a) [30-9A-502(1)] and 9-503(a) [30-9A-503(1)], does not "substantially satisfy[ ] the requirements" of Part 5 within the meaning of this section and so is ineffective.

In addition to requiring the debtor's name and an indication of the collateral, Section 9-502(a) [30-9A-502(1)] requires a financing statement to provide the name of the secured party or a representative of the secured party. Inasmuch as searches are not conducted under the secured party's name, and no filing is needed to continue the perfected status of security interest after it is assigned, an error in the name of the secured party or its representative will not be seriously misleading. However, in an appropriate case, an error of this kind may give rise to an estoppel in favor of a particular holder of a conflicting claim to the collateral. See Section 1-103 [30-1-103].

3. **New Debtors.** Subsection (d) [subsection (4)] provides that, in determining the extent to which a financing statement naming an original debtor is effective against a new debtor, the sufficiency of the financing statement should be tested against the name of the new debtor.

30-9A-507. Effect of certain events on effectiveness of financing statement.

Official Comments

1. **Source.** Former Section 9-402(7) [30-9-402(7), now repealed].

2. **Scope of Section.** This section deals with situations in which the information in a proper financing statement becomes inaccurate after the financing statement is filed. Compare Section 9-338 [30-9A-338], which deals with situations in which a financing statement contains a particular kind of information concerning the debtor (i.e., the information described in Section 9-516(b)(5) [30-9A-516(2)(e)]) that is incorrect at the time it is filed.

3. **Post-Filing Disposition of Collateral.** Under subsection (a) [subsection (1)], a financing statement remains effective even if the collateral is sold or otherwise disposed of. This subsection clarifies the third sentence of former Section 9-402(7) [30-9-402(7), now repealed] by providing that a financing statement remains effective following the disposition of collateral only when the security interest or agricultural lien continues in that collateral. This result is consistent with the conclusion of PEB Commentary No. 3. Normally, a security interest does continue after disposition of the collateral. See Section 9-315(a) [30-9A-315(1)]. Law other than this Article [Title 30, chapter 9A] determines whether an agricultural lien survives disposition of the collateral.

As a consequence of the disposition, the collateral may be owned by a person other than the debtor against whom the financing statement was filed. Under subsection (a) [subsection (1)], the secured party remains perfected even if it does not correct the public record. For this reason, any person seeking to determine whether a debtor owns collateral free of security interests must inquire as to the debtor's source of title and, if circumstances seem to require it, search in the name of a former owner. Subsection (a) [subsection (1)] addresses only the sufficiency of the information contained in the financing statement. A disposition of collateral may result in loss of perfection for other reasons. See Section 9-316 [30-9A-316].

Example: Dee Corp. is an Illinois corporation. It creates a security interest in its equipment in favor of Secured Party. Secured Party files a proper financing statement in Illinois. Dee Corp. sells an item of equipment to Bee Corp., a Pennsylvania corporation, subject to the security interest. The security interest continues, see Section 9-315(a) [30-9A-315(1)], and remains perfected, see Section 9-507(a) [30-9A-507(1)], notwithstanding that the financing statement is filed under "D" (for Dee Corp.) and not under "B." However, because Bee Corp. is located in Pennsylvania and not Illinois, see Section 9-307 [30-9A-307], unless Secured Party perfects under Pennsylvania law within one year after the transfer, its security interest will become unperfected and will be deemed to have been unperfected against purchasers of the collateral. See Section 9-316 [30-9A-316].

4. **Other Post-Filing Changes.** Subsection (b) [subsection (2)] provides that, as a general matter, post-filing changes that render a financing statement inaccurate and seriously misleading have no effect on a financing statement. The financing statement remains effective. It is subject to two exceptions: Section 9-508 [30-9A-508] and Section 9-507(c) [30-9A-507(3)]. Section 9-508 [30-9A-508] addresses the effectiveness of a financing statement filed against an original debtor when a new debtor becomes bound by the original debtor's security agreement. It is discussed in the Comments to that section. Section 9-507(c) [30-9A-507(3)] addresses cases in which a filed financing statement provides a name that, at the time of filing, satisfies the requirements of

Section 9-503(a) [30-9A-503(1)] with respect to the named debtor but, at a later time, no longer does so.

Example 1: Debtor, an individual whose principal residence is in California, grants a security interest to SP in certain business equipment. SP files a financing statement with the California filing office. Alternative A is in effect in California. The financing statement provides the name appearing on Debtor's California driver's license, "James McGinty." Debtor obtains a court order changing his name to "Roger McGuinn" but does not change his driver's license. Even after the court order issues, the name provided for the debtor in the financing statement is sufficient under Section 9-503(a) [30-9A-503(1)]. Accordingly, Section 9-507(c) [30-9A-507(3)] does not apply.

The same result would follow if Alternative B is in effect in California.

Under Section 9-503(a)(4) [30-9A-503(1)(d)] (Alternative A), if the debtor holds a current (i.e., unexpired) driver's license issued by the State where the financing statement is filed, the name required for the financing statement is the name indicated on the license that was issued most recently by that State. If the debtor does not have a current driver's license issued by that State, then the debtor's name is determined under subsection (a)(5) [subsection (1)(e)]. It follows that a debtor's name may change, and a financing statement providing the name on the debtor's then-current driver's license may become seriously misleading, if the license expires and the debtor's name under subsection (a)(5) [subsection (1)(e)] is different. The same consequences may follow if a debtor's driver's license is renewed and the names on the licenses differ.

Example 2: The facts are as in Example 1. Debtor's driver's license expires one year after the entry of the court order changing Debtor's name. Debtor does not renew the license. Upon expiration of the license, the name required for sufficiency by Section 9-503(a) [30-9A-503(1)] is the individual name of the debtor or the debtor's surname and first personal name. The name "James McGinty" has become insufficient.

Example 3: The facts are as in Example 1. Before the license expires, Debtor renews the license. The name indicated on the new license is "Roger McGuinn." Upon issuance of the new license, "James McGinty" becomes insufficient as the debtor's name under Section 9-503(a) [30-9A-503(1)].

The same results would follow if Alternative B is in effect in California (assuming that, following the issuance of the court order, "James McGinty" is neither the individual name of the debtor nor the debtor's surname and first personal name).

Even if the name provided as the name of the debtor becomes insufficient under Section 9-503(a) [30-9A-503(1)], the filed financing statement does not become seriously misleading, and Section 9-507(c) [30-9A-507(3)] does not apply, if the financing statement can be found by searching under the debtor's "correct" name, using the filing office's standard search logic. See Section 9-506 [30-9A-506]. Any name that satisfies Section 9-503(a) [30-9A-503(1)] at the time of the search is a "correct name" for these purposes. Thus, assuming that a search of the records of the California filing office under "Roger McGuinn," using the filing office's standard search logic, would not disclose a financing statement naming "James McGinty," the financing statement in Examples 2 and 3 has become seriously misleading and Section 9-507(c) [30-9A-507(3)] applies.

If a filed financing statement becomes seriously misleading because the name it provides for a debtor becomes insufficient, the financing statement, unless amended to provide a sufficient name for the debtor, is effective only to perfect a security interest in collateral acquired by the debtor before, or within four months after, the change. If an amendment that provides a sufficient name is filed within four months after the change, the financing statement as amended would be effective also with respect to collateral acquired more than four months after the change. If an amendment that provides the new correct a sufficient name is filed more than four months after the change, the financing statement as amended would be effective also with respect to collateral acquired more than four months after the change, but only from the time of the filing of the amendment.

Compiler's Comments

2013 Amendment: Chapter 75 in (3) substituted "If the name" for "If a debtor so changes its name", inserted "provides for a debtor", and inserted "insufficient as the name of the debtor under 30-9A-503(1) so that the financing statement becomes"; in (3)(a) and (3)(b) substituted "filed financing statement becomes seriously misleading" for "change"; in (3)(b) at end substituted "financing statement became seriously misleading" for "change"; and made minor changes in style. Amendment effective July 1, 2013.

Saving Clause: Section 26, Ch. 75, L. 2013, provided: "(1) Except as otherwise provided in [sections 19 through 25] [Title 30, chapter 9A, part 8], this chapter applies to a transaction or lien within its scope, even if the transaction or lien was entered into or created before [the effective of this act] [July 1, 2013].

(2) This chapter does not affect an action, case, or proceeding commenced before [the effective date of this act] [July 1, 2013]."

30-9A-508. Effectiveness of financing statement if new debtor becomes bound by security agreement.

Official Comments

1. **Source.** New.

2. **The Problem.** Section 9-203(d) and (e) [30-9A-203(4) and (5)] and this section deal with situations where one party (the "new debtor") becomes bound as debtor by a security agreement entered into by another person (the "original debtor"). These situations often arise as a consequence of changes in business structure. For example, the original debtor may be an individual debtor who operates a business as a sole proprietorship and then incorporates it. Or, the original debtor may be a corporation that is merged into another corporation. Under both former Article 9 [Title 30, chapter 9, now repealed] and this Article [Title 30, chapter 9A], collateral that is transferred in the course of the incorporation or merger normally would remain subject to a perfected security interest. See Sections 9-315(a), 9-507(a) [30-9A-315(1) and 30-9A-507(1)]. Former Article 9 [Title 30, chapter 9, now repealed] was less clear with respect to whether an after-acquired property clause in a security agreement signed by the original debtor would be effective to create a security interest in property acquired by the new corporation or the merger survivor and, if so, whether a financing statement filed against the original debtor would be effective to perfect the security interest. This section and Sections 9-203(d) and (e) [30-9A-203(4) and (5)] are a clarification.

3. **How New Debtor Becomes Bound.** Normally, a security interest is unenforceable unless the debtor has authenticated a security agreement describing the collateral. See Section 9-203(b) [30-9A-203(2)]. New Section 9-203(e) [30-9A-203(5)] creates an exception, under which a security agreement entered into by one person is effective with respect to the property of another. This exception comes into play if a "new debtor" becomes bound as debtor by a security agreement entered into by another person (the "original debtor"). (The quoted terms are defined in Section 9-102 [30-9A-102].) If a new debtor does become bound, then the security agreement entered into by the original debtor satisfies the security-agreement requirement of Section 9-203(b)(3) [30-9A-203(2)(c)] as to existing or after-acquired property of the new debtor to the extent the property is described in the security agreement. In that case, no other agreement is necessary to make a security interest enforceable in that property. See Section 9-203(e) [30-9A-203(5)].

Section 9-203(d) [30-9A-203(4)] explains when a new debtor becomes bound by an original debtor's security agreement. Under Section 9-203(d)(1) [30-9A-203(4)(a)], a new debtor becomes bound as debtor if, by contract or operation of other law, the security agreement becomes effective to create a security interest in the new debtor's property. For example, if the applicable corporate law of mergers provides that when A Corp merges into B Corp, B Corp becomes a debtor under A Corp's security agreement, then B Corp would become bound as debtor following such a merger. Similarly, B Corp would become bound as debtor if B Corp contractually assumes A's obligations under the security agreement.

Under certain circumstances, a new debtor becomes bound for purposes of this Article [Title 30, chapter 9A] even though it would not be bound under other law. Under Section 9-203(d)(2) [30-9A-203(4)(b)], a new debtor becomes bound when, by contract or operation of other law, it (i) becomes obligated not only for the secured obligation but also generally for the obligations of the original debtor and (ii) acquires or succeeds to substantially all the assets of the original debtor. For example, some corporate laws provide that, when two corporations merge, the surviving corporation succeeds to the assets of its merger partner and "has all liabilities" of both corporations. In the case where, for example, A Corp merges into B Corp (and A Corp ceases to exist), some people have questioned whether A Corp's grant of a security interest in its existing and after-acquired property becomes a "liability" of B Corp, such that B Corp's existing and after-acquired property becomes subject to a security interest in favor of A Corp's lender. Even if corporate law were to give a negative answer, under Section 9-203(d)(2) [30-9A-203(4)(b)], B Corp would become bound for purposes of Section 9-203(e) [30-9A-203(5)] and this section. The "substantially all of the assets" requirement of Section 9-203(d)(2) [30-9A-203(4)(b)] excludes sureties and other secondary obligors as well as persons who become obligated through veil piercing and other non-successorship doctrines. In most cases, it will exclude successors to the assets and liabilities of a division of a debtor.

4. **When Financing Statement Effective Against New Debtor.** Subsection (a) [subsection (1)] provides that a filing against the original debtor is effective to perfect a security interest in collateral that a new debtor has at the time it becomes bound by the original debtor's security agreement and collateral that it acquires before the expiration of four months after the new debtor becomes bound. Under subsection (b) [subsection (2)], however, if the filing against the original debtor is seriously misleading as to the new debtor's name, the filing is effective as to collateral acquired by the new debtor after the four-month period only if a person files during the four-month period an initial financing statement providing the name of the new debtor. Compare Section 9-507(c) [30-9A-507(3)] (four-month period of effectiveness with respect to collateral acquired by a debtor after the name provided for the debtor becomes insufficient as the name of the debtor). As to the meaning of "initial financing statement" in this context, see Section 9-512 [30-9A-512], Comment 5.

5. **Transferred Collateral.** This section does not apply to collateral transferred by the original debtor to a new debtor. Under those circumstances, the filing against the original debtor continues to be effective until it lapses. See subsection (c) [subsection (3)]; Section 9-507(a) [30-9A-507(1)].

6. **Priority.** Section 9-326 [30-9A-326] governs the priority contest between a secured creditor of the original debtor and a secured creditor of the new debtor.

30-9A-509. Persons entitled to file record.

Official Comments

1. **Source.** New.

2. **Scope and Approach of This Section.** This section collects in one place most of the rules determining whether a record may be filed. Section 9-510 [30-9A-510] explains the extent to which a filed record is effective. Under these sections, the identity of the person who effects a filing is immaterial. The filing scheme contemplated by this Part [Title 30, chapter 9A, part 5] does not contemplate that the identity of a "filer" will be a part of the searchable records. This is consistent with, and a necessary aspect of, eliminating signatures or other evidence of authorization from the system. (Note that the 1972 amendments to this Article [Title 30, chapter 9A] eliminated the requirement that a financing statement contain the signature of the secured party.) As long as the appropriate person authorizes the filing, or, in the case of a termination statement, the debtor is entitled to the termination, it is insignificant whether the secured party or another person files any given record. The question of authorization is one for the court, not the filing office. However, a filing office may choose to employ authentication procedures in connection with electronic communications, e.g., to verify the identity of a filer who seeks to charge the filing fee.

3. **Unauthorized Filings.** Records filed in the filing office do not require signatures for their effectiveness. Subsection (a)(1) [subsection (1)(a)] substitutes for the debtor's signature on a financing statement the requirement that the debtor authorize in an authenticated record the filing of an initial financing statement or an amendment that adds collateral. Also, under subsection (a)(1) [subsection (1)(a)], if an amendment adds a debtor, the debtor who is added must authorize the amendment. A person who files an unauthorized record in violation of subsection (a)(1) [subsection (1)(a)] is liable under Section 9-625 [30-9A-625] for actual and statutory damages. Of course, a filed financing statement is ineffective to perfect a security interest if the filing is not authorized. See Section 9-510(a) [30-9A-510(1)]. Law other than this Article [Title 30, chapter 9A], including the law with respect to ratification of past acts, generally determines whether a person has the requisite authority to file a record under this section. See Sections 1-103, 9-502 [30-1-103, 30-9A-502], Comment 3. This Article applies to other issues, such as the priority of a security interest perfected by the filing of a financing statement. See Section 9-322 [30-9A-322], Comment 4.

4. **Ipso Facto Authorization.** Under subsection (b) [subsection (2)], the authentication of a security agreement ipso facto constitutes the debtor's authorization of the filing of a financing statement covering the collateral described in the security agreement. The secured party need not obtain a separate authorization. Similarly, a new debtor's becoming bound by a security agreement ipso facto constitutes the new debtor's authorization of the filing of a financing statement covering the collateral described in the security agreement by which the new debtor has become bound. And, under subsection (c) [not adopted in Montana], the acquisition of collateral in which a security interest continues after disposition under Section 9-315(a)(1) [30-9A-315(1)(a)] ipso facto constitutes an authorization to file an initial financing statement against the person who acquired the collateral. The authorization to file an initial financing statement also constitutes

an authorization to file a record covering actual proceeds of the original collateral, even if the security agreement is silent as to proceeds.

Example 1: Debtor authenticates a security agreement creating a security interest in Debtor's inventory in favor of Secured Party. Secured Party files a financing statement covering inventory and accounts. The financing statement is authorized insofar as it covers inventory and unauthorized insofar as it covers accounts. (Note, however, that the financing statement will be effective to perfect a security interest in accounts constituting proceeds of the inventory to the same extent as a financing statement covering only inventory.)

Example 2: Debtor authenticates a security agreement creating a security interest in Debtor's inventory in favor of Secured Party. Secured Party files a financing statement covering inventory. Debtor sells some inventory, deposits the buyer's payment into a deposit account, and withdraws the funds to purchase equipment. As long as the equipment can be traced to the inventory, the security interest continues in the equipment. See Section 9-315(a)(2) [30-9A-315(1)(b)]. However, because the equipment was acquired with cash proceeds, the financing statement becomes ineffective to perfect the security interest in the equipment on the 21st day after the security interest attaches to the equipment unless Secured Party continues perfection beyond the 20-day period by filing a financing statement against the equipment or amending the filed financing statement to cover equipment. See Section 9-315(d) [30-9A-315(4)]. Debtor's authentication of the security agreement authorizes the filing of an initial financing statement or amendment covering the equipment, which is "property that becomes collateral under Section 9-315(a)(2) [30-9A-315(1)(b)]." See Section 9-509(b)(2) [30-9A-509(2)(b)].

5. **Agricultural Liens.** Under subsection (a)(2) [subsection (1)(b)], the holder of an agricultural lien may file a financing statement covering collateral subject to the lien without obtaining the debtor's authorization. Because the lien arises as matter of law, the debtor's consent is not required. A person who files an unauthorized record in violation of this subsection is liable under Section 9-625(e) [30-9A-625(5)] for a statutory penalty and damages.

6. **Amendments; Termination Statements Authorized by Debtor.** Most amendments may not be filed unless the secured party of record, as determined under Section 9-511 [30-9A-511], authorizes the filing. See subsection (d)(1) [subsection (3)(a)]. However, under subsection (d)(2) [subsection (3)(b)], the authorization of the secured party of record is not required for the filing of a termination statement if the secured party of record failed to send or file a termination statement as required by Section 9-513 [30-9A-513], the debtor authorizes it to be filed, and the termination statement so indicates. An authorization to file a record under subsection (d) [subsection (4)] is effective even if the authorization is not in an authenticated record. Compare subsection (a)(1) [subsection (1)(a)]. However, both the person filing the record and the person giving the authorization may wish to obtain and retain a record indicating that the filing was authorized.

7. **Multiple Secured Parties of Record.** Subsection (e) [subsection (4)] deals with multiple secured parties of record. It permits each secured party of record to authorize the filing of amendments. However, Section 9-510(b) [30-9A-510(2)] protects the rights and powers of one secured party of record from the effects of filings made by another secured party of record. See Section 9-510 [30-9A-510], Comment 3.

8. **Successor to Secured Party of Record.** A person may succeed to the powers of the secured party of record by operation of other law, e.g., the law of corporate mergers. In that case, the successor has the power to authorize filings within the meaning of this section.

Compiler's Comments

2001 Amendment: Chapter 179 at end of (1)(a) inserted "or pursuant to subsection (2) or (3)". Amendment effective July 1, 2001.

30-9A-510. Effectiveness of filed record.

Official Comments

1. **Source.** New.

2. **Ineffectiveness of Unauthorized or Overbroad Filings.** Subsection (a) [subsection (1)] provides that a filed financing statement is effective only to the extent it was filed by a person entitled to file it.

Example 1: Debtor authorizes the filing of a financing statement covering inventory. Under Section 9-509 [30-9A-509], the secured party may file a financing statement covering only inventory; it may not file a financing statement covering other collateral. The secured party files a financing statement covering inventory and equipment. This section provides that the financing statement is effective only to the extent the secured party may file it. Thus, the financing statement is effective to perfect a security interest in inventory but ineffective to perfect a security interest in equipment.

3. **Multiple Secured Parties of Record.** Section 9-509(e) [30-9A-509(4)] permits any secured party of record to authorize the filing of most amendments. Subsection (b) [subsection (2)] of this section prevents a filing authorized by one secured party of record from affecting the rights and powers of another secured party of record without the latter's consent.

Example 2: Debtor creates a security interest in favor of A and B. The filed financing statement names A and B as the secured parties. An amendment deleting some collateral covered by the financing statement is filed pursuant to B's authorization. Although B's security interest in the deleted collateral becomes unperfected, A's security interest remains perfected in all the collateral.

Example 3: Debtor creates a security interest in favor of A and B. The financing statement names A and B as the secured parties. A termination statement is filed pursuant to B's authorization. Although the effectiveness of the financing statement terminates with respect to B's security interest, A's rights are unaffected. That is, the financing statement continues to be effective to perfect A's security interest.

4. **Continuation Statements.** A continuation statement may be filed only within the six months immediately before lapse. See Section 9-515(d) [30-9A-515(4)]. The filing office is obligated to reject a continuation statement that is filed outside the six-month period. See Sections 9-520(a), 9-516(b)(7) [30-9A-520(1) and 30-9A-516(2)(g)]. Subsection (c) [subsection (3)] provides that if the filing office fails to reject a continuation statement that is not filed in a timely manner, the continuation statement is ineffective nevertheless.

30-9A-511. Secured party of record.

Official Comments

1. **Source.** New.

2. **Secured Party of Record.** This new section explains how the secured party of record is to be determined. If SP-1 is named as the secured party in an initial financing statement, it is the secured party of record. Similarly, if an initial financing statement reflects a total assignment from SP-0 to SP-1, then SP-1 is the secured party of record. See subsection (a) [subsection (1)]. If, subsequently, an amendment is filed assigning SP-1's status to SP-2, then SP-2 becomes the secured party of record in place of SP-1. The same result obtains if a subsequent amendment deletes the reference to SP-1 and substitutes therefor a reference to SP-2. If, however, a subsequent amendment adds SP-2 as a secured party but does not purport to remove SP-1 as a secured party, then SP-2 and SP-1 each is a secured party of record. See subsection (b) [subsection (2)]. An amendment purporting to remove the only secured party of record without providing a successor is ineffective. See Section 9-512(e) [30-9A-512(5)]. At any point in time, all effective records that comprise a financing statement must be examined to determine the person or persons that have the status of secured party of record.

3. **Successor to Secured Party of Record.** Application of other law may result in a person succeeding to the powers of a secured party of record. For example, if the secured party of record (A) merges into another corporation (B) and the other corporation (B) survives, other law may provide that B has all of A's powers. In that case, B is authorized to take all actions under this Part that A would have been authorized to take. Similarly, acts taken by a person who is authorized under generally applicable principles of agency to act on behalf of the secured party of record are effective under this Part [Title 30, chapter 9A, part 5].

30-9A-512. Amendment of financing statement.

Official Comments

1. **Source.** Former 9-402(4) [30-9-402(4), now repealed].

2. **Changes to Financing Statements.** This section addresses changes to financing statements, including addition and deletion of collateral. Although termination statements, assignments, and continuation statements are types of amendment, this Article [Title 30, chapter 9A] follows former Article 9 [Title 30, chapter 9, now repealed] and contains separate sections containing additional provisions applicable to particular types of amendments. See Section 9-513 [30-9A-513] (termination statements); 9-514 [30-9A-514] (assignments); 9-515 [30-9A-515] (continuation statements). One should not infer from this separate treatment that this Article [Title 30, chapter 9A] requires a separate amendment to accomplish each change. Rather, a single amendment would be legally sufficient to, e.g., add collateral and continue the effectiveness of the financing statement.

3. **Amendments.** An amendment under this Article [Title 30, chapter 9A] may identify only the information contained in a financing statement that is to be changed; alternatively, it may take the form of an amended and restated financing statement. The latter would state, for example, that the financing statement "is amended and restated to read as follows: . . ." References in this Part [Title 30, chapter 9A, part 5] to an "amended financing statement" are to a financing statement as amended by an amendment using either technique.

This section revises former Section 9-402(4) [30-9-402(4), now repealed] to permit secured parties of record to make changes in the public record without the need to obtain the debtor's signature. However, the filing of an amendment that adds collateral or adds a debtor must be authorized by the debtor or it will not be effective. See Sections 9-509(a), 9-510(a) [30-9A-509(1), 30-9A-510(1)].

4. **Amendment Adding Debtor.** An amendment that adds a debtor is effective, provided that the added debtor authorizes the filing. See Section 9-509(a) [30-9A-509(1)]. However, filing an amendment adding a debtor to a previously filed financing statement affords no advantage over filing an initial financing statement against that debtor and may be disadvantageous. With respect to the added debtor, for purposes of determining the priority of the security interest, the time of filing is the time of the filing of the amendment, not the time of the filing of the initial financing statement. See subsection (d) [subsection (4)]. However, the effectiveness of the financing statement lapses with respect to added debtor at the time it lapses with respect to the original debtor. See subsection (b) [subsection (2)].

5. **Amendment Adding Debtor Name.** Many states have enacted statutes governing the "conversion" of one organization organized under the law of that state, e.g., a corporation, into another such organization, e.g., a limited liability company. This Article [Title 30, chapter 9A] defers to those statutes to determine whether the resulting organization is the same legal person as the initial, converting organization (albeit with a different name) or whether the resulting organization is a different legal person. When the governing statute does not clearly resolve the question, a secured party whose debtor is the converting organization may wish to proceed as if the statute provides for both results. In these circumstances, an amendment adding to the initial financing statement the name of the resulting organization may be preferable to an amendment substituting that name for the name of the debtor provided on the initial financing statement. In the event the governing statute is construed as providing that the resulting organization is the same legal person as the converting organization, but with a different name, the timely filing of such an amendment would satisfy the requirement of Section 9-507(c)(2) [30-9A-507(3)(b)]. If, however, the governing statute is construed as providing that the resulting organization is a different legal person, the financing statement (which continues to provide the name of the original debtor) would be effective as to collateral acquired by the resulting organization ("new debtor") before, and within four months after, the conversion. See Section 9-508(b)(1) [30-9A-508(2)(a)]. Inasmuch as it is the first financing statement filed against the resulting organization by the secured party, the record adding the name of the resulting organization as a debtor would constitute "an initial financing statement providing the name of the new debtor " under Section 9-508(b)(2) [30-9-A-508(2)(b)]. The secured party also may wish to file another financing statement naming the resulting organization as debtor. See Comment 4.

6. **Deletion of All Debtors or Secured Parties of Record.** Subsection (e) [subsection (5)] assures that there will be a debtor and secured party of record for every financing statement.

Example: A filed financing statement names A and B as secured parties of record and covers inventory and equipment. An amendment deletes equipment and purports to delete A and B as secured parties of record without adding a substitute secured party. The amendment is ineffective to the extent it purports to delete the secured parties of record but effective with respect to the deletion of collateral. As a consequence, the financing statement, as amended, covers only inventory, but A and B remain as secured parties of record.

30-9A-513. Termination statement.

Official Comments

1. **Source.** Former Section 9-404 [30-9-404, now repealed].

2. **Duty to File or Send.** This section specifies when a secured party must cause the secured party of record to file or send to the debtor a termination statement for a financing statement. Because most financing statements expire in five years unless a continuation statement is filed (Section 9-515 [30-9A-515]), no compulsion is placed on the secured party to file a termination statement unless demanded by the debtor, except in the case of consumer goods. Because many consumers will not realize the importance to them of clearing the public record, an affirmative

duty is put on the secured party in that case. But many purchase-money security interests in consumer goods will not be filed, except for motor vehicles. See Section 9-309(1) [30-9A-309(1)]. Under Section 9-311(b) [30-9A-311(2)], compliance with a certificate-of-title statute is "equivalent to the filing of a financing statement under this article." Thus, this section applies to a certificate of title unless the section is superseded by a certificate-of-title statute that contains a specific rule addressing a secured party's duty to cause a notation of a security interest to be removed from a certificate of title. In the context of a certificate of title, however, the secured party could comply with this section by causing the removal itself or providing the debtor with documentation sufficient to enable the debtor to effect the removal.

Subsections (a) and (b) [subsections (1) and (2)] apply to a financing statement covering consumer goods. Subsection (c) [subsection (3)] applies to other financing statements. Subsection (a) and (c) [subsections (1) and (3)] each makes explicit what was implicit under former Article 9 [Title 30, chapter 9, now repealed]: If the debtor did not authorize the filing of a financing statement in the first place, the secured party of record should file or send a termination statement. The liability imposed upon a secured party that fails to comply with subsection (a) or (c) [subsections (1) or (3)] is identical to that imposed for the filing of an unauthorized financing statement or amendment. See Section 9-625(e) [30-9A-625(5)].

3. **"Bogus" Filings.** A secured party's duty to send a termination statement arises when the secured party "receives" an authenticated demand from the debtor. In the case of an unauthorized financing statement, the person named as debtor in the financing statement may have no relationship with the named secured party and no reason to know the secured party's address. Inasmuch as the address in the financing statement is "held out by [the person named as secured party in the financing statement] as the place for receipt of such communications [i.e., communications relating to security interests]," the putative secured party is deemed to have "received" a notification delivered to that address. See Section 1-202(e) [30-1-210(5)]. If a termination statement is not forthcoming, the person named as debtor itself may authorize the filing of a termination statement, which will be effective if it indicates that the person authorized it to be filed. See Sections 9-509(d)(2), 9-510(c) [30-9A-509(3)(b), 30-9A-510(3)].

4. **Buyers of Receivables.** Applied literally, former Section 9-404(1) [30-9-404(1), now repealed] would have required many buyers of receivables to file a termination statement immediately upon filing a financing statement because "there is no outstanding secured obligation and no commitment to make advances, incur obligations, or otherwise give value." Subsections (c)(1) and (2) [subsections (3)(a) and (3)(b)] remedy this problem. While the security interest of a buyer of accounts or chattel paper (B-1) is perfected, the debtor is not deemed to retain an interest in the sold receivables and thus could transfer no interest in them to another buyer (B-2) or to a lien creditor (LC). However, for purposes of determining the rights of the debtor's creditors and certain purchasers of accounts or chattel paper from the debtor, while B-1's security interest is unperfected, the debtor-seller is deemed to have rights in the sold receivables, and a competing security interest or judicial lien may attach to those rights. See Sections 9-318, 9-109 [30-9A-318 and 30-9A-109], Comment 5. Suppose that B-1's security interest in certain accounts and chattel paper is perfected by filing, but the effectiveness of the financing statement lapses. Both before and after lapse, B-1 collects some of the receivables. After lapse, LC acquires a lien on the accounts and chattel paper. B-1's unperfected security interest in the accounts and chattel paper is subordinate to LC's rights. See Section 9-317(a)(2) [30-9A-317(1)(b)]. But collections on accounts and chattel paper are not "accounts" or "chattel paper." Even if B-1's security interest in the accounts and chattel paper is or becomes unperfected, neither the debtor nor LC acquires rights to the collections that B-1 collects (and owns) before LC acquires a lien.

5. **Effect of Filing.** Subsection (d) [subsection (4)] states the effect of filing a termination statement: the related financing statement ceases to be effective. If one of several secured parties of record files a termination statement, subsection (d) [subsection (4)] applies only with respect to the rights of the person who authorized the filing of the termination statement. See Section 9-510(b) [30-9A-510(2)]. The financing statement remains effective with respect to the rights of the others. However, even if a financing statement is terminated (and thus no longer is effective) with respect to all secured parties of record, the financing statement, including the termination statement, will remain of record until at least one year after it lapses with respect to all secured parties of record. See Section 9-519(g) [30-9A-519(7)].

Compiler's Comments

2001 Amendment: Chapter 179 in (4) inserted second sentence concerning lapse in effectiveness for debtor who is a transmitting utility. Amendment effective July 1, 2001.

30-9A-514. Assignment powers of secured party of record.

Official Comments

1. **Source.** Former Section 9-405 [30-9-405, now repealed].

2. **Assignments.** This section provides a permissive device whereby a secured party of record may effectuate an assignment of its power to affect a financing statement. It may also be useful for a secured party who has assigned all or part of its security interest or agricultural lien and wishes to have the fact noted of record, so that inquiries concerning the transaction would be addressed to the assignee. See Section 9-502 [30-9A-502], Comment 2. Upon the filing of an assignment, the assignee becomes the "secured party of record" and may authorize the filing of a continuation statement, termination statement, or other amendment. Note that under Section 9-310(c) [30-9A-310(3)] no filing of an assignment is required as a condition of continuing the perfected status of the security interest against creditors and transferees of the original debtor. However, if an assignment is not filed, the assignor remains the secured party of record, with the power (even if not the right) to authorize the filing of effective amendments. See Sections 9-511(c), 9-509(d) [30-9A-511(3) and 30-9A-509(4)].

Where a record of a mortgage is effective as a financing statement filed as a fixture filing (Section 9-502(c) [30-9A-502(3)]), then an assignment of record of the security interest may be made only in the manner in which an assignment of record of the mortgage may be made under local real-property law.

3. **Comparison to Prior Law.** Most of the changes reflected in this section are for clarification or to embrace medium-neutral drafting. As a general matter, this section preserves the opportunity given by former Section 9-405 [30-9-405, now repealed] to assign a security interest of record in one of two different ways. Under subsection (a) [subsection (1)], a secured party may assign all of its power to affect a financing statement by naming an assignee in the initial financing statement. The secured party of record may accomplish the same result under subsection (b) [subsection (2)] by making a subsequent filing. Subsection (b) [subsection (2)] also may be used for an assignment of only some of the secured party of record's power to affect a financing statement, e.g., the power to affect the financing statement as it relates to particular items of collateral or as it relates to an undivided interest in a security interest in all the collateral. An initial financing statement may not be used to change the secured party of record under these circumstances. However, an amendment adding the assignee as a secured party of record may be used.

30-9A-515. Duration and effectiveness of financing statement — effect of lapsed financing statement.

Official Comments

1. **Source.** Former Section 9-403(2), (3), (6) [30-9-403(2), (3), (6), now repealed].

2. **Period of Financing Statement's Effectiveness.** Subsection (a) [subsection (1)] states the general rule: a financing statement is effective for a five-year period unless its effectiveness is continued under this section or terminated under Section 9-513 [30-9A-513]. Subsection (b) [subsection (2)] provides that if the financing statement relates to a public-finance transaction or a manufactured-home transaction and so indicates, the financing statement is effective for 30 years. These financings typically extend well beyond the standard, five-year period. Under subsection (f) [subsection (6)], a financing statement filed against a transmitting utility remains effective indefinitely, until a termination statement is filed. Likewise, under subsection (g) [subsection (7)], a mortgage effective as a fixture filing remains effective until its effectiveness terminates under real-property law.

3. **Lapse.** When the period of effectiveness under subsection (a) or (b) [subsection (1) or (2)] expires, the effectiveness of the financing statement lapses. The last sentence of subsection (c) [subsection (3)] addresses the effect of lapse. The deemed retroactive unperfection applies only with respect to purchasers for value; unlike former Section 9-403(2) [30-9-403(2), now repealed], it does not apply with respect to lien creditors.

Example 1: SP-1 and SP-2 both hold security interests in the same collateral. Both security interests are perfected by filing. SP-1 filed first and has priority under Section 9-322(a)(1) [30-9A-322(1)(a)]. The effectiveness of SP-1's filing lapses. As long as SP-2's security interest remains perfected thereafter, SP-2 is entitled to priority over SP-1's security interest, which is deemed never to have been perfected as against a purchaser for value (SP-2). See Section 9-322(a)(2) [30-9A-322(1)(b)].

Example 2: SP holds a security interest perfected by filing. On July 1, LC acquires a judicial lien on the collateral. Two weeks later, the effectiveness of the financing statement lapses. Although the security interest becomes unperfected upon lapse, it was perfected when LC acquired its lien. Accordingly, notwithstanding the lapse, the perfected security interest has priority over the rights of LC, who is not a purchaser. See Section 9-317(a)(2) [30-9A-317(1)(b)].

4. **Effect of Debtor's Bankruptcy.** Under former Section 9-403(2) [30-9-403(2), now repealed], lapse was tolled if the debtor entered bankruptcy or another insolvency proceeding. Nevertheless, being unaware that insolvency proceedings had been commenced, filing offices routinely removed records from the files as if lapse had not been tolled. Subsection (c) [subsection (3)] deletes the former tolling provision and thereby imposes a new burden on the secured party: to be sure that a financing statement does not lapse during the debtor's bankruptcy. The secured party can prevent lapse by filing a continuation statement, even without first obtaining relief from the automatic stay. See Bankruptcy Code Section 362(b)(3). Of course, if the debtor enters bankruptcy before lapse, the provisions of this Article [Title 30, chapter 9A] with respect to lapse would be of no effect to the extent that federal bankruptcy law dictates a contrary result (e.g., to the extent that the Bankruptcy Code determines rights as of the date of the filing of the bankruptcy petition).

5. **Continuation Statements.** Subsection (d) [subsection (4)] explains when a continuation statement may be filed. A continuation statement filed at a time other than that prescribed by subsection (d) [subsection (4)] is ineffective, see Section 9-510(c) [30-9A-510(3)], and the filing office may not accept it. See Sections 9-520(a), 9-516(b) [30-9A-520(1) and 30-9A-516(2)]. Subsection (e) [subsection (5)] specifies the effect of a continuation statement and provides for successive continuation statements.

Compiler's Comments

2013 Amendment: Chapter 75 in (6) inserted "initial". Amendment effective July 1, 2013.

Saving Clause: Section 26, Ch. 75, L. 2013, provided: "(1) Except as otherwise provided in [sections 19 through 25] [Title 30, chapter 9A, part 8], this chapter applies to a transaction or lien within its scope, even if the transaction or lien was entered into or created before [the effective of this act] [July 1, 2013].

(2) This chapter does not affect an action, case, or proceeding commenced before [the effective date of this act] [July 1, 2013]."

Case Notes

DECISIONS UNDER UNIFORM COMMERCIAL CODE

Failure to File Continuation Statement — Never Perfected: In anticipation of establishing a meat packing plant in Malta, Montana, Big Sky Beef, LLC (Big Sky) entered into a contract in the summer of 2000 with Lafond Enterprises (Lafond) to install the prospective plant's refrigeration equipment. Shortly thereafter, Lafond contracted to acquire the refrigeration equipment from Thermal Supply, Inc. (Thermal). Lafond, Big Sky, and Thermal entered into a Joint Check Agreement and Assignment dated August 3, 2000. According to the Agreement, Lafond assigned Thermal the right to receive $231,256 from any money due or that may become due to Lafond from Big Sky. Big Sky agreed to hold $231,256 in trust for Thermal, to make payments directly to Thermal within 30 days of delivery, and to guarantee payment to Thermal. Thermal shipped the refrigeration equipment to Big Sky, but it was never installed. On June 25, 2001, a financing statement signed by representatives of Big Sky and Thermal was filed with the Montana Secretary of State, naming Big Sky as debtor and Thermal as the secured party. A list identifying the refrigeration equipment was attached to the financing statement. In May of 2001, Big Sky Beef signed a promissory note for $250,000 and executed a security agreement to secure the note to B-4 Ventures, LLC (B-4 Ventures). B-4 Ventures then assigned all of its rights to the note and agreement to Saulsbury. On July 2, 2001, a financing statement was filed in the office of the Montana Secretary of State signed by Big Sky as debtor, B-4 Ventures as creditor, and Saulsbury as assignee. This financing statement contained broad language encompassing all equipment owned by Big Sky. On June 26, 2006, Saulsbury filed a continuation statement, extending its financing statement's period of effectiveness until 2011. Thermal did not receive payment and initiated this action on March 19, 2004, claiming it had a perfected security interest in the refrigeration equipment. Saulsbury defended, denying that Thermal had a security interest and stating that, if it did, the interest had lapsed. Thermal moved for summary judgment and was denied by the District Court, which held that the documents of the transaction were insufficient in themselves to create a security interest as a matter of law, but that ultimate resolution of the issue would be reserved for trial. Saulsbury also moved for summary judgment, arguing that Thermal's failure to file a timely continuation statement had caused Thermal's financing statement to lapse. The court denied Saulsbury's motion, reasoning that any need for filing a continuation statement had been tolled by Thermal's initiation of litigation. Saulsbury then moved for summary judgment on the same grounds the District Court had used to deny Thermal's motion—that Thermal had not initially created a security interest in the equipment. At a summary judgment hearing, after Thermal acknowledged to the court that no other documents signed by Big Sky and relevant to the creation of a security interest between Thermal and Big Sky existed, the court granted Saulsbury's subsequent motion for summary judgment, concluding that a security interest had not been created and entering judgment in full in favor of Saulsbury. Thermal appealed. Under Revised Article 9 of the UCC, there is no provision that expressly tolls or extends the period of effectiveness of a financing statement during litigation. The District Court concluded that the 5-year period of effectiveness was nonetheless tolled during litigation by virtue of the "relate back" provisions of 30-9A-601(5). The Supreme Court cited the official comment and precedent in holding that perfected status must be maintained throughout litigation to maintain a priority position or to "relate back" in the enforcement of a UCC secured interest. Any perfected security interest that Thermal may have held at the time it initiated this suit lapsed due to its failure to timely file a continuation statement and, pursuant to 30-9A-515(4), is considered to never have been perfected. Summary judgment for Saulsbury was appropriate. Thermal Supply, Inc. v. Big Sky Beef, LLC, 2008 MT 355, 346 M 341, 195 P3d 1227 (2008).

DECISIONS UNDER UNIFORM TRUST RECEIPTS ACT

Trust Receipt Transaction: Even though none of the documents in a trust receipt transaction between an automobile dealer and a finance company were filed or recorded, the fact made no difference with respect to the liability of an insurer for injury to an automobile in the possession of the insured dealer. Keating v. Univ. Underwriters Ins. Co., 133 M 89, 320 P2d 351 (1958).

Attorney General's Opinions

DECISIONS UNDER UNIFORM TRUST RECEIPTS ACT

Continuation Statement: A valid continuation statement becomes effective upon the conclusion of the 5-year initial period during which a financing statement is effective or upon the conclusion of any previous 5-year extension of that initial period. To be valid, continuation statements must be filed during the 6-month period preceding conclusion of the initial 5-year financing statement period or any extension thereof. 40 A.G. Op. 60 (1984).

Filing and Effect of Continuation Statement: Under 30-9-403(3) (section now repealed, see 30-9A-515): (1) the 5-year extension period effected by a valid continuation statement begins to run upon conclusion of the initial 5-year financing statement period and any previous 5-year extension period; (2) conversely, extension periods do not begin on the date a continuation statement is filed; (3) to be effective, a continuation statement must be filed during the 6-month period preceding termination of the original 5-year financing statement period and any 5-year extension period; and (4) County Clerk and Recorders are not required to accept for filing continuation statements tendered outside the 6-month period. 40 A.G. Op. 60 (1984).

30-9A-516. What constitutes filing — effectiveness of filing.

Official Comments

1. **Source.** Subsection (a) [subsection (1)]: former Section 9-403(1) [30-9-403(1), now repealed]; the remainder is new.

2. **What Constitutes Filing.** Subsection (a) [subsection (1)] deals generically with what constitutes filing of a record, including an initial financing statement and amendments of all kinds (e.g., assignments, termination statements, and continuation statements). It follows former Section 9-403(1) [30-9-403(1), now repealed], under which either acceptance of a record by the filing office or presentation of the record and tender of the filing fee constitutes filing.

3. **Effectiveness of Rejected Record.** Subsection (b) [subsection (2)] provides an exclusive list of grounds upon which the filing office may reject a record. See Section 9-520(a) [30-9A-520(1)]. Although some of these grounds would also be grounds for rendering a filed record ineffective (e.g., an initial financing statement does not provide a name for the debtor), many others would not be (e.g., an initial financing statement does not provide a mailing address for the debtor or secured party of record). Neither this section nor Section 9-520 [30-9A-520] requires or authorizes the filing office to determine, or even consider, the accuracy of information provided in a record.

A financing statement or other record that is communicated to the filing office but which the filing office refuses to accept provides no public notice, regardless of the reason for the rejection. However, this section distinguishes between records that the filing office rightfully rejects and those that it wrongfully rejects. A filer is able to prevent a rightful rejection by complying with the requirements of subsection (b) [subsection (2)]. No purpose is served by giving effect to records that justifiably never find their way into the system, and subsection (b) [subsection (2)] so provides.

Subsection (d) [subsection (4)] deals with the filing office's unjustified refusal to accept a record. Here, the filer is in no position to prevent the rejection and as a general matter should not be prejudiced by it. Although wrongfully rejected records generally are effective, subsection (d) [subsection (4)] contains a special rule to protect a third-party purchaser of the collateral (e.g., a buyer or competing secured party) who gives value in reliance upon the apparent absence of the record from the files. As against a person who searches the public record and reasonably relies on what the public record shows, subsection (d) [subsection (4)] imposes upon the filer the risk that a record failed to make its way into the filing system because of the filing office's wrongful rejection of it. (Compare Section 9-517 [30-9A-517], under which a mis-indexed financing statement is fully effective.) This risk is likely to be small, particularly when a record is presented electronically, and the filer can guard against this risk by conducting a post-filing search of the records. Moreover, Section 9-520(b) [30-9A-520(2)] requires the filing office to give prompt notice of its refusal to accept a record for filing.

4. **Method or Medium of Communication.** Rejection pursuant to subsection (b) (1) [subsection (2)(a)] for failure to communicate a record properly should be understood to mean noncompliance with procedures relating to security, authentication, or other communication-related requirements that the filing office may impose. Subsection (b)(1) [subsection (2)(a)] does not authorize a filing office to impose additional substantive requirements. See Section 9-520 [30-9A-520], Comment 2.

5. **Address for Secured Party of Record.** Under subsection (b)(4) [subsection (2)(d)] and Section 9-520(a) [30-9A-520(1)], the lack of a mailing address for the secured party of record requires the filing office to reject an initial financing statement. The failure to include an address for the secured party of record no longer renders a financing statement ineffective. See Section 9-502(a) [30-9A-502(1)]. The function of the address is not to identify the secured party of record but rather to provide an address to which others can send required notifications, e.g., of a purchase-money security interest in inventory or of the disposition of collateral. Inasmuch as the address shown on a filed financing statement is an "address that is reasonable under the circumstances," a person required to send a notification to the secured party may satisfy the requirement by sending a notification to that address, even if the address is or becomes incorrect. See Section 9-102 [30-9A-102] (definition of "send"). Similarly, because the address is "held out by [the secured party] as the place for receipt of such communications [i.e., communications relating to security interests]," the secured party is deemed to have received a notification delivered to that address. See Section 1-202(e) [30-1-210(5)].

6. **Uncertainty Concerning Individual Debtor's Surname.** Subsection (b)(3)(C) [subsection (2)(c)(iii)] requires the filing office to reject an initial financing statement or amendment adding an individual debtor if the office cannot index the record because it does not identify the debtor's surname (e.g., it is unclear whether the debtor's name is Elton or John).

7. **Inability of Filing Office to Read or Decipher Information.** Under subsection (c)(1) [subsection (3)(a)], if the filing office cannot read or decipher information, the information is not provided by a record for purposes of subsection (b) [subsection (2)].

8. **Classification of Records.** For purposes of subsection (b) [subsection (2)], a record that does not indicate it is an amendment or identify an initial financing statement to which it relates is deemed to be an initial financing statement. See subsection (c)(2) [subsection (3)(b)].

9. **Effectiveness of Rejectable But Unrejected Record.** Section 9-520(a) [30-9A-520(1)] requires the filing office to refuse to accept an initial financing statement for a reason set forth in subsection (b) [subsection (2)]. However, if the filing office accepts such a financing statement nevertheless, the financing statement generally is effective if it complies with the requirements of Section 9-502(a) and (b) [30-9A-502(1) and (2)]. See Section 9-520(c) [30-9A-520(3)]. Similarly, an otherwise effective financing statement generally remains so even though the information in the financing statement becomes incorrect. See Section 9-507(b) [30-9A-507(2)]. (Note that if the information required by subsection (b)(5) [subsection (2)(e)] is incorrect when the financing statement is filed, Section 9-338 [30-9A-338] applies.)

Compiler's Comments

2013 Amendment: Chapter 75 in (2)(c)(ii) substituted "information statement" for "correction statement"; in (2)(c)(iii) substituted "debtor's surname" for "debtor's last name"; in (2)(e)(ii) substituted "name provided as the name of the debtor is the name of" for "debtor is"; deleted former (2)(e)(iii) that read: "(iii) if the financing statement indicates that the debtor is an organization, provide:

(A) a type of organization for the debtor;
(B) a jurisdiction of organization for the debtor; or
(C) an organizational identification number for the debtor or indicate that the debtor has none"; and made minor changes in style. Amendment effective July 1, 2013.

Saving Clause: Section 26, Ch. 75, L. 2013, provided: "(1) Except as otherwise provided in [sections 19 through 25] [Title 30, chapter 9A, part 8], this chapter applies to a transaction or lien within its scope, even if the transaction or lien was entered into or created before [the effective of this act] [July 1, 2013].

(2) This chapter does not affect an action, case, or proceeding commenced before [the effective date of this act] [July 1, 2013]."

Administrative Rules

ARM 44.6.201 Defining search criteria for Uniform Commercial Code certified searches.

30-9A-517. Effect of indexing errors.

Official Comments

1. **Source.** New.

2. **Effectiveness of Mis-Indexed Records.** This section provides that the filing office's error in mis-indexing a record does not render ineffective an otherwise effective record. As did former Section 9-401 [30-9-401, now repealed, see 30-9A-501], this section imposes the risk of filing-office error on those who search the files rather than on those who file.

30-9A-518. Claim concerning inaccurate or wrongfully filed record.

Official Comments

1. **Source.** New.

2. **Information Statements.** Former Article 9 [Title 30, chapter 9, now repealed] did not afford a nonjudicial means for a debtor to indicate that a financing statement or other record was inaccurate or wrongfully filed. Subsection (a) [subsection (1)] affords the debtor the right to file an information statement. Among other requirements, the information statement must provide the basis for the debtor's belief that the public record should be corrected. See subsection (b) [subsection (2)]. These provisions, which resemble the analogous remedy in the Fair Credit Reporting Act, 15 U.S.C. § 1681i, afford an aggrieved person the opportunity to state its position on the public record. They do not permit an aggrieved person to change the legal effect of the public record. Thus, although a filed information statement becomes part of the "financing statement," as defined in Section 9-102 [30-9A-102], the filing does not affect the effectiveness of the initial financing statement or any other filed record. See subsection (e) [subsection (5)].

Sometimes a person files a termination statement or other record relating to a filed financing statement without being entitled to do so. A secured party of record with respect to the financing statement who believes that such a record has been filed may, but need not, file an information statement indicating that the person that filed the record was not entitled to do so. See subsection (c) [subsection (3)]. An information statement has no legal effect. Its sole purpose is to provide some limited public notice that the efficacy of a filed record is disputed. If the person that filed the record was not entitled to do so, the filed record is ineffective, regardless of whether the secured party of record files an information statement. Likewise, if the person that filed the record was entitled to do so, the filed record is effective, even if the secured party of record files an information statement. See Sections 9-510(a) [30-9A-510(1)], 9-518(e) [30-9A-518(5)]. Because an information statement filed under subsection (c) [subsection (3)] has no legal effect, a secured party of record—even one who is aware of the unauthorized filing of a record—has no duty to file one. Just as searchers bear the burden of determining whether the filing of initial financing statement was authorized, searchers bear the burden of determining whether the filing of every subsequent record was authorized.

Inasmuch as the filing of an information statement has no legal effect, this section does not provide a mechanism by which a secured party can correct an error that it discovers in its own financing statement.

This section does not displace other provisions of this Article [Title 30, chapter 9A] that impose liability for making unauthorized filings or failing to file or send a termination statement (see Section 9-625(e) [30-9A-625(5)]), nor does it displace any available judicial remedies.

3. **Resort to Other Law.** This Article [Title 30, chapter 9A] cannot provide a satisfactory or complete solution to problems caused by misuse of the public records. The problem of "bogus" filings is not limited to the UCC filing system but extends to the real-property records, as well. A summary judicial procedure for correcting the public record and criminal penalties for those

who misuse the filing and recording systems are likely to be more effective and put less strain on the filing system than provisions authorizing or requiring action by filing and recording offices.

Compiler's Comments

2013 Amendment: Chapter 75 in (1), (2), (2)(a)(ii), (2)(b), and (5) substituted "information statement" for "correction statement"; in (2) after "An information statement" inserted "under subsection (1)"; inserted (3) and (4) regarding information statements for a secured party; and made minor changes in style. Amendment effective July 1, 2013.

Saving Clause: Section 26, Ch. 75, L. 2013, provided: "(1) Except as otherwise provided in [sections 19 through 25] [Title 30, chapter 9A, part 8], this chapter applies to a transaction or lien within its scope, even if the transaction or lien was entered into or created before [the effective of this act] [July 1, 2013].

(2) This chapter does not affect an action, case, or proceeding commenced before [the effective date of this act] [July 1, 2013]."

30-9A-519. Numbering, maintaining, and indexing records — communicating information provided in records.

Official Comments

1. **Source.** Former Sections 9-403(4), (7), 9-405(2) [30-9-403(4), (7), 30-9-405(2), both now repealed].

2. **Filing Office's Duties.** Subsections (a) through (e) [subsections (1) through (5)] set forth the duties of the filing office with respect to filed records. Subsection (h) [subsection (8)], which is new, imposes a minimum standard of performance for those duties. Prompt indexing is crucial to the effectiveness of any filing system. An accepted but un-indexed record affords no public notice. Subsection (f) [subsection (6)] requires the filing office to maintain appropriate storage and retrieval facilities, and subsection (g) [subsection (7)] contains minimum requirements for the retention of records.

3. **File Number.** Subsection (a)(1) [subsection (1)(a)] requires the filing office to assign a unique number to each filed record. That number is the "file number" only if the record is an initial financing statement. See Section 9-102 [30-9A-102].

4. **Time of Filing.** Subsection (a)(2) and Section 9-523 [subsection (1)(b) and 30-9A-523] refer to the "date and time" of filing. The statutory text does not contain any instructions to a filing office as to how the time of filing is to be determined. The method of determining or assigning a time of filing is an appropriate matter for filing-office rules to address.

5. **Related Records.** Subsections (c) and (f) [subsections (3) and (6)] are designed to ensure that an initial financing statement and all filed records relating to it are associated with one another, indexed under the name of the debtor, and retrieved together. To comply with subsection (f) [subsection (6)], a filing office (other than a real-property recording office in a State that enacts subsection (f) [subsection (6)], Alternative B) must be capable of retrieving records in each of two ways: by the name of the debtor and by the file number of the initial financing statement to which the record relates.

6. **Prohibition on Deleting Names from Index.** This Article [Title 30, chapter 9A] contemplates that the filing office will not delete the name of a debtor from the index until at least one year passes after the effectiveness of the financing statement lapses as to all secured parties of record. See subsection (g) [subsection (7)]. This rule applies even if the filing office accepts an amendment purporting to delete or modify the name of a debtor or terminate the effectiveness of the financing statement. If an amendment provides a modified name for a debtor, the amended name should be added to the index, see subsection (c)(2) [subsection (3)(b)], but the pre-amendment name should remain in the index.

Compared to former Article 9 [Title 30, chapter 9, now repealed], the rule in subsection (g) [subsection (7)] increases the amount of information available to those who search the public records. The rule also contemplates that searchers-not the filing office-will determine the significance and effectiveness of filed records.

Administrative Rules

ARM 44.6.201 Defining search criteria for Uniform Commercial Code certified searches.
ARM 44.6.202 Effective date and time.
ARM 44.6.203 Requirements for filing U.C.C. amendments.

30-9A-520. Acceptance and refusal to record.

Official Comments

1. **Source.** New.

2. **Refusal to Accept Record for Filing.** In some States, filing offices considered themselves obligated by former Article 9 [Title 30, chapter 9, now repealed] to review the form and content of a financing statement and to refuse to accept those that they determine are legally insufficient. Some filing offices imposed requirements for or conditions to filing that do not appear in the statute. Under this section, the filing office is not expected to make legal judgments and is not permitted to impose additional conditions or requirements.

Subsection (a) [subsection (1)] both prescribes and limits the bases upon which the filing office must and may reject records by reference to the reasons set forth in Section 9-516(b) [30-9A-516(2)]. For the most part, the bases for rejection are limited to those that prevent the filing office from dealing with a record that it receives-because some of the requisite information (e.g., the debtor's name) is missing or cannot be deciphered, because the record is not communicated by a method (e.g., it is MIME- rather than UU-encoded) or medium (e.g., it is written rather than electronic) that the filing office accepts, or because the filer fails to tender an amount equal to or greater than the filing fee.

3. **Consequences of Accepting Rejectable Record.** Section 9-516(b) [30-9A-516(2)] includes among the reasons for rejecting an initial financing statement the failure to give certain information that is not required as a condition of effectiveness. In conjunction with Section 9-516(b)(5) [30-9A-516(2)(e)], this section requires the filing office to refuse to accept a financing statement that is legally sufficient to perfect a security interest under Section 9-502 [30-9A-502] but does not contain a mailing address for the debtor or disclose whether the debtor is an individual or an organization. The information required by Section 9-516(b)(5) [30-9A-516(2)(e)] assists searchers in weeding out "false positives," i.e., records that a search reveals but which do not pertain to the debtor in question. It assists filers by helping to ensure that the debtor's name is correct and that the financing statement is filed in the proper jurisdiction.

If the filing office accepts a financing statement that does not give this information at all, the filing is fully effective. Section 9-520(c) [30-9A-520(3)]. The financing statement also generally is effective if the information is given but is incorrect; however, Section 9-338 [30-9A-338] affords protection to buyers and holders of perfected security interests who give value in reasonable reliance upon the incorrect information.

4. **Filing Office's Duties with Respect to Rejected Record.** Subsection (b) [subsection (2)] requires the filing office to communicate the fact of rejection and the reason therefor within a fixed period of time. Inasmuch as a rightfully rejected record is ineffective and a wrongfully rejected record is not fully effective, prompt communication concerning any rejection is important.

5. **Partial Effectiveness of Record.** Under subsection (d) [subsection (4)], the provisions of this Part [Title 30, chapter 9A, part 5] apply to each debtor separately. Thus, a filing office may reject an initial financing statement or other record as to one named debtor but accept it as to the other.

Example: An initial financing statement is communicated to the filing office. The financing statement names two debtors, John Smith and Jane Smith. It contains all of the information described in Section 9-516(b)(5) [30-9A-516(2)(e)] with respect to John but lacks some of the information with respect to Jane. The filing office must accept the financing statement with respect to John, reject it with respect to Jane, and notify the filer of the rejection.

30-9A-521. Uniform form of written financing statement and amendment.

Official Comments

1. **Source.** New.

2. **"Safe Harbor" Written Forms.** Although Section 9-520 [30-9A-520] limits the bases upon which the filing office can refuse to accept records, this section provides sample written forms that must be accepted in every filing office in the country, as long as the filing office's rules permit it to accept written communications. By completing one of the forms in this section, a secured party can be certain that the filing office is obligated to accept it.

The forms in this section are based upon national financing statement forms that were in use under former Article 9 [Title 30, chapter 9, now repealed]. Those forms were developed over an extended period and reflect the comments and suggestions of filing officers, secured parties and their counsel, and service companies. The formatting of those forms and of the ones in this section has been designed to reduce error by both filers and filing offices.

A filing office that accepts written communications may not reject, on grounds of form or format, a filing using these forms. Although filers are not required to use the forms, they are encouraged and can be expected to do so, inasmuch as the forms are well designed and avoid the risk of rejection on the basis of form or format. As their use expands, the forms will rapidly become familiar to both filers and filing-office personnel. Filing offices may and should encourage the use of these forms by declaring them to be the "standard" (but not exclusive) forms for each jurisdiction, albeit without in any way suggesting that alternative forms are unacceptable.

The multi-purpose form in subsection (b) [subsection (2), form not adopted in Montana—Secretary of State authorized to adopt model form] covers changes with respect to the debtor, the secured party, the collateral, and the status of the financing statement (termination and continuation). A single form may be used for several different types of amendments at once (e.g., both to change a debtor's name and continue the effectiveness of the financing statement).

Compiler's Comments

2013 Amendment: Chapter 75 in (1) after "statement" substituted language regarding official text of the amendments to Article 9 for "in the model form adopted by the secretary of state"; in (1) and (2) before "30-9A-516(2)" deleted "30-9A-502 and"; and in (2) after "record" substituted language regarding Form UCC3 and Form UCC3Ad in the final official text of the amendments to Article 9 for "in the model form adopted by the secretary of state". Amendment effective July 1, 2013.

Saving Clause: Section 26, Ch. 75, L. 2013, provided: "(1) Except as otherwise provided in [sections 19 through 25] [Title 30, chapter 9A, part 8], this chapter applies to a transaction or lien within its scope, even if the transaction or lien was entered into or created before [the effective of this act] [July 1, 2013].

(2) This chapter does not affect an action, case, or proceeding commenced before [the effective date of this act] [July 1, 2013]."

Deviation From Uniform Act — No Substantial Difference: The final official text of the 2010 amendments to Article 9 of the Uniform Commercial Code promulgated by The American Law Institute and the National Conference of Commissioners on Uniform State Laws incorporated forms directly into the text of this section. Rather than inserting the forms into the text, Montana has instead chosen to incorporate the forms by reference.

30-9A-522. Maintenance and destruction of records.

Official Comments

1. **Source.** Former Section 9-403(3) [30-9-403(3), now repealed], revised substantially.
2. **Maintenance of Records.** Section 9-523 [30-9A-523] requires the filing office to provide information concerning certain lapsed financing statements. Accordingly, subsection (a) [subsection (1)] requires the filing office to maintain a record of the information in a financing statement for at least one year after lapse. During that time, the filing office may not delete any information with respect to a filed financing statement; it may only add information. This approach relieves the filing office from any duty to determine whether to substitute or delete information upon receipt of an amendment. It also assures searchers that they will receive all information with respect to financing statements filed against a debtor and thereby be able themselves to determine the state of the public record.

The filing office may maintain this information in any medium. Subsection (b) [subsection (2)] permits the filing office immediately to destroy written records evidencing a financing statement, provided that the filing office maintains another record of the information contained in the financing statement as required by subsection (a) [subsection (1)].

Compiler's Comments

2015 Amendment: Chapter 348 in (1) substituted "part 11" for "part 2". Amendment effective October 1, 2015.

Severability: Section 72, Ch. 348, L. 2015, was a severability clause.

Administrative Rules

ARM 44.6.201 Defining search criteria for Uniform Commercial Code certified searches.

30-9A-523. Information from filing office — sale or license of records.

Official Comments

1. **Source.** Former Section 9-407 [30-9-407, now repealed]; subsections (d) and (e) [subsections (4) and (5)] are new.
2. **Filing Office's Duty to Provide Information.** Former Section 9-407 [30-9-407, now repealed], dealing with obtaining information from the filing office, was bracketed to suggest to

legislatures that its enactment was optional. Experience has shown that the method by which interested persons can obtain information concerning the public records should be uniform. Accordingly, the analogous provisions of this Article [Title 30, chapter 9A] are not in brackets.

Most of the other changes from former Section 9-407 [30-9-407, now repealed] are for clarification, to embrace medium-neutral drafting, or to impose standards of performance on the filing office.

3. **Acknowledgments of Filing.** Subsections (a) and (b) [subsections (1) and (2)] require the filing office to acknowledge the filing of a record. Under subsection (a) [subsection (1)], the filing office is required to acknowledge the filing of a written record only upon request of the filer. Subsection (b) [subsection (2)] requires the filing office to acknowledge the filing of a non-written record even in the absence of a request from the filer.

4. **Response to Search Request.** Subsection (c)(3) [subsection (3)(c)] requires the filing office to provide "the information contained in each financing statement" to a person who requests it. This requirement can be satisfied by providing copies, images, or reports. The requirement does not in any manner inhibit the filing office from also offering to provide less than all of the information (presumably for a lower fee) to a person who asks for less. Thus, subsection (c) [subsection (3)] accommodates the practice of providing only the type of record (e.g., initial financing statement, continuation statement), number assigned to the record, date and time of filing, and names and addresses of the debtor and secured party when a requesting person asks for no more (i.e., when the person does not ask for copies of financing statements). In contrast, the filing office's obligation under subsection (b) [subsection (2)] to provide an acknowledgment containing "the information contained in the record" is not defined by a customer's request. Thus unless the filer stipulates otherwise, to comply with subsection (b) [subsection (2)] the filing office's acknowledgment must contain all of the information in a record.

Subsection (c) [subsection (3)] assures that a minimum amount of information about filed records will be available to the public. It does not preclude a filing office from offering additional services.

5. **Lapsed and Terminated Financing Statements.** This section reflects the policy that terminated financing statements will remain part of the filing office's data base. The filing office may remove from the data base only lapsed financing statements, and then only when at least a year has passed after lapse. See Section 9-519(g) [30-9A-519(7)]. Subsection (c)(1)(C) [subsection (3)(a)(iii)] requires a filing office to conduct a search and report as to lapsed financing statements that have not been removed from the data base, when requested.

6. **Search by Debtor's Address.** Subsection (c)(1)(A) [subsection (3)(a)(i)] contemplates that, by making a single request, a searcher will receive the results of a search of the entire public record maintained by any given filing office. Addition of the bracketed language in subsection (c)(1)(A) [subsection (3)(a)(i)] would permit a search report limited to financing statements showing a particular address for the debtor, but only if the search request is so limited. With or without the bracketed language, this subsection does not permit the filing office to compel a searcher to limit a request by address.

7. **Medium of Communication; Certificates.** Former Article 9 [Title 30, chapter 9, now repealed] provided that the filing office respond to a request for information by providing a certificate. The principle of medium-neutrality would suggest that the statute not require a written certificate. Subsection (d) [subsection (4)] follows this principle by permitting the filing office to respond by communicating "in any medium." By permitting communication "in any medium," subsection (d) [subsection (4)] is not inconsistent with a system in which persons other than filing office staff conduct searches of the filing office's (computer) records.

Some searchers find it necessary to introduce the results of their search into evidence. Because official written certificates might be introduced into evidence more easily than official communications in another medium, subsection (d) [subsection (4)] affords States the option of requiring the filing office to issue written certificates upon request. The alternative bracketed language in subsection (d) [subsection (4)] recognizes that some States may prefer to permit the filing office to respond in another medium, as long as the response can be admitted into evidence in the courts of that State without extrinsic evidence of its authenticity.

8. **Performance Standard.** The utility of the filing system depends on the ability of searchers to get current information quickly. Accordingly, subsection (e) [subsection (5)] requires that the filing office respond to a request for information no later than two business days after it receives the request. The information contained in the response must be current as of a date no earlier than three business days before the filing office receives the request. See subsection (c)(1)

[subsection (3)(a)]. The failure of the filing office to comply with performance standards, such as subsection (e) [subsection (5)], has no effect on the private rights of persons affected by the filing of records.

9. **Sales of Records in Bulk.** Subsection (f) [subsection (6)], which is new, mandates that the appropriate official or the filing office sell or license the filing records to the public in bulk, on a nonexclusive basis, in every medium available to the filing office. The details of implementation are left to filing-office rules.

Administrative Rules

ARM 44.5.301 Definitions and requirements for annual report online filing.
ARM 44.6.302 Nonstandard inquiry.

30-9A-524. Delay by filing office.

Official Comments

Source. New; derived from Section 4-109 [now repealed].

30-9A-525. Fees.

Official Comments

1. **Source.** Various sections of former Part 4 [Title 30, chapter 9, part 4, now repealed].

2. **Fees.** This section contains all fee requirements for filing, indexing, and responding to requests for information. Uniformity in the fee structure (but not necessarily in the amount of fees) makes this Article [Title 30, chapter 9A] easier for secured parties to use and reduces the likelihood that a filed record will be rejected for failure to pay at least the correct amount of the fee. See Section 9-516(b)(2) [30-9A-516(2)(b)].

The costs of processing electronic records are less than those with respect to written records. Accordingly, this section mandates a lower fee as an incentive to file electronically and imposes the additional charge (if any) for multiple debtors only with respect to written records. When written records are used, this Article [Title 30, chapter 9A] encourages the use of the uniform forms in Section 9-521 [30-9A-521, forms not adopted in Montana]. The fee for filing these forms should be no greater than the fee for other written records.

To make the relevant information included in a filed record more accessible once the record is found, this section mandates a higher fee for longer written records than for shorter ones. Finally, recognizing that financing statements naming more than one debtor are most often filed against a husband and wife, any additional charge for multiple debtors applies to records filed with respect to more than two debtors, rather than with respect to more than one.

Compiler's Comments

2023 Amendment: See 2023 Session Law for amendment made by sec. 1, Ch. 568, L. 2023. Amendment effective May 18, 2023.

2001 Amendment — Coordination: Section 29(1), Ch. 396, L. 2001, a coordination instruction, provided that if Senate Bill No. 23 and Ch. 396 were both passed and approved, then the amendments to this section were those contained in sec. 29. Senate Bill No. 23 was passed and approved as Ch. 179, L. 2001. Section 29, Ch. 396, substituted (1) concerning fees to be set and deposited in accordance with 2-15-405 for former (1) through (4) that read: "(1) Except as otherwise provided in subsection (5), the fee for filing and indexing a record under this part, other than an initial financing statement of the kind described in 30-9-522(3), must be commensurate with costs and must be established by rule.

(2) Except as otherwise provided in subsection (5), the fee for filing and indexing an initial financing statement of the kind described in 30-9-522(3) must be commensurate with costs and must be established by rule.

(3) The number of names required to be indexed does not affect the amount of the fees in subsections (1) and (2).

(4) The fee for responding to a request for information from the filing office, including for communicating whether there is on file any financing statement naming a particular debtor, must be commensurate with costs and must be established by rule"; and made minor changes in style. Amendment effective July 1, 2001.

The amendments to this section made by sec. 18, Ch. 179, L. 2001, and sec. 14, Ch. 396, L. 2001, were replaced by sec. 29(1), Ch. 396, L. 2001, a coordination section.

Administrative Rules

ARM 44.5.121 Miscellaneous fees.
ARM 44.6.104 Fees for filing notice of federal tax lien.
ARM 44.6.105 Uniform Commercial Code fees.

ARM 44.6.111 Liens appearing on farm bill master list and fees for obtaining the farm bill master list.

30-9A-526. Filing-office rules.

Official Comments

1. **Source.** New; subsection (b) [subsection (2)] derives in part from the Uniform Consumer Credit Code (1974).

2. **Rules Required.** Operating a filing office is a complicated business, requiring many more rules and procedures than this Article [Title 30, chapter 9A] can usefully provide. Subsection (a) [subsection (1)] requires the adoption of rules to carry out the provisions of Article 9 [Title 30, chapter 9A]. The filing-office rules must be consistent with the provisions of the statute and adopted in accordance with local procedures. The publication requirement informs secured parties about filing-office practices, aids secured parties in evaluating filing-related risks and costs, and promotes regularity of application within the filing office.

3. **Importance of Uniformity.** In today's national economy, uniformity of the policies and practices of the filing offices will reduce the costs of secured transactions substantially. The International Association of Corporate Administrators (IACA), referred to in subsection (b) [subsection (2)], is an organization whose membership includes filing officers from every State. These individuals are responsible for the proper functioning of the Article 9 [Title 30, chapter 9A] filing system and have worked diligently to develop model filing-office rules, with a view toward efficiency and uniformity.

Although uniformity is an important desideratum, subsection (a) [subsection (1)] affords considerable flexibility in the adoption of filing-office rules. Each State may adopt a version of subsection (a) [subsection (1)] that reflects the desired relationship between the statewide filing office described in Section 9-501(a)(2) [30-9A-501(1)(b)] and the local filing offices described in Section 9-501(a)(1) [30-9A-501(1)(a)] and that takes into account the practices of its filing offices. Subsection (a) [subsection (1)] need not designate a single official or agency to adopt rules applicable to all filing offices, and the rules applicable to the statewide filing office need not be identical to those applicable to the local filing office. For example, subsection (a) [subsection (1)] might provide for the statewide filing office to adopt filing-office rules, and, if not prohibited by other law, the filing office might adopt one set of rules for itself and another for local offices. Or, subsection (a) [subsection (1)] might designate one official or agency to adopt rules for the statewide filing office and another to adopt rules for local filing offices.

Administrative Rules

Title 44, chapter 6, ARM Secretary of State — Uniform Commercial Code.

30-9A-527. Duty to report.

Official Comments

1. **Source.** New; derived in part from the Uniform Consumer Credit Code (1974).

2. **Duty to Report.** This section is designed to promote compliance with the standards of performance imposed upon the filing office and with the requirement that the filing office's policies, practices, and technology be consistent and compatible with the policies, practices, and technology of other filing offices.

Compiler's Comments

2013 Amendment: Chapter 155 in first sentence inserted "If there have been any changes affecting filing-office rules" and substituted "the state administration and veterans' affairs interim committee by September 15 in the year preceding the regular legislative session" for "each session of the legislature"; and made minor changes in style. Amendment effective October 1, 2013.

Preamble: The preamble attached to Ch. 155, L. 2013, provided: "WHEREAS, House Bill No. 142 (Chapter 126, Laws of 2011) required interim committees to "review statutorily established advisory councils and required reports of assigned agencies to make recommendations to the next legislature"; and

WHEREAS, the State Administration and Veterans' Affairs Interim Committee voted to make the recommendations contained in this bill."

Part 6
Default

Part Compiler's Comments

Saving Clause: Section 169, Ch. 305, L. 1999, provided: "(1) Except as otherwise provided in [sections 164 through 169] [sections 162 through 167—30-9A-703 through 30-9A-706, 30-9A-708, and 30-9A-709], [this act] applies to a transaction or lien within its scope, even if the transaction or lien was entered into or created before [this act] takes effect.

(2) Except as otherwise provided in subsection (3) and [sections 164 through 169] [sections 162 through 167—30-9A-703 through 30-9A-706, 30-9A-708, and 30-9A-709]:

(a) transactions and liens that were not governed by [former chapter 9, now repealed] were validly entered into or created before [this act] takes effect and would be subject to [this act] if they had been entered into or created after [this act] takes effect, and the rights, duties, and interests flowing from those transactions and liens remain valid after [this act] takes effect; and

(b) the transactions and liens may be terminated, completed, consummated, or enforced as required or permitted by [this act] or by the law that otherwise would apply if [this act] did not take effect.

(3) [This act] does not affect an action, case, or proceeding commenced before [this act] takes effect."

Part Case Notes

CASES DECIDED AFTER 1999 REVISION

Security Interest Terminated — Creditor's Obligations Under U.C.C. Chapter 9A Not Terminated: The debtors entered an installment contract to buy a mobile home from the sellers. They became delinquent on monthly payments, and eventually the seller invoked the acceleration clause and demanded the outstanding balance due plus notice fees. The debtors returned the mobile home to the seller, who sold it to a new buyer 2 months later. The Supreme Court found that although the seller's disposition of the mobile home terminated the security interest under 30-9A-617, the seller's obligations as a creditor under Title 30, ch. 9A, remained, including the obligation to give the debtor notice of how the creditor intends to dispose of the collateral under 30-9A-611 and 30-9A-614, the obligation to conduct a commercially reasonable resale of the collateral under 30-9A-610, and the obligation to account to the debtor for any surplus realized from the sale of the collateral under 30-9A-608, 30-9A-615, 30-9A-616, and 30-9A-626. Christman v. Clause, 2019 MT 132, 396 Mont. 142, 443 P.3d 472.

Repossession of Mobile Home — Accounting and Surplus Obligations Not Terminated by Release: The plaintiff entered into a purchase sale agreement with the defendant to purchase a mobile home. She later vacated the home and allowed the defendant to take possession of it. After the defendant sold the home for more than what the plaintiff had owed on it, she requested an accounting from the sale and to receive the excess proceeds. The defendant argued that the plaintiff had signed a release relinquishing all rights to the home, thereby terminating any obligation it had to provide an accounting under the Uniform Commercial Code (U.C.C.). The District Court agreed and granted the defendant summary judgment. On appeal, the Supreme Court reversed, holding that the release did not terminate U.C.C. obligations, and remanded the matter back to the District Court. Hutzenbiler v. RJC Inv., Inc., 2019 MT 80, 395 Mont. 250, 439 P.3d 378.

Debtor Signed Release Provided by Creditor — Creditor Did Not Refund Surplus — Debtor Sought Surplus — Release Did Not End Article 9 Protections for Creditor: The District Court erred in granting summary judgment to the defendant creditor and in determining that a release agreement the plaintiff debtor signed terminated any further application of the Uniform Commercial Code. The plaintiff entered into an installment sale contract and security agreement to purchase a mobile home with a company that assigned the contract to the defendant. Six years later, the plaintiff voluntarily vacated the mobile home and allowed the defendant to take possession of it. When the plaintiff returned the mobile home to the defendant, she owed $39,791.80. The plaintiff signed a full release of contract, under which she released all rights to the mobile home. The defendant resold the mobile home 1 month later, without notice to the plaintiff, for $53,500, which the plaintiff alleged was $13,708.20 more than the principal she owed when she returned the mobile home. The defendant did not refund any surplus to the plaintiff and disputed that a surplus was in fact realized. The plaintiff argued that the execution of the release did not terminate the defendant's duty under 30-9A-608 to pay her the surplus proceeds from the resale of the mobile home. The Supreme Court determined that despite the release, Article 9 of the U.C.C. (Title 30, ch. 9A) may still require the creditor to account for a surplus realized from the collection of an account or from the disposition of the collateral. The plaintiff's relationship to the defendant was one of debtor to creditor through a secured transaction governed by Article 9. When the plaintiff defaulted on her obligations under the contract, the defendant's rights and responsibilities as a creditor also were governed by Article 9. The defendant's argument that Article 9 no longer governed the parties' relationship following execution of the release was based on its representation that it agreed in the release to absolve the plaintiff from any further contractual obligation she owed to the defendant. The release did not, by its express terms, lift the parties' relationship from that of debtor and creditor under Article 9 or render obsolete the protections afforded a debtor under 30-9A-608 and 30-9A-615. Kapor v. RJC Inv., Inc., 2019 MT 41, 394 Mont. 311, 434 P.3d 869.

CASES DECIDED PRIOR TO 1999 REVISION

Cancellation of Promissory Notes — Erases Security Interest: In fashioning judgment in a case involving fraud and misrepresentation, the District Court awarded the bank all of plaintiff's property and canceled all of the promissory notes from plaintiffs to the bank. The bank contended this violated its rights as a secured creditor. It contended it was entitled to a variety of options in enforcing its security interest and could not be forced to satisfy its claim by taking possession of the property. On appeal, the Supreme Court upheld the award. By finding the bank guilty of fraud and misrepresentation, the trial court could properly cancel the promissory notes. Canceling the notes erased the bank's specific security interests. Having canceled the notes, the trial court, sitting in equity, had a great deal of leeway in fashioning a remedy. The remedy allowed the bank to mitigate its losses and was proper. Crystal Springs Trout Co. v. First State Bank of Froid, 225 M 122, 732 P2d 819, 44 St. Rep. 90 (1987).

30-9A-601. Rights after default — judicial enforcement — consignor or buyer of accounts, chattel paper, payment intangibles, or promissory notes.

Official Comments

1. **Source.** Former Section 9-501(1), (2), (5) [30-9-501(1), (2), (5), now repealed].

2. **Enforcement: In General.** The rights of a secured party to enforce its security interest in collateral after the debtor's default are an important feature of a secured transaction. (Note that the term "rights," as defined in Section 1-201 [30-1-201], includes "remedies.") This Part provides those rights as well as certain limitations on their exercise for the protection of the defaulting debtor, other creditors, and other affected persons. However, subsections (a) and (d) [subsections (1) and (4)] make clear that the rights provided in this Part do not exclude other rights provided by agreement.

3. **When Remedies Arise.** Under subsection (a) [subsection (1)] the secured party's rights arise "[a]fter default." As did former Section 9-501 [30-9-501, now repealed], this Article [Title 30, chapter 9A] leaves to the agreement of the parties the circumstances giving rise to a default. This Article [Title 30, chapter 9A] does not determine whether a secured party's post-default conduct can constitute a waiver of default in the face of an agreement stating that such conduct shall not constitute a waiver. Rather, it continues to leave to the parties' agreement, as supplemented by law other than this Article [Title 30, chapter 9A], the determination whether a default has occurred or has been waived. See Section 1-103 [30-1-103].

4. **Possession of Collateral; Section 9-207 [30-9A-207].** After a secured party takes possession of collateral following a default, there is no longer any distinction between a security interest that before default was nonpossessory and a security interest that was possessory before default, as under a common-law pledge. This Part [Title 30, chapter 9A, part 6] generally does not distinguish between the rights of a secured party with a nonpossessory security interest and those of a secured party with a possessory security interest. However, Section 9-207 [30-9A-207] addresses rights and duties with respect to collateral in a secured party's possession. Under subsection (b) [subsection (2)] of this section, Section 9-207 [30-9A-207] applies not only to possession before default but also to possession after default. Subsection (b) [subsection (2)] also has been conformed to Section 9-207 [30-9A-207], which, unlike former Section 9-207 [30-9-207, now repealed, see 30-9A-207], applies to secured parties having control of collateral.

5. **Cumulative Remedies.** Former Section 9-501(1) [30-9-501(1), now repealed] provided that the secured party's remedies were cumulative, but it did not explicitly provide whether the remedies could be exercised simultaneously. Subsection (c) [subsection (3)] permits the simultaneous exercise of remedies if the secured party acts in good faith. The liability scheme of Subpart 2 [30-9A-625 through 30-9A-628] affords redress to an aggrieved debtor or obligor. Moreover, permitting the simultaneous exercise of remedies under subsection (c) [subsection (3)] does not override any non-UCC law, including the law of tort and statutes regulating collection of

debts, under which the simultaneous exercise of remedies in a particular case constitutes abusive behavior or harassment giving rise to liability.

6. **Judicial Enforcement.** Under subsection (a) [subsection (1)] a secured party may reduce its claim to judgment or foreclose its interest by any available procedure outside this Article [Title 30, chapter 9A] under applicable law. Subsection (e) [subsection (5)] generally follows former Section 9-501(5) [30-9-501(5), now repealed]. It makes clear that any judicial lien that the secured party may acquire against the collateral effectively is a continuation of the original security interest (if perfected) and not the acquisition of a new interest or a transfer of property on account of a preexisting obligation. Under former Section 9-501(5) [30-9-501(5), now repealed], the judicial lien was stated to relate back to the date of perfection of the security interest. Subsection (e) [subsection (5)], however, provides that the lien relates back to the earlier of the date of filing or the date of perfection. This provides a secured party who enforces a security interest by judicial process with the benefit of the "first-to-file-or-perfect" priority rule of Section 9-322(a)(1) [30-9A-322(1)(a)].

7. **Agricultural Liens.** Part 6 [Title 30, chapter 9A, part 6] provides parallel treatment for the enforcement of agricultural liens and security interests. Because agricultural liens are statutory rather than consensual, this Article [Title 30, chapter 9A] does draw a few distinctions between these liens and security interests. Under subsection (e) [subsection (5)], the statute creating an agricultural lien would govern whether and the date to which an execution lien relates back. Section 9-606 [30-9A-606] explains when a "default" occurs in the agricultural lien context.

8. **Execution Sales.** Subsection (f) [subsection (6)] also follows former Section 9-501(5) [30-9-501(5), now repealed]. It makes clear that an execution sale is an appropriate method of foreclosure contemplated by this Part [Title 30, chapter 9A, part 6]. However, the sale is governed by other law and not by this Article [Title 30, chapter 9A], and the limitations under Section 9-610 [30-9A-610] on the right of a secured party to purchase collateral do not apply.

9. **Sales of Receivables; Consignments.** Subsection (g) [subsection (7)] provides that, except as provided in Section 9-607(c) [30-9A-607(3)], the duties imposed on secured parties do not apply to buyers of accounts, chattel paper, payment intangibles, or promissory notes. Although denominated "secured parties," these buyers own the entire interest in the property sold and so may enforce their rights without regard to the seller ("debtor") or the seller's creditors. Likewise, a true consignor may enforce its ownership interest under other law without regard to the duties that this Part imposes on secured parties. Note, however, that Section 9-615 [30-9A-615] governs cases in which a consignee's secured party (other than a consignor) is enforcing a security interest that is senior to the security interest (i.e., ownership interest) of a true consignor.

Compiler's Comments

2005 Amendment: Chapter 575 in (2) inserted "30-7-107". Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

Case Notes

Reliance on Numerous Extensions of Loan to Receive Another — No Excuse for Nonpayment of Debt — Foreclosure — No Error: The defendant argued that the plaintiff bank waived its right to the mature debt of a loan at the end of a seventh extension period by continuing to give extensions, and the defendant did not pay off the loan because he assumed he would receive another extension. However, the plaintiff waived its rights only for a defined period within the extension agreements, not its right to full, eventual payment. Because the defendant was not promised another extension period and the evidence indicated that the plaintiff informed the defendant the loan would not be extended again, there was no issue of material fact to excuse the defendant's nonpayment of the debt, and the District Court did not err in granting the plaintiff summary judgment to foreclose. Furthermore, the plaintiff was not obligated by the covenant of good faith and fair dealing to extend the loan repayment an eighth time. HSBC Bank USA, N.A. v. Anderson, 2017 MT 257, 389 Mont. 106, 406 P.3d 416.

Enforcement of Agricultural Lien Following Sale or Transfer of Farm Products — Assignment of Inchoate or Unperfected Lien Interests Allowed: A crop of sugar beets was sold, and a pesticide sprayer that held an agricultural lien sought to enforce the lien after the sale. Plaintiff bank also held a secured interest on the proceeds of the crop. The buyer issued checks made payable jointly to the bank and the sprayer, honoring the agricultural lien, and the lienholder's unconditioned negotiation of the check acknowledged satisfaction and release of its lien. The bank asserted that, not being an agricultural supplier, the sprayer had no right to file the lien and further contended that because inchoate or unperfected liens are not assignable, any argument that the supplier had assigned its lien right to the sprayer must fail as a matter of law. The sprayer argued that the supplier was clearly eligible to file an agricultural lien and that all actions taken by the sprayer were taken in an agency capacity for the supplier, as indicated in the lien filing, so the payment was not an assignment. Alternatively, the sprayer contended that the transaction was a pass-through between related entities constituting a limited assignment for collection purposes only and that even if the bank's evidence was sufficient to demonstrate that the transaction was a full assignment supported by consideration, inchoate lien interests are nonetheless assignable. The Supreme Court concluded that the dispute was best resolved on the issue of the assignability of inchoate lien interests, noting that generally property of any kind may be transferred, that a right arising out of an obligation is the property of the person to whom it is due and may be transferred, and that Montana's general policy supports the free assignability of rights and obligations stemming from contractual obligations. An agricultural lien is a security and ought to follow the debt or contract to which it pertains, and the free assignability of the right to perfect an agricultural lien comports with lien statutes as well as modern business practices. Thus, even though the supplier's lien was not yet perfected when transferred to the sprayer, it was assignable, and the sprayer validly proceeded to perfect and enforce the lien and was entitled to funds in the amount stipulated by the parties as payment for the chemicals sold by the supplier to the farm and applied by the sprayer and was entitled to the interest on the funds to be credited on that sum. Stockman Bank of Mont. v. Mon-Kota, Inc., 2008 MT 74, 342 M 115, 180 P3d 1125 (2008).

30-9A-602. Waiver and variance of rights and duties.

Official Comments

1. **Source.** Former Section 9-501(3) [30-9-501(3), now repealed].

2. **Waiver: In General.** Section 1-102(3) [30-1-102(3)] addresses which provisions of the UCC are mandatory and which may be varied by agreement. With exceptions relating to good faith, diligence, reasonableness, and care, immediate parties, as between themselves, may vary its provisions by agreement. However, in the context of rights and duties after default, our legal system traditionally has looked with suspicion on agreements that limit the debtor's rights and free the secured party of its duties. As stated in former Section 9-501 [30-9-501, now repealed], Comment 4, "no mortgage clause has ever been allowed to clog the equity of redemption." The context of default offers great opportunity for overreaching. The suspicious attitudes of the courts have been grounded in common sense. This section, like former Section 9-501(3) [30-9-501(3), now repealed], codifies this long-standing and deeply rooted attitude. The specified rights of the debtor and duties of the secured party may not be waived or varied except as stated. Provisions that are not specified in this section are subject to the general rules in Section 1-102(3) [30-1-102(3)].

3. **Nonwaivable Rights and Duties.** This section revises former Section 9-501(3) [30-9-501(3), now repealed] by restricting the ability to waive or modify additional specified rights and duties: (i) duties under Section 9-207(b)(4)(C) [30-9A-207(2)(d)(iii)], which deals with the use and operation of consumer goods, (ii) the right to a response to a request for an accounting, concerning a list of collateral, or concerning a statement of account (Section 9-210 [30-9A-210]), (iii) the duty to collect collateral in a commercially reasonable manner (Section 9-607 [30-9A-607]), (iv) the implicit duty to refrain from a breach of the peace in taking possession of collateral under Section 9-609 [30-9A-609], (v) the duty to apply noncash proceeds of collection or disposition in a commercially reasonable manner (Sections 9-608 and 9-615 [30-9A-608 and 30-9A-615]), (vi) the right to a special method of calculating a surplus or deficiency in certain dispositions to a secured party, a person related to secured party, or a secondary obligor (Section 9-615 [30-9A-615]), (vii) the duty to give an explanation of the calculation of a surplus or deficiency (Section 9-616 [30-9A-616]), (viii) the right to limitations on the effectiveness of certain waivers (Section 9-624 [30-9A-624]), and (ix) the right to hold a secured party liable for failure to comply with this Article [Title 30, chapter 9A] (Sections 9-625 and 9-626 [30-9A-625 and 30-9A-626]). For clarity

and consistency, this Article [Title 30, chapter 9A] uses the term "waive or vary" instead of "renounc[e] or modify[]," which appeared in former Section 9-504(3) [30-9-504(3), now repealed].

This section provides generally that the specified rights and duties "may not be waived or varied." However, it does not restrict the ability of parties to agree to settle, compromise, or renounce claims for past conduct that may have constituted a violation or breach of those rights and duties, even if the settlement involves an express "waiver."

Section 9-610(c) [30-9A-610(3)] limits the circumstances under which a secured party may purchase at its own private disposition. Transactions of this kind are equivalent to "strict foreclosures" and are governed by Sections 9-620 [30-9A-620], 9-621 [30-9A-621], and 9-622 [30-9A-622]. The provisions of these sections can be waived only to the extent provided in Section 9-624(b) [30-9A-624(2)]. See Section 9-602 [30-9A-602].

4. **Waiver by Debtors and Obligors.** The restrictions on waiver contained in this section apply to obligors as well as debtors. This resolves a question under former Article 9 [Title 30, chapter 9, now repealed] as to whether secondary obligors, assuming that they were "debtors" for purposes of former Part 5 [Title 30, chapter 9, part 5, now repealed], were permitted to waive, under the law of suretyship, rights and duties under that Part.

5. **Certain Post-Default Waivers.** Section 9-624 [30-9A-624] permits post-default waivers in limited circumstances. These waivers must be made in agreements that are authenticated. Under Section 1-201 [30-1-201], an "'agreement' means the bargain of the parties in fact." In considering waivers under Section 9-624 [30-9A-624] and analogous agreements in other contexts, courts should carefully scrutinize putative agreements that appear in records that also address many additional or unrelated matters.

Case Notes

No Authenticated Agreement — Waiver of Right to Notification of Disposition of Collateral Invalid: The debtors entered an installment contract to buy a mobile home from the sellers. They became delinquent on monthly payments, and eventually the seller invoked the acceleration clause and demanded the outstanding balance due plus notice fees. The debtors returned the mobile home to the seller, who sold it to a new buyer 2 months later without notifying the debtors. On review, the Supreme Court held that the debtors' voluntary surrender of and transfer of title to the collateral mobile home to the sellers did not automatically waive their right to notice of its resale. Rather, any waiver of the notice would have had to take the form of an authenticated writing signed after the default. Because no authenticated writing was signed after the default, the debtors' right to notice remained intact and was violated. Christman v. Clause, 2019 MT 132, 396 Mont. 142, 443 P.3d 472.

Security Interest Terminated — Creditor's Obligations Under U.C.C. Chapter 9A Not Terminated: The debtors entered an installment contract to buy a mobile home from the sellers. They became delinquent on monthly payments, and eventually the seller invoked the acceleration clause and demanded the outstanding balance due plus notice fees. The debtors returned the mobile home to the seller, who sold it to a new buyer 2 months later. The Supreme Court found that although the seller's disposition of the mobile home terminated the security interest under 30-9A-617, the seller's obligations as a creditor under Title 30, ch. 9A, remained, including the obligation to give the debtor notice of how the creditor intends to dispose of the collateral under 30-9A-611 and 30-9A-614, the obligation to conduct a commercially reasonable resale of the collateral under 30-9A-610, and the obligation to account to the debtor for any surplus realized from the sale of the collateral under 30-9A-608, 30-9A-615, 30-9A-616, and 30-9A-626. Christman v. Clause, 2019 MT 132, 396 Mont. 142, 443 P.3d 472.

Debtor Signed Release Provided by Creditor — Creditor Did Not Refund Surplus — Debtor Sought Surplus — Release Did Not End Article 9 Protections for Creditor: The District Court erred in granting summary judgment to the defendant creditor and in determining that a release agreement the plaintiff debtor signed terminated any further application of the Uniform Commercial Code. The plaintiff entered into an installment sale contract and security agreement to purchase a mobile home with a company that assigned the contract to the defendant. Six years later, the plaintiff voluntarily vacated the mobile home and allowed the defendant to take possession of it. When the plaintiff returned the mobile home to the defendant, she owed $39,791.80. The plaintiff signed a full release of contract, under which she released all rights to the mobile home. The defendant resold the mobile home 1 month later, without notice to the plaintiff, for $53,500, which the plaintiff alleged was $13,708.20 more than the principal she owed when she returned the mobile home. The defendant did not refund any surplus to the plaintiff and disputed that a surplus was in fact realized. The plaintiff argued that the execution of the release did not terminate the defendant's duty under 30-9A-608 to pay her the surplus proceeds from the resale of the mobile home. The Supreme Court determined that despite the release, Article 9 of the U.C.C. (Title 30, ch. 9A) may still require the creditor to account for a surplus realized from the collection of an account or from the disposition of the collateral. The plaintiff's relationship to the defendant was one of debtor to creditor through a secured transaction governed by Article 9. When the plaintiff defaulted on her obligations under the contract, the defendant's rights and responsibilities as a creditor also were governed by Article 9. The defendant's argument that Article 9 no longer governed the parties' relationship following execution of the release was based on its representation that it agreed in the release to absolve the plaintiff from any further contractual obligation she owed to the defendant. The release did not, by its express terms, lift the parties' relationship from that of debtor and creditor under Article 9 or render obsolete the protections afforded a debtor under 30-9A-608 and 30-9A-615. Kapor v. RJC Inv., Inc., 2019 MT 41, 394 Mont. 311, 434 P.3d 869.

30-9A-603. Agreement on standards concerning rights and duties.

Official Comments

1. **Source.** Former Section 9-501(3) [30-9-501(3), now repealed].

2. **Limitation on Ability to Set Standards.** Subsection (a) [subsection (1)], like former Section 9-501(3) [30-9-501(3), now repealed], permits the parties to set standards for compliance with the rights and duties under this Part if the standards are not "manifestly unreasonable." Under subsection (b) [subsection (2)], the parties are not permitted to set standards measuring fulfillment of the secured party's duty to take collateral without breaching the peace.

30-9A-604. Procedure if security agreement covers real property or fixtures.

Official Comments

1. **Source.** Former Sections 9-501(4), 9-313(8) [30-9-501(4), 30-9-313(8), both now repealed].

2. **Real-Property-Related Collateral.** The collateral in many transactions consists of both real and personal property. In the interest of simplicity, speed, and economy, subsection (a) [subsection (1)], like former Section 9-501(4) [30-9-501(4), now repealed], permits (but does not require) the secured party to proceed as to both real and personal property in accordance with its rights and remedies with respect to the real property. Subsection (a) [subsection (1)] also makes clear that a secured party who exercises rights under Part 6 [Title 30, chapter 9A, part 6] with respect to personal property does not prejudice any rights under real-property law.

This Article [Title 30, chapter 9A] does not address certain other real-property-related problems. In a number of States, the exercise of remedies by a creditor who is secured by both real property and non-real property collateral is governed by special legal rules. For example, under some anti-deficiency laws, creditors risk loss of rights against personal property collateral if they err in enforcing their rights against the real property. Under a "one-form-of-action" rule (or rule against splitting a cause of action), a creditor who judicially enforces a real property mortgage and does not proceed in the same action to enforce a security interest in personalty may (among other consequences) lose the right to proceed against the personalty. Although statutes of this kind create impediments to enforcement of security interests, this Article [Title 30, chapter 9A] does not override these limitations under other law.

3. **Fixtures.** Subsection (b) [subsection (2)] is new. It makes clear that a security interest in fixtures may be enforced either under real-property law or under any of the applicable provisions of Part 6 [Title 30, chapter 9A, part 6], including sale or other disposition either before or after removal of the fixtures (see subsection (c) [subsection (3)]). Subsection (b) [subsection (2)] also serves to overrule cases holding that a secured party's only remedy after default is the removal of the fixtures from the real property. See, e.g., Maplewood Bank & Trust v. Sears, Roebuck & Co., 625 A.2d 537 (N.J. Super. Ct. App. Div. 1993).

Subsection (c) [subsection (3)] generally follows former Section 9-313(8) [30-9-313(8), now repealed]. It gives the secured party the right to remove fixtures under certain circumstances. A secured party whose security interest in fixtures has priority over owners and encumbrancers of the real property may remove the collateral from the real property. However, subsection (d) [subsection (4)] requires the secured party to reimburse any owner (other than the debtor) or encumbrancer for the cost of repairing any physical injury caused by the removal. This right to reimbursement is implemented by the last sentence of subsection (d) [subsection (4)], which gives the owner or encumbrancer a right to security or indemnity as a condition for giving permission to remove.

Case Notes

CASES DECIDED AFTER 1999 REVISION

Evidence of Malicious Attachment — Motion to Dismiss Properly Denied: In Spooner Constr. & Tree Serv., Inc. v. Maner, 2000 MT 161, 300 M 268, 3 P3d 641 (2000), it was held that plaintiff admitted no entitlement to any money from a logging agreement or any rental fees associated with defendant's use of a logging skidder. Nevertheless, plaintiff made no attempt to contact defendant to submit a bill, request payment, or discuss the logging contract, but instead, after disabling the skidder, plaintiff filed a lien against and later attached the skidder, with the intent to bid on it at a Sheriff's sale. Defendant presented both direct and circumstantial evidence that, without probable cause, plaintiff wrongfully attached the skidder with an improper motive and with reckless disregard for the facts, constituting a prima facie case of malicious wrongful attachment. Plaintiff's motion to dismiss was properly denied. Spooner Constr. & Tree Serv., Inc. v. Maner, 2003 MT 43, 314 M 268, 66 P3d 263 (2003).

CASES DECIDED PRIOR TO 1999 REVISION

Filing of Quitclaim Deed Not Precluding Deficiency Judgment in Foreclosure Proceeding: To secure a bank loan in a different transaction, the Haugens gave the bank a quitclaim deed to a motel that they had agreed to purchase under a contract for deed. The Haugens defaulted on the bank loan. The bank's filing of the deed did not preclude the bank from a deficiency judgment in its foreclosure action in regard to the other transaction. Prior to that default and the bank's filing of the deed, the Haugens had defaulted on the contract for deed and had relinquished any interest in the motel. The Haugens contended that once the bank filed the deed, it could not collect a deficiency judgment. However, because the Haugens no longer had an interest in the motel, the bank could take nothing from the deed and the bank's filing of the deed had no legal effect. Blaine Bank of Mont. v. Haugen, 249 M 381, 816 P2d 447, 48 St. Rep. 777 (1991), affirmed in Blaine Bank of Mont. v. Haugen, 260 M 29, 858 P2d 14, 50 St. Rep. 927 (1993).

Remedies Provided by Agreement Not Precluded: The statement of rights and remedies of the Uniform Commercial Code does not exclude other remedies provided by agreement. Ottersen v. Rubick, 246 M 93, 803 P2d 1066, 47 St. Rep. 2274 (1990).

Promissory Note Secured by Alleged Mortgage on Real Property as Well as Collateral — Writ of Attachment for Possession of Collateral Harmless Error: Defendants, who borrowed $5,000, claimed the District Court erred in issuing a Writ of Attachment when the promissory note was secured by an alleged mortgage on real property as well as other collateral. The Supreme Court found a grave question as to whether the wording of the note constituted a hypothecation for real estate mortgage purposes, but noted that the parties did not dispute a security interest in the other collateral. Under the Uniform Commercial Code, plaintiff as secured party had the right to take possession of the collateral upon default, and the alleged erroneous issuance of the Writ of Attachment to take possession of the collateral was harmless error. Montgomery v. Hunt, 227 M 279, 738 P2d 887, 44 St. Rep. 1081 (1987).

Failure to Give Required Notice of Sale of Collateral — Deficiency Judgment Precluded: Plaintiffs defaulted on loan. Pursuant to an order of the Blackfeet Tribal Court enforceable in the Montana courts as a matter of comity, the creditor sold the collateral and applied the proceeds to the amount due, leaving a deficiency. The loan agreement required notice of sale of collateral to be given at least 5 days before the sale and to state the time and place of the sale. The notice stated neither the time nor the place. This failure of notice precluded the creditor from obtaining a deficiency judgment in the Montana courts. Wippert v. The Blackfeet Tribe of the Blackfeet Indian Reservation, 215 M 85, 695 P2d 461, 42 St. Rep. 200 (1985), overruled in part on other grounds by Green v. Gerber, 2013 MT 35, 369 Mont. 20, 303 P.3d 729.

Repossession Not Required of Secured Creditor as Condition Precedent to Judgment Against Other Property: The defendant defaulted on a secured loan from the plaintiff, and the plaintiff, rather than repossessing the defendant's personal property in which it had been given a security interest, obtained a judgment against the defendant for the amount owed and brought a declaratory judgment action to determine if the judgment constituted a lien on the defendant's real property. The Supreme Court reversed the District Court's ruling that there was no effective lien, holding that the plaintiff was not required to first repossess the secured property and then sue for the deficiency. AVCO Financial Serv. of Billings One, Inc. v. Christiaens, 201 M 117, 651 P2d 220, 39 St. Rep. 1993 (1982).

Guaranty Distinguished From Other Contracts: Guarantors are not "debtors" within meaning of section of Uniform Commercial Code prohibiting waiver of rules granting rights to debtor and imposing duties on the secured party. First Nat'l Park Bank v. Johnson, 553 F2d 599 (C.A. Mont. 1977), distinguished in Westmont Tractor Co. v. Continental I, Inc., 224 M 516, 731 P2d 327, 43 St. Rep. 2380 (1986).

30-9A-605. Unknown debtor or secondary obligor.

Official Comments

1. **Source.** New.

2. **Duties to Unknown Persons.** This section relieves a secured party from duties owed to a debtor or obligor, if the secured party does not know about the debtor or obligor. Similarly, it relieves a secured party from duties owed to a secured party or lienholder who has filed a financing statement against the debtor, if the secured party does not know about the debtor. For example, a secured party may be unaware that the original debtor has sold the collateral subject to the security interest and that the new owner has become the debtor. If so, the secured party owes no duty to the new owner (debtor) or to a secured party who has filed a financing statement against the new owner. This section should be read in conjunction with the exculpatory provisions in Section 9-628 [30-9A-628]. Note that it relieves a secured party not only from duties arising under this Article [Title 30, chapter 9A] but also from duties arising under other law by virtue of the secured party's status as such under this Article [Title 30, chapter 9A], unless the other law otherwise provides.

30-9A-606. Time of default for agricultural lien.

Official Comments

1. **Source.** New.

2. **Time of Default.** Remedies under this Part [Title 30, chapter 9A, part 6] become available upon the debtor's "default." See Section 9-601 [30-9A-601]. This section explains when "default" occurs in the agricultural-lien context. It requires one to consult the enabling statute to determine when the lienholder is entitled to enforce the lien.

30-9A-607. Collection and enforcement by secured party.

Official Comments

1. **Source.** Former Section 9-502 [30-9-502, now repealed]; subsections (b), (d), and (e) [subsections (2), (4), and (5)] are new.

2. **Collections: In General.** Collateral consisting of rights to payment is not only the most liquid asset of a typical debtor's business but also is property that may be collected without any interruption of the debtor's business This situation is far different from that in which collateral is inventory or equipment, whose removal may bring the business to a halt. Furthermore, problems of valuation and identification, present with collateral that is tangible personal property, frequently are not as serious in the case of rights to payment and other intangible collateral. Consequently, this section, like former Section 9-502 [30-9-502, now repealed], recognizes that financing through assignments of intangibles lacks many of the complexities that arise after default in other types of financing. This section allows the assignee to liquidate collateral by collecting whatever may become due on the collateral, whether or not the method of collection contemplated by the security arrangement before default was direct (i.e., payment by the account debtor to the assignee, "notification" financing) or indirect (i.e., payment by the account debtor to the assignor, "nonnotification" financing).

3. **Scope.** The scope of this section is broader than that of former Section 9-502 [30-9-502, now repealed]. It applies not only to collections from account debtors and obligors on instruments but also to enforcement more generally against all persons obligated on collateral. It explicitly provides for the secured party's enforcement of the debtor's rights in respect of the account debtor's (and other third parties') obligations and for the secured party's enforcement of supporting obligations with respect to those obligations. (Supporting obligations are components of the collateral under Section 9-203(f) [30-9A-203(6)].) The rights of a secured party under subsection (a) [subsection (1)] include the right to enforce claims that the debtor may enjoy against others. For example, the claims might include a breach- of-warranty claim arising out of a defect in equipment that is collateral or a secured party's action for an injunction against infringement of a patent that is collateral. Those claims typically would be proceeds of original collateral under Section 9-315 [30-9A-315].

4. **Collection and Enforcement Before Default.** Like Part 6 [Title 30, chapter 9A, part 6] generally, this section deals with the rights and duties of secured parties following default. However, as did former Section 9-502 [30-9-502, now repealed] with respect to collection rights, this section also applies to the collection and enforcement rights of secured parties even if a

default has not occurred, as long as the debtor has so agreed. It is not unusual for debtors to agree that secured parties are entitled to collect and enforce rights against account debtors prior to default.

5. **Collections by Junior Secured Party.** A secured party who holds a security interest in a right to payment may exercise the right to collect and enforce under this section, even if the security interest is subordinate to a conflicting security interest in the same right to payment. Whether the junior secured party has priority in the collected proceeds depends on whether the junior secured party qualifies for priority as a purchaser of an instrument (e.g., the account debtor's check) under Section 9-330(d) [30-9A-330(4)], as a holder in due course of an instrument under Sections 3-305 and 9-331(a) [30-3-305 and 30-9A-331(1)], or as a transferee of money under Section 9-332(a) [30-9A-332(1)]. See Sections 9-330 [30-9A-330], Comment 7; 9-331 [30-9A-331], Comment 5; and 9-332 [30-9A-332].

6. **Relationship to Rights and Duties of Persons Obligated on Collateral.** This section permits a secured party to collect and enforce obligations included in collateral in its capacity as a secured party. It is not necessary for a secured party first to become the owner of the collateral pursuant to a disposition or acceptance. However, the secured party's rights, as between it and the debtor, to collect from and enforce collateral against account debtors and others obligated on collateral under subsection (a) [subsection (1)] are subject to Section 9-341 [30-9A-341], Part 4 [Title 30, chapter 9A, part 4], and other applicable law. Neither this section nor former Section 9-502 [30-9-502, now repealed] should be understood to regulate the duties of an account debtor or other person obligated on collateral. Subsection (e) [subsection (5)] makes this explicit. For example, the secured party may be unable to exercise the debtor's rights under an instrument if the debtor is in possession of the instrument, or under a non-transferable letter of credit if the debtor is the beneficiary. Unless a secured party has control over a letter-of-credit right and is entitled to receive payment or performance from the issuer or a nominated person under Article 5 [Title 30, chapter 5], its remedies with respect to the letter-of-credit right may be limited to the recovery of any identifiable proceeds from the debtor. This section establishes only the baseline rights of the secured party vis-a-vis the debtor-the secured party is entitled to enforce and collect after default or earlier if so agreed.

7. **Deposit Account Collateral.** Subsections (a)(4) and (5) [subsections (1)(d) and (1)(e)] set forth the self-help remedy for a secured party whose collateral is a deposit account. Subsection (a)(4) [subsection (1)(d)] addresses the rights of a secured party that is the bank with which the deposit account is maintained. That secured party automatically has control of the deposit account under Section 9-104(a)(1) [30-9A-104(1)(a)]. After default, and otherwise if so agreed, the bank/secured party may apply the funds on deposit to the secured obligation.

If a security interest of a third party is perfected by control (Section 9-104(a)(2) or (a)(3) [30-9A-104(1)(b) or (1)(c)]), then after default, and otherwise if so agreed, the secured party may instruct the bank to pay out the funds in the account. If the third party has control under Section 9-104(a)(3) [30-9A-104(1)(c)], the depositary institution is obliged to obey the instruction because the secured party is its customer. See Section 4-401 [30-4-401]. If the third party has control under Section 9-104(a)(2) [30-9A-104(1)(b)], the control agreement determines the depositary institution's obligation to obey.

If a security interest in a deposit account is unperfected, or is perfected by filing by virtue of the proceeds rules of Section 9-315 [30-9A-315], the depositary institution ordinarily owes no obligation to obey the secured party's instructions. See Section 9-341 [30-9A-341]. To reach the funds without the debtor's cooperation, the secured party must use an available judicial procedure.

8. **Rights Against Mortgagor of Real Property.** Subsection (b) [subsection (2)] addresses the situation in which the collateral consists of a mortgage note (or other obligation secured by a mortgage on real property). After the debtor's (mortgagee's) default, the secured party (assignee) may wish to proceed with a nonjudicial foreclosure of the mortgage securing the note but may be unable to do so because it has not become the assignee of record. The assignee/secured party may not have taken a recordable assignment at the commencement of the transaction (perhaps the mortgage note in question was one of hundreds assigned to the secured party as collateral). Having defaulted, the mortgagee may be unwilling to sign a recordable assignment. This section enables the secured party (assignee) to become the assignee of record by recording in the applicable real-property records the security agreement and an affidavit certifying default. Of course, the secured party's rights derive from those of its debtor. Subsection (b) [subsection (2)] would not entitle the secured party to proceed with a foreclosure unless the mortgagor also were in default or the debtor (mortgagee) otherwise enjoyed the right to foreclose.

9. **Commercial Reasonableness.** Subsection (c) [subsection (3)] provides that the secured party's collection and enforcement rights under subsection (a) [subsection (1)] must be exercised in a commercially reasonable manner. These rights include the right to settle and compromise claims against the account debtor. The secured party's failure to observe the standard of commercial reasonableness could render it liable to an aggrieved person under Section 9-625 [30-9A-625], and the secured party's recovery of a deficiency would be subject to Section 9-626 [30-9A-626]. Subsection (c) [subsection (3)] does not apply if, as is characteristic of most sales of accounts, chattel paper, payment intangibles, and promissory notes, the secured party (buyer) has no right of recourse against the debtor (seller) or a secondary obligor. However, if the secured party does have a right of recourse, the commercial-reasonableness standard applies to collection and enforcement even though the assignment to the secured party was a "true" sale. The obligation to proceed in a commercially reasonable manner arises because the collection process affects the extent of the seller's recourse liability, not because the seller retains an interest in the sold collateral (the seller does not).

10. **Attorney's Fees and Legal Expenses.** The phrase "reasonable attorney's fees and legal expenses," which appears in subsection (d) [subsection (4)], includes only those fees and expenses incurred in proceeding against account debtors or other third parties. The secured party's right to recover these expenses from the collections arises automatically under this section. The secured party also may incur other attorney's fees and legal expenses in proceeding against the debtor or obligor. Whether the secured party has a right to recover those fees and expenses depends on whether the debtor or obligor has agreed to pay them, as is the case with respect to attorney's fees and legal expenses under Sections 9-608(a)(1)(A) and 9-615(a)(1) [30-9A-608(1)(a)(i) and 30-9A-615(1)(a)]. The parties also may agree to allocate a portion of the secured party's overhead to collection and enforcement under subsection (d) or Section 9-608(a) [subsection (4) or 30-9A-608(1)].

Compiler's Comments

2013 Amendment: Chapter 75 in (2)(b)(i) inserted "with respect to the obligation secured by the mortgage". Amendment effective July 1, 2013.

Saving Clause: Section 26, Ch. 75, L. 2013, provided: "(1) Except as otherwise provided in [sections 19 through 25] [Title 30, chapter 9A, part 8], this chapter applies to a transaction or lien within its scope, even if the transaction or lien was entered into or created before [the effective of this act] [July 1, 2013].

(2) This chapter does not affect an action, case, or proceeding commenced before [the effective date of this act] [July 1, 2013]."

Case Notes

CASES DECIDED PRIOR TO 1999 REVISION

Notification of Account Debtor by Secured Party Not Interference With Third-Party Contracts: A bank that was an undisputed secured party contacted the debtor's customers and instructed them to pay their debts directly to the bank, which the debtor contended was tortious interference with its third-party contracts. However, under 30-9-502 (now repealed, see 30-9A-607 and 30-9A-608), a secured party is entitled to notify an account debtor to make payment to the secured party in the event of default, and such notification does not constitute tortious interference. Citizens First Nat'l Bank of Wolf Point v. Moe Motor Co., 248 M 495, 813 P2d 400, 48 St. Rep. 528 (1991).

30-9A-608. Application of proceeds of collection or enforcement — liability for deficiency and right to surplus.

Official Comments

1. **Source.** Subsection (a) [subsection (1)] is new; subsection (b) [subsection (2)] derives from former Section 9-502(2) [30-9-502(2), now repealed].

2. **Modifications of Prior Law.** Subsections (a) and (b) [subsections (1) and (2)] modify former Section 9-502(2) [30-9-502(2), now repealed] by explicitly providing for the application of proceeds recovered by the secured party in substantially the same manner as provided in Section 9-615(a) and (e) [30-9A-615(1) and (5)] for dispositions of collateral.

3. **Surplus and Deficiency.** Subsections (a)(4) and (b) [subsections (1)(d) and (2)] omit, as unnecessary, the references contained in former Section 9-502(2) [30-9-502(2), now repealed] to agreements varying the baseline rules on surplus and deficiency. The parties are always free to agree that an obligor will not be liable for a deficiency, even if the collateral secures an obligation, and that an obligor is liable for a deficiency, even if the transaction is a sale of receivables. For parallel provisions, see Section 9-615(d) and (e) [30-9A-615(4) and (5)].

4. **Noncash Proceeds.** Subsection (a)(3) [subsection (1)(c)] addresses the situation in which an enforcing secured party receives noncash proceeds.

Example: An enforcing secured party receives a promissory note from an account debtor who is unable to pay an account when it is due. The secured party accepts the note in exchange for extending the date on which the account debtor's obligation is due. The secured party may wish to credit its debtor (the assignor) with the principal amount of the note upon receipt of the note, but probably will prefer to credit the debtor only as and when the note is paid.

Under subsection (a)(3) [subsection (1)(c)], the secured party is under no duty to apply the note or its value to the outstanding obligation unless its failure to do so would be commercially unreasonable. If the secured party does apply the note to the outstanding obligation, however, it must do so in a commercially reasonable manner. The parties may provide for the method of application of noncash proceeds by agreement, if the method is not manifestly unreasonable. See Section 9-603 [30-9A-603]. This section does not explain when the failure to apply noncash proceeds would be commercially unreasonable; it leaves that determination to case-by-case adjudication. In the example, the secured party appears to have accepted the account debtor's note in order to increase the likelihood of payment and decrease the likelihood that the account debtor would dispute its obligation. Under these circumstances, it may well be commercially reasonable for the secured party to credit its debtor's obligations only as and when cash proceeds are collected from the account debtor, especially given the uncertainty that attends the account debtor's eventual payment. For an example of a secured party's receipt of noncash proceeds in which it may well be commercially unreasonable for the secured party to delay crediting its debtor's obligations with the value of noncash proceeds, see Section 9-615 [30-9A-615], Comment 3.

When the secured party is not required to "apply or pay over for application noncash proceeds," the proceeds nonetheless remain collateral subject to this Article [Title 30, chapter 9A]. If the secured party were to dispose of them, for example, appropriate notification would be required (see Section 9-611 [30-9A-611]), and the disposition would be subject to the standards provided in this Part (see Section 9-610 [30-9A-610]). Moreover, a secured party in possession of the noncash proceeds would have the duties specified in Section 9-207 [30-9A-207].

5. **No Effect on Priority of Senior Security Interest.** The application of proceeds required by subsection (a) [subsection (1)] does not affect the priority of a security interest in collateral which is senior to the interest of the secured party who is collecting or enforcing collateral under Section 9-607 [30-9A-607]. Although subsection (a) [subsection (1)] imposes a duty to apply proceeds to the enforcing secured party's expenses and to the satisfaction of the secured obligations owed to it and to subordinate secured parties, that duty applies only among the enforcing secured party and those persons. Concerning the priority of a junior secured party who collects and enforces collateral, see Section 9-607 [30-9A-607], Comment 5.

Compiler's Comments

2001 Amendment: Chapter 179 in (1)(a) and (1)(c) substituted references to 30-9A-607 for references to this section. Amendment effective July 1, 2001.

Case Notes

CASES DECIDED AFTER 1999 REVISION

Repossession of Mobile Home — Accounting and Surplus Obligations Not Terminated by Release: The plaintiff entered into a purchase sale agreement with the defendant to purchase a mobile home. She later vacated the home and allowed the defendant to take possession of it. After the defendant sold the home for more than what the plaintiff had owed on it, she requested an accounting from the sale and to receive the excess proceeds. The defendant argued that the plaintiff had signed a release relinquishing all rights to the home, thereby terminating any obligation it had to provide an accounting under the Uniform Commercial Code (U.C.C.). The District Court agreed and granted the defendant summary judgment. On appeal, the Supreme Court reversed, holding that the release did not terminate U.C.C. obligations, and remanded the matter back to the District Court. Hutzenbiler v. RJC Inv., Inc., 2019 MT 80, 395 Mont. 250, 439 P.3d 378.

Debtor Signed Release Provided by Creditor — Creditor Did Not Refund Surplus — Debtor Sought Surplus — Release Did Not End Article 9 Protections for Creditor: The District Court erred in granting summary judgment to the defendant creditor and in determining that a release agreement the plaintiff debtor signed terminated any further application of the Uniform Commercial Code. The plaintiff entered into an installment sale contract and security agreement to purchase a mobile home with a company that assigned the contract to the defendant. Six years later, the plaintiff voluntarily vacated the mobile home and allowed the defendant to take possession of it. When the plaintiff returned the mobile home to the defendant, she owed $39,791.80. The plaintiff signed a full release of contract, under which she released all rights to the mobile home. The defendant resold the mobile home 1 month later, without notice to the plaintiff, for $53,500, which the plaintiff alleged was $13,708.20 more than the principal she owed when she returned the mobile home. The defendant did not refund any surplus to the plaintiff and disputed that a surplus was in fact realized. The plaintiff argued that the execution of the release did not terminate the defendant's duty under 30-9A-608 to pay her the surplus proceeds from the resale of the mobile home. The Supreme Court determined that despite the release, Article 9 of the U.C.C. (Title 30, ch. 9A) may still require the creditor to account for a surplus realized from the collection of an account or from the disposition of the collateral. The plaintiff's relationship to the defendant was one of debtor to creditor through a secured transaction governed by Article 9. When the plaintiff defaulted on her obligations under the contract, the defendant's rights and responsibilities as a creditor also were governed by Article 9. The defendant's argument that Article 9 no longer governed the parties' relationship following execution of the release was based on its representation that it agreed in the release to absolve the plaintiff from any further contractual obligation she owed to the defendant. The release did not, by its express terms, lift the parties' relationship from that of debtor and creditor under Article 9 or render obsolete the protections afforded a debtor under 30-9A-608 and 30-9A-615. Kapor v. RJC Inv., Inc., 2019 MT 41, 394 Mont. 311, 434 P.3d 869.

CASES DECIDED PRIOR TO 1999 REVISION

Absence of Claim for Foreclosure of Security Interest — Award of Attorney Fees Improper: The Supreme Court vacated an award of attorney fees made pursuant to 30-9-511 (now repealed) in the absence of a claim regarding foreclosure of a security interest in personal property. Schulke v. Gemar, 264 M 184, 870 P2d 1378, 51 St. Rep. 220 (1994).

Stipulation by Parties Not Binding: In an action to foreclose a mortgage of real property or a security interest in personal property the court must allow as a part of the costs a reasonable attorney's fee which shall be fixed by the court notwithstanding any stipulation in the instrument of any agreement between the parties to the contrary. Stewart v. Casey, 182 M 185, 595 P2d 1176 (1979).

Tortious Conversion in Foreclosure: When a complaint alleged a tortious conversion against some defendants in a foreclosure action against another defendant, 30-9-511 (now repealed) was not applicable to the former. However, defendants in the alleged tortious conversion were entitled to attorney fees by virtue of 28-3-704, even though such action arose out of events that occurred prior to that section's effective date. Belgrade St. Bank v. Swainson, 172 M 350, 564 P2d 174 (1977).

Deficiency After Foreclosure: The provision for allowance of attorney's fees did not apply to an action in personam on the note after exhaustion of the security. Goggins v. Bookout, 141 M 449, 378 P2d 212 (1963).

Priority of Claim: The cost of extending abstract and attorney fees borne by mortgagee seeking foreclosure took priority over federal tax liens, which attached after the mortgage was in default. Streeter Bros. v. Overfelt, 202 F. Supp. 143 (D.C. Mont. 1962).

Defense Attorney's Fees: Section 30-9-511 (now repealed) making it incumbent upon the District Court in a mortgage foreclosure action to allow a reasonable attorney's fee applies as well to the fees of defense counsel when the action has been dismissed. Graham v. Superior Mines, 100 M 427, 49 P2d 443 (1935), distinguished in Valeo v. Tabish, 1999 MT 146, 295 M 34, 983 P2d 334, 56 St. Rep. 579 (1999).

Power of Sale in Mortgage: Where a chattel mortgage provides that in case of default in payment of the note secured, the mortgagee may have the property sold and out of the proceeds retain a reasonable attorney's fee, the only method of recovering it is by sale, and therefore the mortgagor may not assert that the fee intended was one to be fixed by the court in its discretion on institution of foreclosure proceedings. Nett v. Stockgrowers' Fin. Corp., 84 M 116, 274 P 497 (1929).

Evidence as to Fees: In fixing an attorney's fee in a foreclosure proceeding the District Court may consider the practice of the court and its own knowledge of the usual compensation for such services, and while it also may call to its aid attorneys as expert witnesses, it is not required to make its decision in accordance with their testimony. Bohan v. Harris, 71 M 495, 230 P 586 (1924).

Pleadings as to Fees: Under 30-9-511 (now repealed), the District Court must allow a reasonable attorney's fee in a foreclosure action, and with its determination in that respect the parties have nothing to do; hence allegations in the pleadings with reference thereto present no issues of fact and are surplusage. Bohan v. Harris, 71 M 495, 230 P 586 (1924).

30-9A-609. Secured party's right to take possession after default.

Official Comments

1. **Source.** Former Section 9-503 [30-9-503, now repealed].

2. **Secured Party's Right to Possession.** This section follows former Section 9-503 [30-9-503, now repealed] and earlier uniform legislation. It provides that the secured party is entitled to take possession of collateral after default.

3. **Judicial Process; Breach of Peace.** Subsection (b) [subsection (2)] permits a secured party to proceed under this section without judicial process if it does so "without breach of the peace." Although former Section 9-503 [30-9-503, now repealed] placed the same condition on a secured party's right to take possession of collateral, subsection (b) [subsection (2)] extends the condition to the right provided in subsection (a)(2) [subsection (1)(b)] as well. Like former Section 9-503 [30-9-503, now repealed], this section does not define or explain the conduct that will constitute a breach of the peace, leaving that matter for continuing development by the courts. In considering whether a secured party has engaged in a breach of the peace, however, courts should hold the secured party responsible for the actions of others taken on the secured party's behalf, including independent contractors engaged by the secured party to take possession of collateral.

This section does not authorize a secured party who repossesses without judicial process to utilize the assistance of a law-enforcement officer. A number of cases have held that a repossessing secured party's use of a law-enforcement officer without benefit of judicial process constituted a failure to comply with former Section 9-503 [30-9-503, now repealed].

4. **Damages for Breach of Peace.** Concerning damages that may be recovered based on a secured party's breach of the peace in connection with taking possession of collateral, see Section 9-625 [30-9A-625], Comment 3.

5. **Multiple Secured Parties.** More than one secured party may be entitled to take possession of collateral under this section. Conflicting rights to possession among secured parties are resolved by the priority rules of this Article [Title 30, chapter 9A]. Thus, a senior secured party is entitled to possession as against a junior claimant. Non-UCC law governs whether a junior secured party in possession of collateral is liable to the senior in conversion. Normally, a junior who refuses to relinquish possession of collateral upon the demand of a secured party having a superior possessory right to the collateral would be liable in conversion.

6. **Secured Party's Right to Disable and Dispose of Equipment on Debtor's Premises.** In the case of some collateral, such as heavy equipment, the physical removal from the debtor's plant and the storage of the collateral pending disposition may be impractical or unduly expensive. This section follows former Section 9-503 [30-9-503, now repealed] by providing that, in lieu of removal, the secured party may render equipment unusable or may dispose of collateral on the debtor's premises. Unlike former Section 9-503 [30-9-503, now repealed], however, this section explicitly conditions these rights on the debtor's default. Of course, this section does not validate unreasonable action by a secured party. Under Section 9-610 [30-9A-610], all aspects of a disposition must be commercially reasonable.

7. **Debtor's Agreement to Assemble Collateral.** This section follows former Section 9-503 [30-9-503, now repealed] also by validating a debtor's agreement to assemble collateral and make it available to a secured party at a place that the secured party designates. Similar to the treatment of agreements to permit collection prior to default under Section 9-607 [30-9A-607] and former 9-502 [30-9-502, now repealed], however, this section validates these agreements whether or not they are conditioned on the debtor's default. For example, a debtor might agree to make available to a secured party, from time to time, any instruments or negotiable documents that the debtor receives on account of collateral. A court should not infer from this section's validation that a debtor's agreement to assemble and make available collateral would not be enforceable under other applicable law.

8. **Agreed Standards.** Subject to the limitation imposed by Section 9-603(b) [30-9A-603(2)], this section's provisions concerning agreements to assemble and make available collateral and a secured party's right to disable equipment and dispose of collateral on a debtor's premises are likely topics for agreement on standards as contemplated by Section 9-603 [30-9A-603].

Case Notes

CASES DECIDED AFTER 1999 REVISION

Repossession of Collateral Pursuant to Uniform Commercial Code to Follow Judicial Procedures: A secured party that seeks to repossess collateral after default pursuant to 30-9A-609 of the Uniform Commercial Code must follow the specific, systematic judicial procedures provided in either the claim and delivery statutes in Title 27, ch. 17, or the prejudgment attachment statutes in Title 27, ch. 18, if applicable. Yellowstone Fed. Credit Union v. Daniels, 2008 MT 111, 342 M 451, 181 P3d 595 (2008).

Evidence of Malicious Attachment — Motion to Dismiss Properly Denied: In Spooner Constr. & Tree Serv., Inc. v. Maner, 2000 MT 161, 300 M 268, 3 P3d 641 (2000), it was held that plaintiff admitted no entitlement to any money from a logging agreement or any rental fees associated with defendant's use of a logging skidder. Nevertheless, plaintiff made no attempt to contact defendant to submit a bill, request payment, or discuss the logging contract, but instead, after disabling the skidder, plaintiff filed a lien against and later attached the skidder, with the intent to bid on it at a Sheriff's sale. Defendant presented both direct and circumstantial evidence that, without probable cause, plaintiff wrongfully attached the skidder with an improper motive and with reckless disregard for the facts, constituting a prima facie case of malicious wrongful attachment. Plaintiff's motion to dismiss was properly denied. Spooner Constr. & Tree Serv., Inc. v. Maner, 2003 MT 43, 314 M 268, 66 P3d 263 (2003).

CASES DECIDED PRIOR TO 1999 REVISION

Possession Upon Default: Debtor farmers brought suit against the Farmers Home Administration for alleged failure to properly notify farmers prior to disposing of collateral on debtor farmers' default. Under Montana law, a second creditor may take possession of loan collateral upon default without judicial process. Love v. U.S. 60 F3d 642 (9th Cir. 1995).

Lock Cutting Breach of Peace: The Supreme Court reversed the lower court's ruling that the defendant, Dorn Equipment Company, Inc., had not breached the peace when it cut a lock on the Martins' property to repossess certain farm equipment. The Supreme Court held that any form of forcible entry constitutes a breach of the peace. Martin v. Dorn Equip. Co., Inc., 250 M 422, 821 P2d 1025, 48 St. Rep. 978 (1991).

Obligations of Escrow Holder — Strict Adherence to Agreement: A bank acted as escrow agent in an agreement for the purchase of property. The escrow agreement provided that upon default, the seller was "entitled to the immediate return from the escrow agent of the contract for deed, warranty deeds and abstracts" in order to facilitate foreclosure. The agreement further held the escrow agent "liable only to account for the money received by it and for the delivery of the instruments and documents escrowed". The only obligation of the bank was to adhere strictly to the instructions in the agreement. The bank was not obligated to ascertain whether: (1) the demand for return of the documents was technically correct; (2) the notice of default to the buyer was legally sufficient; (3) performance of the contract was impossible; or (4) the contract and default notice were void for vagueness. Turbiville v. Hansen, 233 M 487, 761 P2d 389, 45 St. Rep. 1665 (1988).

Promissory Note Secured by Alleged Mortgage on Real Property as Well as Collateral — Writ of Attachment for Possession of Collateral Harmless Error: Defendants, who borrowed $5,000, claimed the District Court erred in issuing a Writ of Attachment when the promissory note was secured by an alleged mortgage on real property as well as other collateral. The Supreme Court found a grave question as to whether the wording of the note constituted a hypothecation for real estate mortgage purposes, but noted that the parties did not dispute a security interest in the other collateral. Under the Uniform Commercial Code, plaintiff as secured party had the right to take possession of the collateral upon default, and the alleged erroneous issuance of the Writ of Attachment to take possession of the collateral was harmless error. Montgomery v. Hunt, 227 M 279, 738 P2d 887, 44 St. Rep. 1081 (1987).

Defense: Action for breach of contract and conversion will not prevail where secured party had right to take possession and sell security interest on default. Fairchild v. Williams Feed, Inc., 169 M 18, 544 P2d 1216 (1976).

30-9A-610. Disposition of collateral after default.

Official Comments

1. **Source.** Former Section 9-504(1), (3) [30-9-504(1), (3), now repealed].

2. **Commercially Reasonable Dispositions.** Subsection (a) [subsection (1)] follows former Section 9-504 [30-9-504, now repealed] by permitting a secured party to dispose of collateral in

a commercially reasonable manner following a default. Although subsection (b) [subsection (2)] permits both public and private dispositions, including public and private dispositions conducted over the Internet, "every aspect of a disposition . . . must be commercially reasonable." This section encourages private dispositions on the assumption that they frequently will result in higher realization on collateral for the benefit of all concerned. Subsection (a) [subsection (1)] does not restrict dispositions to sales; collateral may be sold, leased, licensed, or otherwise disposed. Section 9-627 [30-9A-627] provides guidance for determining the circumstances under which a disposition is "commercially reasonable."

3. **Time of Disposition.** This Article [Title 30, chapter 9A] does not specify a period within which a secured party must dispose of collateral. This is consistent with this Article's [Title 30, chapter 9A] policy to encourage private dispositions through regular commercial channels. It may, for example, be prudent not to dispose of goods when the market has collapsed. Or, it might be more appropriate to sell a large inventory in parcels over a period of time instead of in bulk. Of course, under subsection (b) [subsection (2)] every aspect of a disposition of collateral must be commercially reasonable. This requirement explicitly includes the "method, manner, time, place and other terms." For example, if a secured party does not proceed under Section 9-620 [30-9A-620] and holds collateral for a long period of time without disposing of it, and if there is no good reason for not making a prompt disposition, the secured party may be determined not to have acted in a "commercially reasonable" manner. See also Section 1-203 [30-1-203] (general obligation of good faith).

4. **Pre-Disposition Preparation and Processing.** Former Section 9-504(1) [30-9-504(1), now repealed] appeared to give the secured party the choice of disposing of collateral either "in its then condition or following any commercially reasonable preparation or processing." Some courts held that the "commercially reasonable" standard of former Section 9-504(3) [30-9-504(3), now repealed] nevertheless could impose an affirmative duty on the secured party to process or prepare the collateral prior to disposition. Subsection (a) [subsection (1)] retains the substance of the quoted language. Although courts should not be quick to impose a duty of preparation or processing on the secured party, subsection (a) [subsection (1)] does not grant the secured party the right to dispose of the collateral "in its then condition" under all circumstances. A secured party may not dispose of collateral "in its then condition" when, taking into account the costs and probable benefits of preparation or processing and the fact that the secured party would be advancing the costs at its risk, it would be commercially unreasonable to dispose of the collateral in that condition.

5. **Disposition by Junior Secured Party.** Disposition rights under subsection (a) [subsection (1)] are not limited to first-priority security interests. Rather, any secured party as to whom there has been a default enjoys the right to dispose of collateral under this subsection. The exercise of this right by a secured party whose security interest is subordinate to that of another secured party does not of itself constitute a conversion or otherwise give rise to liability in favor of the holder of the senior security interest. Section 9-615 [30-9A-615] addresses application of the proceeds of a disposition by a junior secured party. Under Section 9-615(a) [30-9A-615(1)], a junior secured party owes no obligation to apply the proceeds of disposition to the satisfaction of obligations secured by a senior security interest. Section 9-615(g) [30-9A-615(7)] builds on this general rule by protecting certain juniors from claims of a senior concerning cash proceeds of the disposition. Even if a senior were to have a non-Article 9 [Title 30, chapter 9A] claim to proceeds of a junior's disposition, Section 9-615(g) [30-9A-615(7)] would protect a junior that acts in good faith and without knowledge that its actions violate the rights of a senior party. Because the disposition by a junior would not cut off a senior's security interest or other lien (see Section 9-617 [30-9A-617]), in many (probably most) cases the junior's receipt of the cash proceeds would not violate the rights of the senior.

The holder of a senior security interest is entitled, by virtue of its priority, to take possession of collateral from the junior secured party and conduct its own disposition, provided that the senior enjoys the right to take possession of the collateral from the debtor. See Section 9-609 [30-9A-609]. The holder of a junior security interest normally must notify the senior secured party of an impending disposition. See Section 9-611 [30-9A-611]. Regardless of whether the senior receives a notification from the junior, the junior's disposition does not of itself discharge the senior's security interest. See Section 9-617 [30-9A-617]. Unless the senior secured party has authorized the disposition free and clear of its security interest, the senior's security interest ordinarily will survive the disposition by the junior and continue under Section 9-315(a) [30-9A-315(1)]. If the senior enjoys the right to repossess the collateral from the debtor, the senior likewise may recover the collateral from the transferee.

When a secured party's collateral is encumbered by another security interest or other lien, one of the claimants may seek to invoke the equitable doctrine of marshaling. As explained by the Supreme Court, that doctrine "rests upon the principle that a creditor having two funds to satisfy his debt, may not by his application of them to his demand, defeat another creditor, who may resort to only one of the funds." Meyer v. United States, 375 U.S. 233, 236 (1963), quoting Sowell v. Federal Reserve Bank, 268 U.S. 449, 456-57 (1925). The purpose of the doctrine is "to prevent the arbitrary action of a senior lienor from destroying the rights of a junior lienor or a creditor having less security." Id. at 237. Because it is an equitable doctrine, marshaling "is applied only when it can be equitably fashioned as to all of the parties" having an interest in the property. Id. This Article [Title 30, chapter 9A] leaves courts free to determine whether marshaling is appropriate in any given case. See Section 1-103 [30-1-103].

6. **Security Interests of Equal Rank.** Sometimes two security interests enjoy the same priority. This situation may arise by contract, e.g., pursuant to "equal and ratable" provisions in indentures, or by operation of law. See Section 9-328(6) [30-9A-328(6)]. This Article [Title 30, chapter 9A] treats a security interest having equal priority like a senior security interest in many respects. Assume, for example, that SP-X and SP-Y enjoy equal priority, SP-W is senior to them, and SP-Z is junior. If SP-X disposes of the collateral under this section, then (i) SP-W's and SP-Y's security interests survive the disposition but SP-Z's does not, see Section 9-617 [30-9A-617], and (ii) neither SP-W nor SP-Y is entitled to receive a distribution of proceeds, but SP-Z is. See Section 9-615(a)(3) [30-9A-615(1)(c)].

When one considers the ability to obtain possession of the collateral, a secured party with equal priority is unlike a senior secured party. As the senior secured party, SP-W should enjoy the right to possession as against SP-X. See Section 9-609 [30-9A-609], Comment 5. If SP-W takes possession and disposes of the collateral under this section, it is entitled to apply the proceeds to satisfy its secured claim. SP-Y, however, should not have such a right to take possession from SP-X; otherwise, once SP-Y took possession from SP-X, SP-X would have the right to get possession from SP-Y, which would be obligated to redeliver possession to SP-X, and so on. Resolution of this problem is left to the parties and, if necessary, the courts.

7. **Public vs. Private Dispositions.** This Part [Title 30, chapter 9A, part 6] maintains two distinctions between "public" and other dispositions: (i) the secured party may buy at the former, but normally not at the latter (Section 9-610(c) [30-9A-610(3)]), and (ii) the debtor is entitled to notification of "the time and place of a public disposition" and notification of "the time after which" a private disposition or other intended disposition is to be made (Section 9-613(1)(E) [30-9A-613(1)(a)(v)]). It does not retain the distinction under former Section 9-504(4) [30-9-504(4), now repealed], under which transferees in a noncomplying public disposition could lose protection more easily than transferees in other noncomplying dispositions. Instead, Section 9-617(b) [30-9A-617(2)] adopts a unitary standard. Although the term is not defined, as used in this Article [Title 30, chapter 9A], a "public disposition" is one at which the price is determined after the public has had a meaningful opportunity for competitive bidding. "Meaningful opportunity" is meant to imply that some form of advertisement or public notice must precede the sale (or other disposition) and that the public must have access to the sale (disposition).

A secured party's purchase of collateral at its own private disposition is equivalent to a "strict foreclosure" and is governed by Sections 9-620 [30-9A-620], 9-621 [30-9A-621], and 9-622 [30-9A-622]. The provisions of these sections can be waived only to the extent provided in Section 9-624(b) [30-9A-624(2)]. See Section 9-602 [30-9A-602].

8. **Investment Property.** Dispositions of investment property may be regulated by the federal securities laws. Although a "public" disposition of securities under this Article [Title 30, chapter 9A] may implicate the registration requirements of the Securities Act of 1933, it need not do so. A disposition that qualifies for a "private placement" exemption under the Securities Act of 1933 nevertheless may constitute a "public" disposition within the meaning of this section. Moreover, the "commercially reasonable" requirements of subsection (b) [subsection (2)] need not prevent a secured party from conducting a foreclosure sale without the issuer's compliance with federal registration requirements.

9. **"Recognized Market."** A "recognized market," as used in subsection (c) [subsection (3)] and Section 9-611(d) [30-9A-611(4)], is one in which the items sold are fungible and prices are not subject to individual negotiation. For example, the New York Stock Exchange is a recognized market. A market in which prices are individually negotiated or the items are not fungible is not a recognized market, even if the items are the subject of widely disseminated price guides or are disposed of through dealer auctions.

10. **Relevance of Price.** While not itself sufficient to establish a violation of this Part [Title 30, chapter 9A, part 6], a low price suggests that a court should scrutinize carefully all aspects of a disposition to ensure that each aspect was commercially reasonable. Note also that even if the disposition is commercially reasonable, Section 9-615(f) [30-9A-615(6)] provides a special method for calculating a deficiency or surplus if (i) the transferee in the disposition is the secured party, a person related to the secured party, or a secondary obligor, and (ii) the amount of proceeds of the disposition is significantly below the range of proceeds that a complying disposition to a person other than the secured party, a person related to the secured party, or a secondary obligor would have brought.

11. **Warranties.** Subsection (d) [subsection (4)] affords the transferee in a disposition under this section the benefit of any title, possession, quiet enjoyment, and similar warranties that would have accompanied the disposition by operation of non-Article 9 [Title 30, chapter 9A] law had the disposition been conducted under other circumstances. For example, the Article 2 [Title 30, chapter 2] warranty of title would apply to a sale of goods, the analogous warranties of Article 2A [Title 30, chapter 2A] would apply to a lease of goods, and any common-law warranties of title would apply to dispositions of other types of collateral. See, e.g., Restatement (2d), Contracts § 333 (warranties of assignor).

Subsection (e) [subsection (5)] explicitly provides that these warranties can be disclaimed either under other applicable law or by communicating a record containing an express disclaimer. The record need not be written, but an oral communication would not be sufficient. See Section 9-102 [30-9A-102] (definition of "record"). Subsection (f) [subsection (6)] provides a sample of wording that will effectively exclude the warranties in a disposition under this section, whether or not the exclusion would be effective under non-Article 9 [Title 30, chapter 9A] law.

The warranties incorporated by subsection (d) [subsection (4)] are those relating to "title, possession, quiet enjoyment, and the like." Depending on the circumstances, a disposition under this section also may give rise to other statutory or implied warranties, e.g., warranties of quality or fitness for purpose. Law other than this Article [Title 30, chapter 9A] determines whether such other warranties apply to a disposition under this section. Other law also determines issues relating to disclaimer of such warranties. For example, a foreclosure sale of a car by a car dealer could give rise to an implied warranty of merchantability (Section 2-314 [30-2-314]) unless effectively disclaimed or modified (Section 2-316 [30-2-316]).

This section's approach to these warranties conflicts with the former Comment to Section 2-312 [30-2-312]. This Article [Title 30, chapter 9A] rejects the baseline assumption that commercially reasonable dispositions under this section are out of the ordinary commercial course or peculiar. The Comment to Section 2-312 [30-2-312] has been revised accordingly.

Case Notes

CASES DECIDED AFTER 1999 REVISION

Security Interest Terminated — Creditor's Obligations Under U.C.C. Chapter 9A Not Terminated: The debtors entered an installment contract to buy a mobile home from the sellers. They became delinquent on monthly payments, and eventually the seller invoked the acceleration clause and demanded the outstanding balance due plus notice fees. The debtors returned the mobile home to the seller, who sold it to a new buyer 2 months later. The Supreme Court found that although the seller's disposition of the mobile home terminated the security interest under 30-9A-617, the seller's obligations as a creditor under Title 30, ch. 9A, remained, including the obligation to give the debtor notice of how the creditor intends to dispose of the collateral under 30-9A-611 and 30-9A-614, the obligation to conduct a commercially reasonable resale of the collateral under 30-9A-610, and the obligation to account to the debtor for any surplus realized from the sale of the collateral under 30-9A-608, 30-9A-615, 30-9A-616, and 30-9A-626. Christman v. Clause, 2019 MT 132, 396 Mont. 142, 443 P.3d 472.

Secured Party Entitled to Book of Business — Contracts Analyzed — Secured Interest Survived Termination of Prior Business — Insurance Company Liable for Conversion for Taking Book of Business From Secured Party: The defendant, an exclusive insurance agent for the plaintiff insurance company, sold her business to another agent and retained an economic interest as a secured creditor in the book of business. The purchasing agent was approved by the insurance company, but the insurance company terminated the relationship when the purchasing agent falsified an insurance claim. The insurance company then parked the book of business at another insurance agency and filed a complaint in interpleader to determine the rights of the parties to a contractual termination payment that was elected by the purchasing agent. In District Court, the defendant argued that she had a right to the termination payment, ongoing commissions generated by the policies, an economic interest in the agency book of business, and proceeds under 30-9A-315, while the insurance company argued that under 30-9A-203, the security interest terminated when the insurance company made the termination payment. The District Court held that the defendant retained no security interest in the book of business sold to the purchasing agent. On appeal, the Supreme Court reversed the District Court after analyzing the terms of the contracts between the parties. The court held that the defendant's position in holding an economic interest in the book of business, having the right as a secured creditor to possess the book of business upon default of the purchasing agent, and the insurance company's unauthorized control over the book of business by excluding it from the defendant after the purchasing agent's default satisfied the liability elements of conversion. Allstate Ins. Co. v. Posnien, Inc., 2015 MT 162, 379 Mont. 398, 352 P.3d 1.

CASES DECIDED PRIOR TO 1999 REVISION

Determination of Commercially Reasonable Sale — Obligation of Seller to Protect Rights of Debtor — $150 for Sale of Car Held Not Reasonable Fair Market Value: The Longs purchased a Ford Escort from Auto Credit for $2,795, made timely payments, put 3,500 miles on the car, and returned it to Auto Credit 6 weeks after purchase, notifying Auto Credit that they would be making no more payments on the car. At the time that the car was returned to Auto Credit, the balance owed by the Longs was $2,594.02. Auto Credit notified the Longs that if they failed to make further payments, the car would be sold the next business day after June 27, 1992. The car was eventually sold August 12, 1992, at a private sale for $150. After credit for that amount and deduction of its expenses, Auto Credit calculated that the Longs owed $2,934.15. Auto Credit brought an action to recover the amount owed, and the Longs counterclaimed for damages on the basis that the sale was not commercially reasonable and that Auto Credit had violated the federal Truth in Lending Act. The Supreme Court reviewed its previous opinions holding that a low price obtained for the sale of loan collateral does not alone establish that the sale was commercially unreasonable and that reasonableness is determined on a case-by-case basis. The Supreme Court also noted that Montana, unlike some other jurisdictions, has not held that a seller has an express obligation to protect the debtor's interests. However, the Supreme Court held that "collateral cannot be disposed of, as it was in this case, in total disregard of the debtor's interests". The court further held that: (1) the fact that Auto Credit secured the $2,795 transaction with the vehicle as collateral serves as an admission of the value of the vehicle; (2) there is nothing in the record showing that the vehicle had mechanical difficulty when turned back to Auto Credit or that the 3,500 miles put on the vehicle by the Longs diminished its value by 95%, and therefore the sale for $150 did not represent reasonable fair market value for the car; (3) commercial unreasonableness is also demonstrated by the fact that after the sale, the Longs owed more to Auto Credit than they did before the sale and that the Longs would therefore have been better off destroying the vehicle, a result that is contrary to the requirements of the Uniform Commercial Code that the sale be conducted in a manner that takes into account the interests of both parties to the contract; and (4) depending upon the facts of the case, the price received for the collateral may provide prima facie evidence of whether the sale was reasonable and protected the rights of the debtor. Auto Credit, Inc. v. Long, 1998 MT 327, 292 M 238, 971 P2d 1237, 55 St. Rep. 1326 (1998).

Notice Exception — Commercial Reasonableness in Sale of Horses: Section 30-9-504 (now repealed, see 30-9A-610, 30-9A-611, 30-9A-615, 30-9A-617, 30-9A-618, and 30-9A-624) requires the secured party to give the debtor reasonable notice of the time after which any private sale is to be made unless the collateral is perishable or threatens to decline speedily in value. In this case, when the collateral was thoroughbred horses, private sale was commercially reasonable in light of expert testimony that the private sale of horses often results in higher prices than sale by public auction. The notice requirement was inapplicable because the price of thoroughbred horses dropped rapidly during the time when the sale was to occur. In re Estate of Michael v. Glacier Gen. Assurance Co., 264 M 261, 871 P2d 272, 51 St. Rep. 252 (1994), distinguishing Agricredit Acceptance Corp. v. Michels, 250 M 23, 817 P2d 704 (1991).

Commercial Reasonableness of Notification of Sale: It is not required that a debtor receive actual notice of a sale, only that the creditor take reasonable steps to assure that the debtor is notified. When a bank sent notice to defendant at his last-known address, the bank satisfied the statutory requirements for notice. First Nat'l Bank of Lewistown v. Mork, 257 M 495, 850 P2d 954, 50 St. Rep. 379 (1993).

Denial of Directed Verdict Proper — Sufficient Evidence to Create Question of Whether U.C.C. Notice Given: Defendant, Tezak, moved for a directed verdict on the basis that he was told by plaintiff's attorney to ignore the notice that his repossessed trucks were to be sold. The Supreme Court affirmed the lower court's denial of the motion, stating that there was sufficient evidence to let the jury decide if Tezak's right to ignore the notice was conditional. Mack Financial Corp. v. Tezak, 253 M 492, 834 P2d 396, 49 St. Rep. 556 (1992).

Failure to Consider Affidavit of Expert on Value of Farm Equipment — Question of Whether Sales Were Commercially Reasonable as Precluding Summary Judgment: The District Court granted summary judgment to creditor who sold farm equipment to satisfy deficiencies, finding that the sales were commercially reasonable because the creditor properly notified debtor Michels of the pending sales pursuant to 30-9-504 (now repealed, see 30-9A-610, 30-9A-611, 30-9A-615, 30-9A-617, 30-9A-618, and 30-9A-624). In opposing summary judgment, Michels submitted the affidavit of a former farm implement dealer who was familiar with the equipment and who testified that the amount sought through the sales was far below the value of the equipment. The affidavit raised a genuine issue of material fact concerning whether the sales were commercially reasonable that was sufficient to constitute error in the grant of summary judgment. Agricredit Acceptance Corp. v. Michels, 250 M 23, 817 P2d 704, 48 St. Rep. 874 (1991).

Court Amending Special Verdict Not Error: The jury returned a special verdict, finding that the defendant had breached a car purchase contract and that the plaintiff had acted reasonably in repossessing and reselling the vehicle. The verdict awarded the plaintiff only $22 for the notice of sale publication costs. The lower court amended the verdict to include court costs, attorney fees, and the balance due under the contract. The Supreme Court held that amending the verdict was not error because once the jury decided that the plaintiff had acted in a commercially reasonable manner, a judgment for any deficiency followed as a matter of law. Sportco, Inc. v. Thompson, 247 M 379, 806 P2d 1039, 48 St. Rep. 236 (1991).

Effective Notice of Repossession: The defendants argued that the notice of repossession sent them by the plaintiff was not sufficient. The Supreme Court held that the notice was more than adequate because it contained the name of the prospective buyer and the price, both of which were not required by the statute. Lilly v. Terwilliger, 244 M 93, 796 P2d 199, 47 St. Rep. 1413 (1990).

Sale of Fishing Business Commercially Reasonable: The plaintiff failed to advertise, solicit bids, or secure an appraisal before selling a fishing business he had repossessed from the defendants. The Supreme Court held that the sale price was reasonable because the evidence showed that the fishing season was imminent and the plaintiff had to act quickly and that the state of the business was such that the defendants were unable to make even modest payments. Lilly v. Terwilliger, 244 M 93, 796 P2d 199, 47 St. Rep. 1413 (1990).

Equipment Sale — No Surplus: Under the authority of 30-9-504 (now repealed, see 30-9A-610, 30-9A-611, 30-9A-615, 30-9A-617, 30-9A-618, and 30-9A-624), the secured parties properly disposed of certain printing equipment by selling it in a commercially reasonable manner and applying the proceeds to the indebtedness secured by the security interest. No surplus proceeds remained to distribute to the defaulting debtor. Gay v. Cabinet Publishing, Inc., 239 M 179, 779 P2d 77, 46 St. Rep. 1601 (1989).

Commercial Reasonableness of Agisters' Lien Sale: Appellants claimed the sale of horses at an agisters' lien sale was not commercially reasonable because the horses were sold in lots at less than their value. Looking to 30-9-507 (now repealed, see 30-9A-625 and 30-9A-627) for guidance, the Supreme Court stated that the sale of horses at a low price in lots instead of individually did not make the sale commercially unreasonable. Testimony indicated that horses were often sold in this manner and could have been sold individually if a bidder had so requested. Rose v. Myers, 223 M 13, 724 P2d 176, 43 St. Rep. 1493 (1986).

Unreasonable Notice — Wrong Date — No Notice of Sealed Bids — No Notice of Certain Sales: Plaintiff defaulted on two bank loans, and bank sold the livestock, farm machinery, and equipment put up as collateral, then obtained a deficiency judgment for the remainder of the debt. The judgment was reversed, and the bank could not recover the deficiency. The bank sold half the machinery and equipment upon a notice to the plaintiff which gave the wrong auction date and failed to state that sealed bids were to be submitted. This was not a commercially reasonable notice, and neither notices published in newspapers nor notice posted in the bank's lobby constituted sufficient notice. The remainder of the equipment and machinery was later sold with no notice whatsoever to plaintiff. Bank of Sheridan v. Devers, 217 M 173, 702 P2d 1388, 42 St. Rep. 1107 (1985). See also Westmont Tractor Co. v. Leighty, 222 M 336, 722 P2d 617, 43 St. Rep. 1309 (1986), and Auto Credit, Inc. v. Long, 1998 MT 327, 292 M 238, 971 P2d 1237, 55 St. Rep. 1326 (1998).

Failure to Give Required Notice of Sale of Collateral — Deficiency Judgment Precluded: Plaintiffs defaulted on loan. Pursuant to an order of the Blackfeet Tribal Court enforceable in the Montana courts as a matter of comity, the creditor sold the collateral and applied the proceeds to the amount due, leaving a deficiency. The loan agreement required notice of sale of collateral to be given at least 5 days before the sale and to state the time and place of the sale. The notice stated neither the time nor the place. This failure of notice precluded the creditor from obtaining a deficiency judgment in the Montana courts. Wippert v. The Blackfeet Tribe of the Blackfeet Indian Reservation, 215 M 85, 695 P2d 461, 42 St. Rep. 200 (1985), overruled in part on other grounds by Green v. Gerber, 2013 MT 35, 369 Mont. 20, 303 P.3d 729. See also Westmont Tractor Co. v. Continental I, Inc., 224 M 516, 731 P2d 327, 43 St. Rep. 2380 (1986).

Foreclosure by Secured Party Who Is Also Escrow Agent: Plaintiff bought a photography business and executed a promissory note with defendant. As collateral he assigned stock in the business. Plaintiff sold the business to Wolfe. Wolfe was to make payments to defendant to discharge his obligations, and these payments were to be directly applied to plaintiff's obligation under the promissory note. Defendant was escrow agent. Plaintiff later signed a financing statement granting defendant a security interest in the stock held in escrow. The defendant filed the security agreement. Wolfe became delinquent in his payments, and defendant notified plaintiff his payments were therefore delinquent. A later letter was sent by certified mail to the same address advising plaintiff the stock would be sold and applied to plaintiff's past-due loan. At the sale Wolfe bought the stock for the amount due on plaintiff's note. Plaintiff claimed defendant had breached its fiduciary duty by foreclosing on the stock. The security interest became binding before the parties entered the escrow agreement. The security interest continued in the collateral notwithstanding the sale to Wolfe. Upon default defendant acted within its statutory rights to foreclose on the collateral to satisfy plaintiff's obligation. The escrow arrangement did not prevent defendant as a secured party from exercising its rights to foreclose on collateral on which the debtor defaulted. Dulan v. Mont. Nat'l Bank of Roundup, 203 M 177, 661 P2d 28, 40 St. Rep. 376 (1983), followed in Weldon v. First Citizens Bank of Billings, 259 M 305, 856 P2d 225, 50 St. Rep. 807 (1993).

Price Discrepancy Bearing on Commercial Reasonableness: Plaintiff bought a photography business and executed a promissory note with defendant. As collateral he assigned stock in the business. Plaintiff sold the business to Wolfe. Wolfe was to make payments to defendant to discharge his obligations, and these payments were to be directly applied to plaintiff's obligation under the promissory note. Defendant was escrow agent. Plaintiff later signed a financing statement granting defendant a security interest in the stock held in escrow. The defendant filed the security agreement. Wolfe became delinquent in his payments, and defendant notified plaintiff his payments were therefore delinquent. A later letter was sent by certified mail to the same address advising plaintiff the stock would be sold and applied to plaintiff's past-due loan. At the sale Wolfe bought the stock for the amount due on plaintiff's note. Plaintiff contended the sale of the collateral was not conducted in a commercially reasonable manner as indicated by the low price received. The Supreme Court held that a large discrepancy in price may be considered in determining commercial reasonableness but that the complaining party has the burden of showing the price received was less than the fair market value of the collateral. The court did not find substantial evidence to support the contention. Dulan v. Mont. Nat'l Bank of Roundup, 203 M 177, 661 P2d 28, 40 St. Rep. 376 (1983), followed in Owen v. Ostrum, 259 M 249, 855 P2d 1015, 50 St. Rep. 779 (1993). See also Auto Credit, Inc. v. Long, 1998 MT 327, 292 M 238, 971 P2d 1237, 55 St. Rep. 1326 (1998).

Reasonable Steps to Notify: Plaintiff bought a photography business and executed a promissory note with defendant. As collateral he assigned stock in the business. Plaintiff sold the business to Wolfe. Wolfe was to make payments to defendant to discharge his obligations, and these payments were to be directly applied to plaintiff's obligation under the promissory note. Defendant was escrow agent. Plaintiff later signed a financing statement granting defendant a security interest in the stock held in escrow. The defendant filed the security agreement. Wolfe became delinquent in his payments, and defendant notified plaintiff his payments were therefore delinquent. A later letter was sent by certified mail to the same address advising plaintiff the stock would be sold and applied to plaintiff's past-due loan. At the sale Wolfe bought the stock for the amount due on plaintiff's note. Plaintiff contended that notice of the foreclosure was deficient because he had moved and had not received the letter. The Supreme Court held that a creditor must only take reasonable steps to notify the debtor. Plaintiff received notice when the letter was delivered to the address. The actions of defendant were those reasonably required to notify plaintiff. Dulan v. Mont. Nat'l Bank of Roundup, 203 M 177, 661 P2d 28, 40 St. Rep. 376 (1983).

Repossession Not Required of Secured Creditor as Condition Precedent to Judgment Against Other Property: The defendant defaulted on a secured loan from the plaintiff, and the plaintiff, rather than repossessing the defendant's personal property in which it had been given a security interest, obtained a judgment against the defendant for the amount owed and brought a declaratory judgment action to determine if the judgment constituted a lien on the defendant's real property. The Supreme Court reversed the District Court's ruling that there was no effective lien, holding that the plaintiff was not required to first repossess the secured property and then sue for the deficiency. AVCO Financial Serv. of Billings One, Inc. v. Christiaens, 201 M 117, 651 P2d 220, 39 St. Rep. 1993 (1982).

Proving Commercial Reasonableness: The burden of proving the commercial reasonableness of the disposition of collateral is on the secured party. Farmers St. Bank v. Mobile Homes Unlimited, 181 M 342, 593 P2d 734 (1979). See also Auto Credit, Inc. v. Long, 1998 MT 327, 292 M 238, 971 P2d 1237, 55 St. Rep. 1326 (1998).

Failure to Give Notice: A secured creditor's failure to give the notice required under 30-9-504 (now repealed, see 30-9A-610, 30-9A-611, 30-9A-615, 30-9A-617, 30-9A-618, and 30-9A-624) prior to disposition of collateral precludes or limits the creditor's right to recover a deficiency judgment. Farmers St. Bank v. Mobile Homes Unlimited, 181 M 342, 593 P2d 734 (1979), followed in Ottersen v. Rubick, 246 M 93, 803 P2d 1066, 47 St. Rep. 2274 (1990). See also Owen v. Ostrum, 259 M 249, 855 P2d 1015, 50 St. Rep. 779 (1993).

Guaranties Covering Costs and Expenses: Language in guaranty agreement referring to recovery of attorney fees incidental to collection of debt from the principal debtor did not authorize recovery of attorney fees from guarantors who were sued to recover deficiency after repossession and sale of collateral. First Nat'l Park Bank v. Johnson, 553 F2d 599 (1977), distinguished in Westmont Tractor Co. v. Continental I, Inc., 224 M 516, 731 P2d 327, 43 St. Rep. 2380 (1986).

Guaranty Distinguished From Other Contracts: Guarantors are not "debtors" within meaning of section of Uniform Commercial Code prohibiting waiver of rules granting rights to debtor and imposing duties on the secured party. First Nat'l Park Bank v. Johnson, 553 F2d 599 (1977), distinguished in Westmont Tractor Co. v. Continental I, Inc., 224 M 516, 731 P2d 327, 43 St. Rep. 2380 (1986).

Possession as Defense: Action for breach of contract and conversion will not prevail where secured party had right to take possession and sell security interest on default. Fairchild v. Williams Feed, Inc., 169 M 18, 544 P2d 1216 (1976).

Notice: Oral notice to debtor of time and, in case of public sale, place of disposition of goods after foreclosure is sufficient under 30-9-504(3) (section now repealed, see 30-9A-610, 30-9A-611, 30-9A-615, 30-9A-617, 30-9A-618, and 30-9A-624). Fairchild v. Williams Feed, Inc., 169 M 18, 544 P2d 1216 (1976), followed in Schulke v. Gemar, 264 M 184, 870 P2d 1378, 51 St. Rep. 220 (1994).

Sale as a Unit Not Unreasonable: Indication that a better price could have been received at foreclosure sale of a mountain logger, if it had been sold for parts, was not evidence that the sale was unreasonable, since the Uniform Commercial Code does not require the secured creditor to disassemble the collateral and sell it piece by piece. James Talcott, Inc. v. Reynolds, 165 M 404, 529 P2d 352 (1974).

Commercially Reasonable Disposition of Property: Sale of business machinery at private sale for $300 was not commercially unreasonable where guarantors of lease were given advance notice of the sale and declined to bid over $300 for the property; that one of the business machines was later placed on sale to the public for $295 failed to show the sale to be commercially unreasonable since the increase in price was normal, taking into account the expenses of preparation for sale and the commercial markup common to the particular trade. Business Fin. Co., Inc. v. Red Barn, Inc., 163 M 263, 517 P2d 383 (1973).

30-9A-611. Notification before disposition of collateral.

Official Comments

1. **Source.** Former Section 9-504(3) [30-9A-504(3), now repealed].

2. **Reasonable Notification.** This section requires a secured party who wishes to dispose of collateral under Section 9-610 [30-9A-610] to send "a reasonable authenticated notification of disposition" to specified interested persons, subject to certain exceptions. The notification must be reasonable as to the manner in which it is sent, its timeliness (i.e., a reasonable time before the disposition is to take place), and its content. See Sections 9-612 [30-9A-612] (timeliness of notification), 9-613 [30-9A-613] (contents of notification generally), 9-614 [30-9A-614] (contents of notification in consumer-goods transactions).

3. **Notification to Debtors and Secondary Obligors.** This section imposes a duty to send notification of a disposition not only to the debtor but also to any secondary obligor. Subsections (b) and (c) [subsections (2) and (3)] resolve an uncertainty under former Article 9 [Title 30, chapter 9, now repealed] by providing that secondary obligors (sureties) are entitled to receive notification of an intended disposition of collateral, regardless of who created the security interest in the collateral. If the surety created the security interest, it would be the debtor. If it did not, it would be a secondary obligor. (This Article [Title 30, chapter 9A] also resolves the question of the secondary obligor's ability to waive, pre-default, the right to notification-waiver generally is not permitted. See Section 9-602 [30-9A-602].) Section 9-605 [30-9A-605] relieves a secured party from any duty to send notification to a debtor or secondary obligor unknown to the secured party.

Under subsection (b) [subsection (2)], the principal obligor (borrower) is not always entitled to notification of disposition.

Example: Behnfeldt borrows on an unsecured basis, and Bruno grants a security interest in her car to secure the debt. Behnfeldt is a primary obligor, not a secondary obligor. As such, she is not entitled to notification of disposition under this section.

4. **Notification to Other Secured Parties.** Prior to the 1972 amendments to Article 9 [Title 30, chapter 9A], former Section 9-504(3) [30-9-504(3), now repealed] required the enforcing secured party to send reasonable notification of the disposition:

except in the case of consumer goods to any other person who has a security interest in the collateral and who has duly filed a financing statement indexed in the name of the debtor in this State or who is known by the secured party to have a security interest in the collateral.

The 1972 amendments eliminated the duty to give notice to secured parties other than those from whom the foreclosing secured party had received written notice of a claim of an interest in the collateral.

Many of the problems arising from dispositions of collateral encumbered by multiple security interests can be ameliorated or solved by informing all secured parties of an intended disposition and affording them the opportunity to work with one another. To this end, subsection (c)(3)(B) [subsection (3)(c)(ii)] expands the duties of the foreclosing secured party to include the duty to notify (and the corresponding burden of searching the files to discover) certain competing secured parties. The subsection imposes a search burden that in some cases may be greater than the pre-1972 burden on foreclosing secured parties but certainly is more modest than that faced by a new secured lender.

To determine who is entitled to notification, the foreclosing secured party must determine the proper office for filing a financing statement as of a particular date, measured by reference to the "notification date," as defined in subsection (a) [subsection (1)]. This determination requires reference to the choice-of-law provisions of Part 3 [Title 30, chapter 9A, part 3]. The secured party must ascertain whether any financing statements covering the collateral and indexed under the debtor's name, as the name existed as of that date, in fact were filed in that office. The foreclosing secured party generally need not notify secured parties whose effective financing statements have become more difficult to locate because of changes in the location of the debtor, proceeds rules, or changes in the name that is sufficient as the name of the debtor under Section 9-503(a) [30-9A-503(1)].

Under subsection (c)(3)(C) [subsection (3)(c)(iii)], the secured party also must notify a secured party who has perfected a security interest by complying with a statute or treaty described in Section 9-311(a) [30-9A-311(1)], such as a certificate-of-title statute.

Subsection (e) [subsection (5)] provides a "safe harbor" that takes into account the delays that may be attendant to receiving information from the public filing offices. It provides, generally, that the secured party will be deemed to have satisfied its notification duty under subsection (c)(3)(B) [subsection (3)(c)(ii)] if it requests a search from the proper office at least 20 but not more than 30 days before sending notification to the debtor and if it also sends a notification to all secured parties (and other lienholders) reflected on the search report. The secured party's duty under subsection (c)(3)(B) [subsection (3)(c)(ii)] also will be satisfied if the secured party requests but does not receive a search report before the notification is sent to the debtor. Thus, if subsection (e) [subsection (5)] applies, a secured party who is entitled to notification under subsection (c)(3)(B) [subsection (3)(c)(ii)] has no remedy against a foreclosing secured party who does not send the notification. The foreclosing secured party has complied with the notification requirement. Subsection (e) [subsection (5)] has no effect on the requirements of the other paragraphs of subsection (c) [subsection (3)]. For example, if the foreclosing secured party received a notification from the holder of a conflicting security interest in accordance with subsection (c)(3)(A) [subsection (3)(c)(i)] but failed to send to the holder a notification of the disposition, the holder of the conflicting security interest would have the right to recover any loss under Section 9-625(b) [30-9A-625(2)].

5. **Authentication Requirement.** Subsections (b) and (c) [subsections (2) and (3)] explicitly provide that a notification of disposition must be "authenticated." Some cases read former Section 9-504(3) [30-9-504(3), now repealed] as validating oral notification.

6. **Second Try.** This Article [Title 30, chapter 9A] leaves to judicial resolution, based upon the facts of each case, the question whether the requirement of "reasonable notification" requires a "second try," i.e., whether a secured party who sends notification and learns that the debtor did not receive it must attempt to locate the debtor and send another notification.

7. **Recognized Market; Perishable Collateral.** New subsection (d) [subsection (4)] makes it clear that there is no obligation to give notification of a disposition in the case of perishable collateral or collateral customarily sold on a recognized market (e.g., marketable securities). Former Section 9-504(3) [30-9-504(3), now repealed] might be read (incorrectly) to relieve the secured party from its duty to notify a debtor but not from its duty to notify other secured parties in connection with dispositions of such collateral.

8. **Failure to Conduct Notified Disposition.** Nothing in this Article [Title 30, chapter 9A] prevents a secured party from electing not to conduct a disposition after sending a notification. Nor does this Article [Title 30, chapter 9A] prevent a secured party from electing to send a revised notification if its plans for disposition change. This assumes, however, that the secured party acts in good faith, the revised notification is reasonable, and the revised plan for disposition and any attendant delay are commercially reasonable.

9. **Waiver.** A debtor or secondary obligor may waive the right to notification under this section only by a post-default authenticated agreement. See Section 9-624(a) [30-9A-624(1)].

10. **Other Law.** Other State or federal law may contain requirements concerning notification of a disposition of property by a secured party. For example, federal law imposes notification requirements with respect to the enforcement of mortgages on federally documented vessels. Principles of statutory interpretation and, in the context of federal law, supremacy and preemption determine whether and to what extent law other than this Article supplements, displaces, or is displaced by this Article. See Sections 1-103 [30-1-103], 1-104 [30-1-104], 9-109(c)(1) [30-9A-109(3)(a)].

Case Notes

Adequacy of Notice — Question of Law: The debtors entered an installment contract to buy a mobile home from the sellers. They became delinquent on monthly payments, and eventually the seller invoked the acceleration clause and demanded the outstanding balance due plus notice fees. The debtors returned the mobile home to the seller, who sold it to a new buyer 2 months later without notifying the debtors. The Supreme Court found that where there are no questions of fact with regards to the adequacy of or failure to give notice, a court may properly determine the adequacy of a particular notice as a question of law. In this case, the seller's failure to provide notice violated 30-9A-611. Christman v. Clause, 2019 MT 132, 396 Mont. 142, 443 P.3d 472.

No Authenticated Agreement — Waiver of Right to Notification of Disposition of Collateral Invalid: The debtors entered an installment contract to buy a mobile home from the sellers. They became delinquent on monthly payments, and eventually the seller invoked the acceleration clause and demanded the outstanding balance due plus notice fees. The debtors returned the mobile home to the seller, who sold it to a new buyer 2 months later without notifying the debtors. On review, the Supreme Court held that the debtors' voluntary surrender of and transfer of title to the collateral mobile home to the sellers did not automatically waive their right to notice of its resale. Rather, any waiver of the notice would have had to take the form of an authenticated writing signed after the default. Because no authenticated writing was signed after the default, the debtors' right to notice remained intact and was violated. Christman v. Clause, 2019 MT 132, 396 Mont. 142, 443 P.3d 472.

Security Interest Terminated — Creditor's Obligations Under U.C.C. Chapter 9A Not Terminated: The debtors entered an installment contract to buy a mobile home from the sellers. They became delinquent on monthly payments, and eventually the seller invoked the acceleration clause and demanded the outstanding balance due plus notice fees. The debtors returned the mobile home to the seller, who sold it to a new buyer 2 months later. The Supreme Court found that although the seller's disposition of the mobile home terminated the security interest under 30-9A-617, the seller's obligations as a creditor under Title 30, ch. 9A, remained, including the obligation to give the debtor notice of how the creditor intends to dispose of the collateral under 30-9A-611 and 30-9A-614, the obligation to conduct a commercially reasonable resale of the collateral under 30-9A-610, and the obligation to account to the debtor for any surplus realized from the sale of the collateral under 30-9A-608, 30-9A-615, 30-9A-616, and 30-9A-626. Christman v. Clause, 2019 MT 132, 396 Mont. 142, 443 P.3d 472.

30-9A-612. Timeliness of notification before disposition of collateral.

Official Comments

1. **Source.** New.

2. **Reasonable Notification.** Section 9-611(b) [30-9A-611(2)] requires the secured party to send a "reasonable authenticated notification." Under that section, as under former Section 9-504(3) [30-9-504(3), now repealed, see 30-9A-610, 30-9A-611, and 30-9A-624], one aspect of a reasonable notification is its timeliness. This generally means that the notification must be sent at a reasonable time in advance of the date of a public disposition or the date after which a private disposition is to be made. A notification that is sent so near to the disposition date that a notified person could not be expected to act on or take account of the notification would be unreasonable.

3. **Timeliness of Notification: Safe Harbor.** The 10-day notice period in subsection (b) [subsection (2)] is intended to be a "safe harbor" and not a minimum requirement. To qualify for the "safe harbor" the notification must be sent after default. A notification also must be sent in a commercially reasonable manner. See Section 9-611(b) [30-9A-611(2)] ("reasonable authenticated notification"). These requirements prevent a secured party from taking advantage of the "safe harbor" by, for example, giving the debtor a notification at the time of the original extension of credit or sending the notice by surface mail to a debtor overseas.

30-9A-613. Contents and form of notification before disposition of collateral — general.

Official Comments

1. **Source.** New.

2. **Contents of Notification.** To comply with the "reasonable authenticated notification" requirement of Section 9-611(b) [30-9A-611(2)], the contents of a notification must be reasonable. Except in a consumer-goods transaction, the contents of a notification that includes the information set forth in paragraph (1) [subsection (1)(a)] are sufficient as a matter of law, unless the parties agree otherwise. (The reference to "time" of disposition means here, as it did in former Section 9-504(3) [30-9-504(3), now repealed, see 30-9A-610, 30-9A-611, and 30-9A-624], not only the hour of the day but also the date.) Although a secured party may choose to include additional information concerning the transaction or the debtor's rights and obligations, no additional information is required unless the parties agree otherwise. A notification that lacks some of the information set forth in paragraph (1) [subsection (1)(a)] nevertheless may be sufficient if found to be reasonable by the trier of fact, under paragraph (2) [subsection (1)(b)]. A properly completed sample form of notification in paragraph (5) [subsection (2)] or in Section 9-614(a)(3) [30-9A-614(3)] is an example of a notification that would contain the information set forth in paragraph (1) [subsection (1)(a)]. Under paragraph (4) [subsection (1)(d)], however, no particular phrasing of the notification is required.

This section applies to a notification of a public disposition conducted electronically. A notification of an electronic disposition satisfies paragraph (1)(E) [subsection (1)(a)(v)] if it states the time when the disposition is scheduled to begin and states the electronic location. For example, under the technology current in 2010, the Uniform Resource Locator (URL) or other Internet address where the site of the public disposition can be accessed suffices as an electronic location.

Compiler's Comments

2001 Amendment: Chapter 179 in (1)(a)(v) substituted "public disposition" for "public sale". Amendment effective July 1, 2001.

30-9A-614. Contents and form of notification before disposition of collateral — consumer-goods transaction.

Official Comments

1. **Source.** New.

2. **Notification in Consumer-Goods Transactions.** Paragraph (1) [subsection (1)] sets forth the information required for a reasonable notification in a consumer-goods transaction. A notification that lacks any of the information set forth in paragraph (1) [subsection (1)] is insufficient as a matter of law. Compare Section 9-613(2) [30-9A-613(1)(b)], under which the trier of fact may find a notification to be sufficient even if it lacks some information listed in paragraph (1) [subsection (1)(a)] of that section.

3. **Safe-Harbor Form of Notification; Errors in Information.** Although paragraph (2) [subsection (2)] provides that a particular phrasing of a notification is not required, paragraph (3) [subsection (3)] specifies a safe-harbor form that, when properly completed, satisfies paragraph (1) [subsection (1)]. Paragraphs (4), (5), and (6) [subsections (4), (5), and (6)] contain special rules applicable to erroneous and additional information. Under paragraph (4) [subsection (4)], a notification in the safe-harbor form specified in paragraph (3) [subsection (3)] is not rendered insufficient if it contains additional information at the end of the form. Paragraph (5) [subsection (5)] provides that non-misleading errors in information contained in a notification are permitted if the safe-harbor form is used and if the errors are in information not required by paragraph (1) [subsection (1)]. Finally, if a notification is in a form other than the paragraph (3) [subsection (3)] safe-harbor form, other law determines the effect of including in the notification information other than that required by paragraph (1) [subsection (1)].

Case Notes

CASES DECIDED AFTER 1999 REVISION

Security Interest Terminated — Creditor's Obligations Under U.C.C. Chapter 9A Not Terminated: The debtors entered an installment contract to buy a mobile home from the sellers. They became delinquent on monthly payments, and eventually the seller invoked the acceleration clause and demanded the outstanding balance due plus notice fees. The debtors returned the mobile home to the seller, who sold it to a new buyer 2 months later. The Supreme Court found that although the seller's disposition of the mobile home terminated the security interest under 30-9A-617, the seller's obligations as a creditor under Title 30, ch. 9A, remained, including the obligation to give the debtor notice of how the creditor intends to dispose of the collateral under 30-9A-611 and 30-9A-614, the obligation to conduct a commercially reasonable resale of the collateral under 30-9A-610, and the obligation to account to the debtor for any surplus realized from the sale of the collateral under 30-9A-608, 30-9A-615, 30-9A-616, and 30-9A-626. Christman v. Clause, 2019 MT 132, 396 Mont. 142, 443 P.3d 472.

CASES DECIDED PRIOR TO 1999 REVISION

Deficiency Judgment After Foreclosure Sale: Deficiency judgment after foreclosure sale was proper even though sale was not public and contract contained clause that "notice [be] given in the manner provided in 30-9-508 [now repealed]", since mortgagee was given power of sale by contract, with contract setting forth statute as an acceptable method of sale. Bell v. Cole, 154 M 43, 459 P2d 692 (1969).

Change of Possession Not Accomplished by Pendency of the Foreclosure Action: That the pendency of the action to foreclose the mortgage did not ipso facto work a constructive change of possession from the mortgagor to the mortgagee is made plain by 30-9-508 (now repealed), which authorized the joinder in a foreclosure action of one for the recovery of the possession of the mortgaged property. If the institution of foreclosure proceedings worked a constructive change of possession, there would have been no object in authorizing the joinder of an action for the recovery of the possession of the mortgaged property. Griffiths v. Thrasher, 95 M 238, 26 P2d 983 (1933).

Mortgage Foreclosure Action Mortgage Joined With Conversion Action: As an exception to the general rule that an action in tort may not be joined with one on contract, an action to foreclose a chattel mortgage may be united with one in conversion against the purchaser of the mortgaged chattels. Beers v. W. P. Devereux Co., 87 M 210, 286 P 406 (1930).

Strict Statutory Compliance Necessary: The requirements of 30-9-508 (now repealed), under which a mortgagee of chattels may have the same sold on default of the mortgagor in execution of the power granted to him by the terms of the mortgage, must be strictly complied with. Otherwise, jurisdiction to make the sale is absent and it does not divest the mortgagor of title. Trudell v. Hingham St. Bank, 62 M 557, 205 P 667 (1922).

Action to Recover Balance Due After Sale: Where the parties to a chattel mortgage stipulated that the mortgagee might take possession of and sell the property under a power of sale whenever foreclosure became necessary, as they could properly do under 30-9-508 (now repealed), the complaint in an action to recover a balance due after sale, alleging that the property was so sold, was sufficient in the absence of a demurrer, an allegation that demand for payment had been made and notice of sale given not having been necessary. Union Bank & Trust Co. v. Himmelbauer, 56 M 82, 181 P 332 (1919).

Authority of Sheriff:

A sheriff had full authority to contract through his deputy with an individual for the keeping of cattle seized under a power of sale contained in a chattel mortgage, inasmuch as he was authorized to perform all his official acts, either personally or by deputy, and was held to be in the performance of an official duty under the requirements of a section similar to the above. Vose v. Whitney, 7 M 385, 16 P 846 (1888). See also Maddox v. Rader, 9 M 126, 22 P 386 (1889).

Money received by a sheriff from a sale of chattels under a mortgage containing a clause, authorized by statute, empowering the sheriff of the county to execute the power of sale therein granted, is received by him in his official capacity, and a failure to pay over such money is a breach of official duty for which his bondsmen are liable. Maddox v. Rader, 9 M 126, 22 P 386 (1889).

30-9A-615. Application of proceeds of disposition — liability for deficiency and right to surplus.

Official Comments

1. **Source.** Former Section 9-504(1), (2) [30-9-504(1), (2), now repealed].

2. **Application of Proceeds.** This section contains the rules governing application of proceeds and the debtor's liability for a deficiency following a disposition of collateral. Subsection (a) [subsection (1)] sets forth the basic order of application. The proceeds are applied first to the expenses of disposition, second to the obligation secured by the security interest that is being enforced, and third, in the specified circumstances, to interests that are subordinate to that security interest.

Subsections (a) and (d) [subsections (1) and (4)] also address the right of a consignor to receive proceeds of a disposition by a secured party whose interest is senior to that of the consignor. Subsection (a) [subsection (1)] requires the enforcing secured party to pay excess proceeds first to subordinate secured parties or lienholders whose interests are senior to that of a consignor and, finally, to a consignor. Inasmuch as a consignor is the owner of the collateral, secured parties and lienholders whose interests are junior to the consignor's interest will not be entitled to any proceeds. In like fashion, under subsection (d)(1) [subsection (4)(a)] the debtor is not entitled to a surplus when the enforcing secured party is required to pay over proceeds to a consignor.

3. **Noncash Proceeds.** Subsection (c) [subsection (3)] addresses the application of noncash proceeds of a disposition, such as a note or lease. The explanation in Section 9-608 [30-9A-608], Comment 4, generally applies to this subsection.

Example: A secured party in the business of selling or financing automobiles takes possession of collateral (an automobile) following its debtor's default. The secured party decides to sell the automobile in a private disposition under Section 9-610 [30-9A-610] and sends appropriate notification under Section 9-611 [30-9A-611]. After undertaking its normal credit investigation and in accordance with its normal credit policies, the secured party sells the automobile on credit, on terms typical of the credit terms normally extended by the secured party in the ordinary course of its business. The automobile stands as collateral for the remaining balance of the price. The noncash proceeds received by the secured party are chattel paper. The secured party may wish to credit its debtor (the assignor) with the principal amount of the chattel paper or may wish to credit the debtor only as and when the payments are made on the chattel paper by the buyer. Under subsection (c) [subsection (3)], the secured party is under no duty to apply the noncash proceeds (here, the chattel paper) or their value to the secured obligation unless its failure to do so would be commercially unreasonable. If a secured party elects to apply the chattel paper to the outstanding obligation, however, it must do so in a commercially reasonable manner. The facts in the example indicate that it would be commercially unreasonable for the secured party to fail to apply the value of the chattel paper to the original debtor's secured obligation. Unlike the example in Comment 4 to Section 9-608 [30-9A-608], the noncash proceeds received in this example are of the type that the secured party regularly generates in the ordinary course of its financing business in nonforeclosure transactions. The original debtor should not be exposed to delay or uncertainty in this situation. Of course, there will be many situations that fall between the examples presented in the Comment to Section 9-608 [30-9A-608] and in this Comment. This Article [Title 30, chapter 9A] leaves their resolution to the court based on the facts of each case.

One would expect that where noncash proceeds are or may be material, the secured party and debtor would agree to more specific standards in an agreement entered into before or after default. The parties may agree to the method of application of noncash proceeds if the method is not manifestly unreasonable. See Section 9-603 [30-9A-603].

When the secured party is not required to "apply or pay over for application noncash proceeds," the proceeds nonetheless remain collateral subject to this Article [Title 30, chapter 9A]. See Section 9-608 [30-9A-608], Comment 4.

4. **Surplus and Deficiency.** Subsection (d) [subsection (4)] deals with surplus and deficiency. It revises former Section 9-504(2) [30-9-504(2), now repealed] by imposing an explicit requirement that the secured party "pay" the debtor for any surplus, while retaining the secured party's duty to "account." Inasmuch as the debtor may not be an obligor, subsection (d) [subsection (4)] provides that the obligor (not the debtor) is liable for the deficiency. The special rule governing surplus and deficiency when receivables have been sold likewise takes into account the distinction between a debtor and an obligor. Subsection (d) [subsection (4)] also addresses the situation in which a consignor has an interest that is subordinate to the security interest being enforced.

5. **Collateral Under New Ownership.** When the debtor sells collateral subject to a security interest, the original debtor (creator of the security interest) is no longer a debtor inasmuch as it no longer has a property interest in the collateral; the buyer is the debtor. See Section 9-102 [30-9A-102]. As between the debtor (buyer of the collateral) and the original debtor (seller of the collateral), the debtor (buyer) normally would be entitled to the surplus following a disposition. Subsection (d) [subsection (4)] therefore requires the secured party to pay the surplus to the debtor (buyer), not to the original debtor (seller) with which it has dealt. But, because this situation typically arises as a result of the debtor's wrongful act, this Article [Title 30, chapter 9A] does not expose the secured party to the risk of determining ownership of the collateral. If the secured party does not know about the buyer and accordingly pays the surplus to the original debtor, the exculpatory provisions of this Article [Title 30, chapter 9A] exonerate the secured party from liability to the buyer. See Sections 9-605, 9-628(a), (b) [30-9A-605 and 30-9A-628(1) and (2)]. If a debtor sells collateral free of a security interest, as in a sale to a buyer in ordinary course of business (see Section 9-320(a) [30-9-320(1)]), the property is no longer collateral and the buyer is not a debtor.

6. **Certain "Low-Price" Dispositions.** Subsection (f) [subsection (6)] provides a special method for calculating a deficiency or surplus when the secured party, a person related to the secured party (defined in Section 9-102 [30-9A-102]), or a secondary obligor acquires the collateral at a foreclosure disposition. It recognizes that when the foreclosing secured party or a related party is the transferee of the collateral, the secured party sometimes lacks the incentive to maximize the proceeds of disposition. As a consequence, the disposition may comply with the procedural requirements of this Article [Title 30, chapter 9A] (e.g., it is conducted in a commercially reasonable manner following reasonable notice) but nevertheless fetch a low price.

Subsection (f) [subsection (6)] adjusts for this lack of incentive. If the proceeds of a disposition of collateral to a secured party, a person related to the secured party, or a secondary obligor are "significantly below the range of proceeds that a complying disposition to a person other than the secured party, a person related to the secured party, or a secondary obligor would have brought," then instead of calculating a deficiency (or surplus) based on the actual net proceeds, the calculation is based upon the amount that would have been received in a commercially reasonable disposition to a person other than the secured party, a person related to the secured party, or a secondary obligor. Subsection (f) [subsection (6)] thus rejects the view that the secured party's receipt of such a price necessarily constitutes noncompliance with Part 6 [Title 30, chapter 9A, part 6]. However, such a price may suggest the need for greater judicial scrutiny. See Section 9-610 [30-9A-610], Comment 10.

7. **"Person Related To."** Section 9-102 [30-9A-102] defines "person related to." That term is a key element of the system provided in subsection (f) [subsection (6)] for low-price dispositions. One part of the definition applies when the secured party is an individual, and the other applies when the secured party is an organization. The definition is patterned closely on the corresponding definition in Section 1.301(32) of the Uniform Consumer Credit Code.

Compiler's Comments

2001 Amendment: Chapter 179 near end of (1) after "disposition" inserted "under 30-9A-610"; and near middle of (3) substituted "disposition under 30-9A-610" for "disposition under this section". Amendment effective July 1, 2001.

Case Notes

Security Interest Terminated — Creditor's Obligations Under U.C.C. Chapter 9A Not Terminated: The debtors entered an installment contract to buy a mobile home from the sellers. They became delinquent on monthly payments, and eventually the seller invoked the acceleration clause and demanded the outstanding balance due plus notice fees. The debtors returned the mobile home to the seller, who sold it to a new buyer 2 months later. The Supreme Court found that although the seller's disposition of the mobile home terminated the security interest under 30-9A-617, the seller's obligations as a creditor under Title 30, ch. 9A, remained, including the obligation to give the debtor notice of how the creditor intends to dispose of the collateral under 30-9A-611 and 30-9A-614, the obligation to conduct a commercially reasonable resale of the collateral under 30-9A-610, and the obligation to account to the debtor for any surplus realized from the sale of the collateral under 30-9A-608, 30-9A-615, 30-9A-616, and 30-9A-626. Christman v. Clause, 2019 MT 132, 396 Mont. 142, 443 P.3d 472.

Debtor Signed Release Provided by Creditor — Creditor Did Not Refund Surplus — Debtor Sought Surplus — Release Did Not End Article 9 Protections for Creditor: The District Court erred in granting summary judgment to the defendant creditor and in determining that a release agreement the plaintiff debtor signed terminated any further application of the Uniform Commercial Code. The plaintiff entered into an installment sale contract and security agreement to purchase a mobile home with a company that assigned the contract to the defendant. Six years later, the plaintiff voluntarily vacated the mobile home and allowed the defendant to take possession of it. When the plaintiff returned the mobile home to the defendant, she owed $39,791.80. The plaintiff signed a full release of contract, under which she released all rights to the mobile home. The defendant resold the mobile home 1 month later, without notice to the plaintiff, for $53,500, which the plaintiff alleged was $13,708.20 more than the principal she owed when she returned the mobile home. The defendant did not refund any surplus to the plaintiff and disputed that a surplus was in fact realized. The plaintiff argued that the execution of the release did not terminate the defendant's duty under 30-9A-608 to pay her the surplus proceeds from the resale of the mobile home. The Supreme Court determined that despite the release, Article 9 of the U.C.C. (Title 30, ch. 9A) may still require the creditor to account for a surplus realized from the collection of an account or from the disposition of the collateral. The plaintiff's relationship to the defendant was one of debtor to creditor through a secured transaction governed by Article 9. When the plaintiff defaulted on her obligations under the contract, the defendant's rights and responsibilities as a creditor also were governed by Article 9. The defendant's argument that Article 9 no longer governed the parties' relationship following execution of the release was based on its representation that it agreed in the release to absolve the plaintiff from any further contractual obligation she owed to the defendant. The release did not, by its express terms, lift the parties' relationship from that of debtor and creditor under Article 9 or render obsolete the protections afforded a debtor under 30-9A-608 and 30-9A-615. Kapor v. RJC Inv., Inc., 2019 MT 41, 394 Mont. 311, 434 P.3d 869.

30-9A-616. Explanation of calculation of surplus or deficiency.

Official Comments

1. **Source.** New.

2. **Duty to Send Information Concerning Surplus or Deficiency.** This section reflects the view that, in every consumer-goods transaction, the debtor or obligor is entitled to know the amount of a surplus or deficiency and the basis upon which the surplus or deficiency was calculated. Under subsection (b)(1) [subsection (2)(a)], a secured party is obligated to provide this information (an "explanation," defined in subsection (a)(1) [subsection (1)(a)]) no later than the time that it accounts for and pays a surplus or the time of its first written attempt to collect the deficiency. The obligor need not make a request for an accounting in order to receive an explanation. A secured party who does not attempt to collect a deficiency in writing or account for and pay a surplus has no obligation to send an explanation under subsection (b)(1) [subsection (2)(a)] and, consequently, cannot be liable for noncompliance.

A debtor or secondary obligor need not wait until the secured party commences written collection efforts in order to receive an explanation of how a deficiency or surplus was calculated. Subsection (b)(1)(B) [subsection (2)(a)(ii)] obliges the secured party to send an explanation within 14 days after it receives a "request" (defined in subsection (a)(2) [subsection (1)(b)]).

3. **Explanation of Calculation of Surplus or Deficiency.** Subsection (c) [subsection (3)] contains the requirements for how a calculation of a surplus or deficiency must be explained in order to satisfy subsection (a)(1)(B) [subsection (1)(a)(ii)]. It gives a secured party some discretion concerning rebates of interest or credit service charges. The secured party may include these rebates in the aggregate amount of obligations secured, under subsection (c)(1) [subsection (3)(a)], or may include them with other types of rebates and credits under subsection (c)(5) [subsection (3)(e)]. Rebates of interest or credit service charges are the only types of rebates for which this

discretion is provided. If the secured party provides an explanation that includes rebates of pre-computed interest, its explanation must so indicate. The expenses and attorney's fees to be described pursuant to subsection (c)(4) [subsection (3)(d)] are those relating to the most recent disposition, not those that may have been incurred in connection with earlier enforcement efforts and which have been resolved by the parties.

4. **Liability for Noncompliance.** A secured party who fails to comply with subsection (b)(2) [subsection (2)(b)] is liable for any loss caused plus $500. See Section 9-625(b), (c), (e)(6) [30-9A-625(2), (3), and (5)(f)]. A secured party who fails to send an explanation under subsection (b)(1) [subsection (2)(a)] is liable for any loss caused plus, if the noncompliance was "part of a pattern, or consistent with a practice of noncompliance," $500. See Section 9-625(b), (c), (e)(5) [30-9A-625(2), (3), and (5)(e)]. However, a secured party who fails to comply with this section is not liable for statutory minimum damages under Section 9-625(c)(2) [30-9A-625(3)(b)]. See Section 9-628(d) [30-9A-628(4)].

Case Notes

Security Interest Terminated — Creditor's Obligations Under U.C.C. Chapter 9A Not Terminated: The debtors entered an installment contract to buy a mobile home from the sellers. They became delinquent on monthly payments, and eventually the seller invoked the acceleration clause and demanded the outstanding balance due plus notice fees. The debtors returned the mobile home to the seller, who sold it to a new buyer 2 months later. The Supreme Court found that although the seller's disposition of the mobile home terminated the security interest under 30-9A-617, the seller's obligations as a creditor under Title 30, ch. 9A, remained, including the obligation to give the debtor notice of how the creditor intends to dispose of the collateral under 30-9A-611 and 30-9A-614, the obligation to conduct a commercially reasonable resale of the collateral under 30-9A-610, and the obligation to account to the debtor for any surplus realized from the sale of the collateral under 30-9A-608, 30-9A-615, 30-9A-616, and 30-9A-626. Christman v. Clause, 2019 MT 132, 396 Mont. 142, 443 P.3d 472.

30-9A-617. Rights of transferee of collateral.

Official Comments

1. **Source.** Former Section 9-504(4) [30-9-504(4), now repealed].

2. **Title Taken by Good-Faith Transferee.** Subsection (a) [subsection 1] sets forth the rights acquired by persons who qualify under subsection (b) [subsection (2)]-transferees who act in good faith. Such a person is a "transferee," inasmuch as a buyer at a foreclosure sale does not meet the definition of "purchaser" in Section 1-201 [30-1-201] (the transfer is not, vis-a-vis the debtor, "voluntary"). By virtue of the expanded definition of the term "debtor" in Section 9-102 [30-9A-102], subsection (a) [subsection (1)] makes clear that the ownership interest of a person who bought the collateral subject to the security interest is terminated by a subsequent disposition under this Part [Title 30, chapter 9A, part 6]. Such a person is a debtor under this Article [Title 30, chapter 9A]. Under former Article 9 [Title 30, chapter 9, now repealed], the result arguably was the same, but the statute was less clear. Under subsection (a) [subsection (1)], a disposition normally discharges the security interest being foreclosed and any subordinate security interests and other liens.

A disposition has the effect specified in subsection (a) [subsection (1)], even if the secured party fails to comply with this Article [Title 30, chapter 9A]. An aggrieved person (e.g., the holder of a subordinate security interest to whom a notification required by Section 9-611 [30-9A-611] was not sent) has a right to recover any loss under Section 9-625(b) [30-9A-625(2)].

3. **Unitary Standard in Public and Private Dispositions.** Subsection (b) [subsection 2] now contains a unitary standard that applies to transferees in both private and public dispositions—acting in good faith. However, this change from former Section 9-504(4) [30-9-504(4), now repealed] should not be interpreted to mean that a transferee acts in good faith even though it has knowledge of defects or buys in collusion, standards applicable to public dispositions under the former section. Properly understood, those standards were specific examples of the absence of good faith.

4. **Title Taken by Nonqualifying Transferee.** Subsection (c) [subsection (3)] specifies the consequences for a transferee who does not qualify for protection under subsections (a) and (b) [subsections (1) and (2)] (i.e., a transferee who does not act in good faith). The transferee takes subject to the rights of the debtor, the enforcing secured party, and other security interests or other liens.

Case Notes

Security Interest Terminated — Creditor's Obligations Under U.C.C. Chapter 9A Not Terminated: The debtors entered an installment contract to buy a mobile home from the sellers. They became delinquent on monthly payments, and eventually the seller invoked the acceleration clause and demanded the outstanding balance due plus notice fees. The debtors returned the mobile home to the seller, who sold it to a new buyer 2 months later. The Supreme Court found that although the seller's disposition of the mobile home terminated the security interest under 30-9A-617, the seller's obligations as a creditor under Title 30, ch. 9A, remained, including the obligation to give the debtor notice of how the creditor intends to dispose of the collateral under 30-9A-611 and 30-9A-614, the obligation to conduct a commercially reasonable resale of the collateral under 30-9A-610, and the obligation to account to the debtor for any surplus realized from the sale of the collateral under 30-9A-608, 30-9A-615, 30-9A-616, and 30-9A-626. Christman v. Clause, 2019 MT 132, 396 Mont. 142, 443 P.3d 472.

30-9A-618. Rights and duties of certain secondary obligors.

Official Comments

1. **Source.** Former Section 9-504(5) [30-9-504(5), now repealed].

2. **Scope of This Section.** Under this section, assignments of secured obligations and other transactions (regardless of form) that function like assignments of secured obligations are not dispositions to which Part 6 [Title 30, chapter 9A, part 6] applies. Rather, they constitute assignments of rights and (occasionally) delegations of duties. Application of this section may require an investigation into the agreement of the parties, which may not be reflected in the words of the repurchase agreement (e.g., when the agreement requires a recourse party to "purchase the collateral" but contemplates that the purchaser will then conduct an Article 9 [Title 30, chapter 9A] foreclosure disposition).

This section, like former Section 9-504(5) [30-9-504(5), now repealed], does not constitute a general and comprehensive rule for allocating rights and duties upon assignment of a secured obligation. Rather, it applies only in situations involving a secondary obligor described in subsection (a) [subsection (1)]. In other contexts, the agreement of the parties and applicable law other than Article 9 [Title 30, chapter 9A] determine whether the assignment imposes upon the assignee any duty to the debtor and whether the assignor retains its duties to the debtor after the assignment.

Subsection (a)(1) [subsection (1)(a)] applies when there has been an assignment of an obligation that is secured at the time it is assigned. Thus, if a secondary obligor acquires the collateral at a disposition under Section 9-610 [30-9A-610] and simultaneously or subsequently discharges the unsecured deficiency claim, subsection (a)(1) [subsection (1)(a)] is not implicated. Similarly, subsection (a)(3) [subsection (1)(c)] applies only when the secondary obligor is subrogated to the secured party's rights with respect to collateral. Thus, this subsection will not be implicated if a secondary obligor discharges the debtor's unsecured obligation for a post-disposition deficiency. Similarly, if the secured party disposes of some of the collateral and the secondary obligor thereafter discharges the remaining obligation, subsection (a) [subsection (1)] applies only with respect to rights and duties concerning the remaining collateral, and, under subsection (b) [subsection (2)], the subrogation is not a disposition of the remaining collateral.

As discussed more fully in Comment 3, a secondary obligor may receive a transfer of collateral in a disposition under Section 9-610 [30-9A-610] in exchange for a payment that is applied against the secured obligation. However, a secondary obligor who pays and receives a transfer of collateral does not necessarily become subrogated to the rights of the secured party as contemplated by subsection (a)(3) [subsection (1)(c)]. Only to the extent the secondary obligor makes a payment in satisfaction of its secondary obligation would it become subrogated. To the extent its payment constitutes the price of the collateral in a Section 9-610 [30-9A-610] disposition by the secured party, the secondary obligor would not be subrogated. Thus, if the amount paid by the secondary obligor for the collateral in a Section 9-610 [30-9A-610] disposition is itself insufficient to discharge the secured obligation, but the secondary obligor makes an additional payment that satisfies the remaining balance, the secondary obligor would be subrogated to the secured party's deficiency claim. However, the duties of the secured party as such would have come to an end with respect to that collateral. In some situations the capacity in which the payment is made may be unclear. Accordingly, the parties should in their relationship provide clear evidence of the nature and circumstances of the payment by the secondary obligor.

3. **Transfer of Collateral to Secondary Obligor.** It is possible for a secured party to transfer collateral to a secondary obligor in a transaction that is a disposition under Section 9-610

[30-9A-610] and that establishes a surplus or deficiency under Section 9-615 [30-9A-615]. Indeed, this Article [Title 30, chapter 9A] includes a special rule, in Section 9-615(f) [30-9A-615(6)], for establishing a deficiency in the case of some dispositions to, inter alia, secondary obligors. This Article [Title 30, chapter 9A] rejects the view, which some may have ascribed to former Section 9-504(5) [30-9-504(5), now repealed], that a transfer of collateral to a recourse party can never constitute a disposition of collateral which discharges a security interest. Inasmuch as a secured party could itself buy collateral at its own public sale, it makes no sense to prohibit a recourse party ever from buying at the sale.

4. **Timing and Scope of Obligations.** Under subsection (a) [subsection (1)], a recourse party acquires rights and incurs obligations only "after" one of the specified circumstances occurs. This makes clear that when a successor assignee, transferee, or subrogee becomes obligated it does not assume any liability for earlier actions or inactions of the secured party whom it has succeeded unless it agrees to do so. Once the successor becomes obligated, however, it is responsible for complying with the secured party's duties thereafter. For example, if the successor is in possession of collateral, then it has the duties specified in Section 9-207 [30-9A-207].

Under subsection (b) [subsection (2)], the same event (assignment, transfer, or subrogation) that gives rise to rights to, and imposes obligations on, a successor relieves its predecessor of any further duties under this Article [Title 30, chapter 9A]. For example, if the security interest is enforced after the secured obligation is assigned, the assignee-but not the assignor-has the duty to comply with this Part [Title 30, chapter 9A, part 6]. Similarly, the assignment does not excuse the assignor from liability for failure to comply with duties that arose before the event or impose liability on the assignee for the assignor's failure to comply.

30-9A-619. Transfer of record or legal title.

Official Comments

1. **Source.** New.

2. **Transfer of Record or Legal Title.** Potential buyers of collateral that is covered by a certificate of title (e.g., an automobile) or is subject to a registration system (e.g., a copyright) typically require as a condition of their purchase that the certificate or registry reflect their ownership. In many cases, this condition can be met only with the consent of the record owner. If the record owner is the debtor and, as may be the case after the default, the debtor refuses to cooperate, the secured party may have great difficulty disposing of the collateral.

Subsection (b) [subsection 2] provides a simple mechanism for obtaining record or legal title, for use primarily when other law does not provide one. Of course, use of this mechanism will not be effective to clear title to the extent that subsection (b) [subsection (2)] is preempted by federal law. Subsection (b) [subsection 2] contemplates a transfer of record or legal title to a third party, following a secured party's exercise of its disposition or acceptance remedies under this Part [Title 30, chapter 9A, part 6], as well as a transfer by a debtor to a secured party prior to the secured party's exercise of those remedies. Under subsection (c) [subsection (3)], a transfer of record or legal title (under subsection (b) [subsection (2)] or under other law) to a secured party prior to the exercise of those remedies merely puts the secured party in a position to pass legal or record title to a transferee at foreclosure. A secured party who has obtained record or legal title retains its duties with respect to enforcement of its security interest, and the debtor retains its rights as well.

3. **Title-Clearing Systems Under Other Law.** Applicable non-UCC law (e.g., a certificate-of-title statute, federal registry rules, or the like) may provide a means by which the secured party may obtain or transfer record or legal title for the purpose of a disposition of the property under this Article [Title 30, chapter 9A]. The mechanism provided by this section is in addition to any title-clearing provision under law other than this Article [Title 30, chapter 9A].

Case Notes

No Authenticated Agreement — Waiver of Right to Notification of Disposition of Collateral Invalid: The debtors entered an installment contract to buy a mobile home from the sellers. They became delinquent on monthly payments, and eventually the seller invoked the acceleration clause and demanded the outstanding balance due plus notice fees. The debtors returned the mobile home to the seller, who sold it to a new buyer 2 months later without notifying the debtors. On review, the Supreme Court held that the debtors' voluntary surrender of and transfer of title to the collateral mobile home to the sellers did not automatically waive their right to notice of its resale. Rather, any waiver of the notice would have had to take the form of an authenticated writing signed after the default. Because no authenticated writing was signed after the default, the debtors' right to notice remained intact and was violated. Christman v. Clause, 2019 MT 132, 396 Mont. 142, 443 P.3d 472.

30-9A-620. Acceptance of collateral in full or partial satisfaction — compulsory disposition of collateral.

Official Comments

1. **Source.** Former Section 9-505 [30-9-505, now repealed].

2. **Overview.** This section and the two sections following deal with strict foreclosure, a procedure by which the secured party acquires the debtor's interest in the collateral without the need for a sale or other disposition under Section 9-610 [30-9A-610]. Although these provisions derive from former Section 9-505 [30-9-505, now repealed], they have been entirely reorganized and substantially rewritten. The more straightforward approach taken in this Article [Title 30, chapter 9A] eliminates the fiction that the secured party always will present a "proposal" for the retention of collateral and the debtor will have a fixed period to respond. By eliminating the need (but preserving the possibility) for proceeding in that fashion, this section eliminates much of the awkwardness of former Section 9-505 [30-9-505, now repealed]. It reflects the belief that strict foreclosures should be encouraged and often will produce better results than a disposition for all concerned.

Subsection (a) [subsection 1] sets forth the conditions necessary to an effective acceptance (formerly, retention) of collateral in full or partial satisfaction of the secured obligation. Section 9-621 [30-9A-621] requires in addition that a secured party who wishes to proceed under this section notify certain other persons who have or claim to have an interest in the collateral. Unlike the failure to meet the conditions in subsection (a) [subsection (1)], under Section 9-622(b) [30-9A-622(2)] the failure to comply with the notification requirement of Section 9-621 [30-9A-621] does not render the acceptance of collateral ineffective. Rather, the acceptance can take effect notwithstanding the secured party's noncompliance. A person to whom the required notice was not sent has the right to recover damages under Section 9-625(b) [30-9A-625(2)]. Section 9-622(a) [30-9A-622(1)] sets forth the effect of an acceptance of collateral.

3. **Conditions to Effective Acceptance.** Subsection (a) [subsection 1] contains the conditions necessary to the effectiveness of an acceptance of collateral. Subsection (a)(1) [subsection (1)(a)] requires the debtor's consent. Under subsections (c)(1) and (c)(2) [subsections (3)(a) and (3)(b)], the debtor may consent by agreeing to the acceptance in writing after default. Subsection (c)(2) [subsection (3)(b)] contains an alternative method by which to satisfy the debtor's-consent condition in subsection (a)(1) [subsection (1)(a)]. It follows the proposal-and-objection model found in former Section 9-505 [30-9-505, now repealed]: The debtor consents if the secured party sends a proposal to the debtor and does not receive an objection within 20 days. Under subsection (c)(1) [subsection (3)(a)], however, that silence is not deemed to be consent with respect to acceptances in partial satisfaction. Thus, a secured party who wishes to conduct a "partial strict foreclosure" must obtain the debtor's agreement in a record authenticated after default. In all other respects, the conditions necessary to an effective partial strict foreclosure are the same as those governing acceptance of collateral in full satisfaction. (But see subsection (g) [subsection (7)], prohibiting partial strict foreclosure of a security interest in consumer transactions.)

The time when a debtor consents to a strict foreclosure is significant in several circumstances under this section and the following one. See Sections 9-620(a)(1), (d)(2), 9-621(a)(1), (a)(2), (a)(3) [30-9A-620(1)(a) and (4)(b) and 30-9A-621(1)(a), (1)(b), and (1)(c)]. For purposes of determining the time of consent, a debtor's conditional consent constitutes consent.

Subsection (a)(2) [subsection (1)(b)] contains the second condition to the effectiveness of an acceptance under this section-the absence of a timely objection from a person holding a junior interest in the collateral or from a secondary obligor. Any junior party-secured party or lienholder-is entitled to lodge an objection to a proposal, even if that person was not entitled to notification under Section 9-621 [30-9A-621]. Subsection (d) [subsection (4)], discussed below, indicates when an objection is timely.

Subsections (a)(3) and (a)(4) [subsections (1)(c) and (1)(d)] contain special rules for transactions in which consumers are involved. See Comment 12.

4. **Proposals.** Section 9-102 [30-9A-102] defines the term "proposal." It is necessary to send a "proposal" to the debtor only if the debtor does not agree to an acceptance in an authenticated record as described in subsection (c)(1) or (c)(2) [subsection (3)(a) or (3)(b)]. Section 9-621(a) [30-9A-621(1)] determines whether it is necessary to send a proposal to third parties. A proposal need not take any particular form as long as it sets forth the terms under which the secured party is willing to accept collateral in satisfaction. A proposal to accept collateral should specify the amount (or a means of calculating the amount, such as by including a per diem accrual figure) of the secured obligations to be satisfied, state the conditions (if any) under which the proposal may be revoked, and describe any other applicable conditions. Note, however, that a conditional

proposal generally requires the debtor's agreement in order to take effect. See subsection (c) [subsection (3)].

5. **Secured Party's Agreement; No "Constructive" Strict Foreclosure.** The conditions of subsection (a) [subsection (1)] relate to actual or implied consent by the debtor and any secondary obligor or holder of a junior security interest or lien. To ensure that the debtor cannot unilaterally cause an acceptance of collateral, subsection (b) [subsection (2)] provides that compliance with these conditions is necessary but not sufficient to cause an acceptance of collateral. Rather, under subsection (b) [subsection (2)], acceptance does not occur unless, in addition, the secured party consents to the acceptance in an authenticated record or sends to the debtor a proposal. For this reason, a mere delay in collection or disposition of collateral does not constitute a "constructive" strict foreclosure. Instead, delay is a factor relating to whether the secured party acted in a commercially reasonable manner for purposes of Section 9-607 or 9-610 [30-9A-607 or 30-9A-610]. A debtor's voluntary surrender of collateral to a secured party and the secured party's acceptance of possession of the collateral does not, of itself, necessarily raise an implication that the secured party intends or is proposing to accept the collateral in satisfaction of the secured obligation under this section.

6. **When Acceptance Occurs.** This section does not impose any formalities or identify any steps that a secured party must take in order to accept collateral once the conditions of subsections (a) and (b) [subsections (1) and (2)] have been met. Absent facts or circumstances indicating a contrary intention, the fact that the conditions have been met provides a sufficient indication that the secured party has accepted the collateral on the terms to which the secured party has consented or proposed and the debtor has consented or failed to object. Following a proposal, acceptance of the collateral normally is automatic upon the secured party's becoming bound and the time for objection passing. As a matter of good business practice, an enforcing secured party may wish to memorialize its acceptance following a proposal, such as by notifying the debtor that the strict foreclosure is effective or by placing a written record to that effect in its files. The secured party's agreement to accept collateral is self-executing and cannot be breached. The secured party is bound by its agreement to accept collateral and by any proposal to which the debtor consents.

7. **No Possession Requirement.** This section eliminates the requirement in former Section 9-505 [30-9-505, now repealed] that the secured party be "in possession" of collateral. It clarifies that intangible collateral, which cannot be possessed, may be subject to a strict foreclosure under this section. However, under subsection (a)(3) [subsection (1)(c)], if the collateral is consumer goods, acceptance does not occur unless the debtor is not in possession.

8. **When Objection Timely.** Subsection (d) [subsection (4)] explains when an objection is timely and thus prevents an acceptance of collateral from taking effect. An objection by a person to which notification was sent under Section 9-621 [30-9A-621] is effective if it is received by the secured party within 20 days from the date the notification was sent to that person. Other objecting parties (i.e., third parties who are not entitled to notification) may object at any time within 20 days after the last notification is sent under Section 9-621 [30-9A-621]. If no such notification is sent, third parties must object before the debtor agrees to the acceptance in writing or is deemed to have consented by silence. The former may occur any time after default, and the latter requires a 20-day waiting period. See subsection (c) [subsection (3)].

9. **Applicability of Other Law.** This section does not purport to regulate all aspects of the transaction by which a secured party may become the owner of collateral previously owned by the debtor. For example, a secured party's acceptance of a motor vehicle in satisfaction of secured obligations may require compliance with the applicable motor vehicle certificate-of-title law. State legislatures should conform those laws so that they mesh well with this section and Section 9-610 [30-9A-610], and courts should construe those laws and this section harmoniously. A secured party's acceptance of collateral in the possession of the debtor also may implicate statutes dealing with a seller's retention of possession of goods sold.

10. **Accounts, Chattel Paper, Payment Intangibles, and Promissory Notes.** If the collateral is accounts, chattel paper, payment intangibles, or promissory notes, then a secured party's acceptance of the collateral in satisfaction of secured obligations would constitute a sale to the secured party. That sale normally would give rise to a new security interest (the ownership interest) under Sections 1-201(37) and 9-109 [30-1-201(37) and 30-9A-109]. In the case of accounts and chattel paper, the new security interest would remain perfected by a filing that was effective to perfect the secured party's original security interest. In the case of payment intangibles or promissory notes, the security interest would be perfected when it attaches. See Section 9-309

[30-9A-309]. However, the procedures for acceptance of collateral under this section satisfy all necessary formalities and a new security agreement authenticated by the debtor would not be necessary.

11. **Role of Good Faith.** Section 1-304 [30-1-203] imposes an obligation of good faith on a secured party's enforcement under this Article [Title 30, chapter 9A]. This obligation may not be disclaimed by agreement. See Section 1-302 [30-1-302]. Thus, a proposal and acceptance made under this section in bad faith would not be effective. For example, a secured party's proposal to accept marketable securities worth $1,000 in full satisfaction of indebtedness in the amount of $100, made in the hopes that the debtor might inadvertently fail to object, would be made in bad faith. On the other hand, in the normal case proposals and acceptances should be not second-guessed on the basis of the "value" of the collateral involved. Disputes about valuation or even a clear excess of collateral value over the amount of obligations satisfied do not necessarily demonstrate the absence of good faith.

12. **Special Rules in Consumer Cases.** Subsection (e) [subsection (5)] imposes an obligation on the secured party to dispose of consumer goods under certain circumstances. Subsection (f) [subsection (6)] explains when a disposition that is required under subsection (e) [subsection (5)] is timely. An effective acceptance of collateral cannot occur if subsection (e) [subsection (5)] requires a disposition unless the debtor waives this requirement pursuant to Section 9-624(b) [30-9A-624(2)]. Moreover, a secured party who takes possession of collateral and unreasonably delays disposition violates subsection (e) [subsection (5)], if applicable, and may also violate Section 9-610 [30-9A-610] or other provisions of this Part [Title 30, chapter 9A, part 6]. Subsection (e) [subsection (5)] eliminates as superfluous the express statutory reference to "conversion" found in former Section 9-505 [30-9-505, now repealed]. Remedies available under other law, including conversion, remain available under this Article [Title 30, chapter 9A] in appropriate cases. See Sections 1-103 [30-1-103], 1-305 [30-1-106].

Subsection (g) [subsection (7)] prohibits the secured party in consumer transactions from accepting collateral in partial satisfaction of the obligation it secures. If a secured party attempts an acceptance in partial satisfaction in a consumer transaction, the attempted acceptance is void.

Case Notes

CASES DECIDED AFTER 1999 REVISION

Minimal Release Signed by Creditor — Debtor Not Allowed to Use Release to Keep Surplus — Debtor Failed to Commit to Acceptance of Collateral in Full Satisfaction: The District Court erred in granting the defendant creditor summary judgment when it determined that a minimal release constituted an acceptance of collateral in full satisfaction of the plaintiff debtor's secured obligation. The plaintiff voluntarily returned a mobile home to the defendant, signed a full release of contract provided to her by the defendant, and 1 month later the defendant resold the mobile home for $13,708.20 more than the principal the plaintiff owed. The defendant did not refund any surplus to the plaintiff, reasoning it was not required to return it based on the release. The Supreme Court determined that, like its statutory right to surplus, a debtor may not waive or vary the rules for acceptance of collateral in satisfaction of obligation provided in 30-9A-620 through 30-9A-622. The defendant cited no case in which a release as minimal as the one the plaintiff signed would be considered sufficient to meet strict foreclosure requirements, and the Supreme Court determined that relevant case law indicated that more was required. Because the release did not commit the defendant to anything or release any of the defendant's rights, and said nothing about acceptance of the collateral in full satisfaction of the plaintiff's debt, the Supreme Court concluded that the defendant did not satisfy the elements of acceptance of collateral in full satisfaction under 30-9A-620. Kapor v. RJC Inv., Inc., 2019 MT 41, 394 Mont. 311, 434 P.3d 869.

CASES DECIDED PRIOR TO 1999 REVISION

Effect of Notice of Intent to Sell Pledged Collateral: Defaulting debtors could not rely on 30-9-505(2) (section now repealed, see 30-9A-620, 30-9A-621, and 30-9A-624) to contend that secured party's actions in achieving a sale constituted a rescission, and satisfaction of the debt, so as to bar further recovery where defaulting debtors were given notice of an intent to enforce security interest by means of a sale of pledged collateral, and where secured party obtained a Writ of Mandate ultimately effectuating a sale. Stensvad v. Miners & Merchants Bank of Roundup, 163 M 409, 517 P2d 715 (1973).

30-9A-621. Notification of proposal to accept collateral.

Official Comments

1. **Source.** Former Section 9-505 [30-9-505, now repealed].

2. **Notification Requirement.** Subsection (a) [subsection 1] specifies three classes of competing claimants to whom the secured party must send notification of its proposal: (i) those who notify the secured party that they claim an interest in the collateral, (ii) holders of certain security interests and liens who have filed against the debtor, and (iii) holders of certain security interests who have perfected by compliance with a statute (including a certificate-of-title statute), regulation, or treaty described in Section 9-311(a) [30-9A-311(1)]. With regard to (ii), see Section 9-611 [30-9A-611], Comment 4. Subsection (b) [subsection 2] also requires notification to any secondary obligor if the proposal is for acceptance in partial satisfaction.

Unlike Section 9-611 [30-9A-611], this section contains no "safe harbor," which excuses an enforcing secured party from notifying certain secured parties and other lienholders. This is because, unlike Section 9-610 [30-9A-610], which requires that a disposition of collateral be commercially reasonable, Section 9-620 [30-9A-620] permits the debtor and secured party to set the amount of credit the debtor will receive for the collateral subject only to the requirement of good faith. An effective acceptance discharges subordinate security interests and other subordinate liens. See Section 9-622 [30-9A-622]. If collateral is subject to several liens securing debts much larger than the value of the collateral, the debtor may be disinclined to refrain from consenting to an acceptance by the holder of the senior security interest, even though, had the debtor objected and the senior disposed of the collateral under Section 9-610 [30-9A-610], the collateral may have yielded more than enough to satisfy the senior security interest (but not enough to satisfy all the liens). Accordingly, this section imposes upon the enforcing secured party the risk of the filing office's errors and delay. The holder of a security interest who is entitled to notification under this section but to whom the enforcing secured party does not send notification has the right to recover under Section 9-625(b) [30-9A-625(2)] any loss resulting from the secured party's noncompliance with this section.

Case Notes

Minimal Release Signed by Creditor — Debtor Not Allowed to Use Release to Keep Surplus — Debtor Failed to Commit to Acceptance of Collateral in Full Satisfaction: The District Court erred in granting the defendant creditor summary judgment when it determined that a minimal release constituted an acceptance of collateral in full satisfaction of the plaintiff debtor's secured obligation. The plaintiff voluntarily returned a mobile home to the defendant, signed a full release of contract provided to her by the defendant, and 1 month later the defendant resold the mobile home for $13,708.20 more than the principal the plaintiff owed. The defendant did not refund any surplus to the plaintiff, reasoning it was not required to return it based on the release. The Supreme Court determined that, like its statutory right to surplus, a debtor may not waive or vary the rules for acceptance of collateral in satisfaction of obligation provided in 30-9A-620 through 30-9A-622. The defendant cited no case in which a release as minimal as the one the plaintiff signed would be considered sufficient to meet strict foreclosure requirements, and the Supreme Court determined that relevant case law indicated that more was required. Because the release did not commit the defendant to anything or release any of the defendant's rights, and said nothing about acceptance of the collateral in full satisfaction of the plaintiff's debt, the Supreme Court concluded that the defendant did not satisfy the elements of acceptance of collateral in full satisfaction under 30-9A-620. Kapor v. RJC Inv., Inc., 2019 MT 41, 394 Mont. 311, 434 P.3d 869.

30-9A-622. Effect of acceptance of collateral.

Official Comments

1. **Source.** New.

2. **Effect of Acceptance.** Subsection (a) [subsection 1] specifies the effect of an acceptance of collateral in full or partial satisfaction of the secured obligation. The acceptance to which it refers is an effective acceptance. If a purported acceptance is ineffective under Section 9-620 [30-9A-620], e.g., because the secured party receives a timely objection from a person entitled to notification, then neither this subsection nor subsection (b) [subsection (2)] applies. Paragraph (1) [subsection (1)(a)] expresses the fundamental consequence of accepting collateral in full or partial satisfaction of the secured obligation-the obligation is discharged to the extent consented to by the debtor. Unless otherwise agreed, the obligor remains liable for any deficiency. Paragraphs (2) through (4) [subsections (1)(b) through (1)(d)] indicate the effects of an acceptance on various property rights and interests. Paragraph (2) [subsection (1)(b)] follows Section 9-617(a) [subsection

(1)] in providing that the secured party acquires "all of a debtor's rights in the collateral." Under paragraph (3) [subsection (1)(c)], the effect of strict foreclosure on holders of junior security interests and other liens is the same regardless of whether the collateral is accepted in full or partial satisfaction of the secured obligation: all junior encumbrances are discharged. Paragraph (4) [subsections (1)(d)] provides for the termination of other subordinate interests.

Subsection (b) [subsection 2] makes clear that subordinate interests are discharged under subsection (a) [subsection (1)] regardless of whether the secured party complies with this Article [Title 30, chapter 9A]. Thus, subordinate interests are discharged regardless of whether a proposal was required to be sent or, if required, was sent. However, a secured party's failure to send a proposal or otherwise to comply with this Article [Title 30, chapter 9A] may subject the secured party to liability under Section 9-625 [30-9A-625].

Case Notes

Minimal Release Signed by Creditor — Debtor Not Allowed to Use Release to Keep Surplus — Debtor Failed to Commit to Acceptance of Collateral in Full Satisfaction: The District Court erred in granting the defendant creditor summary judgment when it determined that a minimal release constituted an acceptance of collateral in full satisfaction of the plaintiff debtor's secured obligation. The plaintiff voluntarily returned a mobile home to the defendant, signed a full release of contract provided to her by the defendant, and 1 month later the defendant resold the mobile home for $13,708.20 more than the principal the plaintiff owed. The defendant did not refund any surplus to the plaintiff, reasoning it was not required to return it based on the release. The Supreme Court determined that, like its statutory right to surplus, a debtor may not waive or vary the rules for acceptance of collateral in satisfaction of obligation provided in 30-9A-620 through 30-9A-622. The defendant cited no case in which a release as minimal as the one the plaintiff signed would be considered sufficient to meet strict foreclosure requirements, and the Supreme Court determined that relevant case law indicated that more was required. Because the release did not commit the defendant to anything or release any of the defendant's rights, and said nothing about acceptance of the collateral in full satisfaction of the plaintiff's debt, the Supreme Court concluded that the defendant did not satisfy the elements of acceptance of collateral in full satisfaction under 30-9A-620. Kapor v. RJC Inv., Inc., 2019 MT 41, 394 Mont. 311, 434 P.3d 869.

30-9A-623. Right to redeem collateral.

Official Comments

1. **Source.** Former Section 9-506 [30-9-506, now repealed].

2. **Redemption Right.** Under this section, as under former Section 9-506 [30-9-506, now repealed], the debtor or another secured party may redeem collateral as long as the secured party has not collected (Section 9-607 [30-9A-607]), disposed of or contracted for the disposition of (Section 9-610 [30-9A-610]), or accepted (Section 9-620 [30-9A-620]) the collateral. Although this section generally follows former Section 9-506 [30-9-506, now repealed], it extends the right of redemption to holders of nonconsensual liens. To redeem the collateral a person must tender fulfillment of all obligations secured, plus certain expenses. If the entire balance of a secured obligation has been accelerated, it would be necessary to tender the entire balance. A tender of fulfillment obviously means more than a new promise to perform an existing promise. It requires payment in full of all monetary obligations then due and performance in full of all other obligations then matured. If unmatured secured obligations remain, the security interest continues to secure them (i.e., as if there had been no default).

3. **Redemption of Remaining Collateral Following Partial Enforcement.** Under Section 9-610 [30-9A-610] a secured party may make successive dispositions of portions of its collateral. These dispositions would not affect the debtor's, another secured party's, or a lienholder's right to redeem the remaining collateral.

4. **Effect of "Repledging."** Section 9-207 [30-9A-207] generally permits a secured party having possession or control of collateral to create a security interest in the collateral. As explained in the Comments to that section, the debtor's right (as opposed to its practical ability) to redeem collateral is not affected by, and does not affect, the priority of a security interest created by the debtor's secured party.

Case Notes

CASES DECIDED PRIOR TO 1999 REVISION

Redemption of Portion of Collateral: The debtor tendered a sum that covered the balance owed on one airplane in which the defendants had a security interest, but since that sum did not satisfy the balance owed on a second airplane, which was also secured by the first plane, the tender offered did not fulfill the requirements of 30-9-506 (now repealed, see 30-9A-623 and 30-9A-624) allowing redemption. Sturdevant v. First Sec. Bank, 186 M 91, 606 P2d 525 (1980).

30-9A-624. Waiver.

Official Comments

1. **Source.** Former Sections 9-504(3), 9-505, 9-506 [30-9-504(3), 30-9-505, 30-9-506, all now repealed].

2. **Waiver.** This section is a limited exception to Section 9-602 [30-9A-602], which generally prohibits waiver by debtors and obligors. It makes no provision for waiver of the rule prohibiting a secured party from buying at its own private disposition. Transactions of this kind are equivalent to "strict foreclosures" and are governed by Sections 9-620, 9-621, and 9-622 [30-9A-620, 30-9A-621, and 30-9A-622].

Case Notes

No Authenticated Agreement — Waiver of Right to Notification of Disposition of Collateral Invalid: The debtors entered an installment contract to buy a mobile home from the sellers. They became delinquent on monthly payments, and eventually the seller invoked the acceleration clause and demanded the outstanding balance due plus notice fees. The debtors returned the mobile home to the seller, who sold it to a new buyer 2 months later without notifying the debtors. On review, the Supreme Court held that the debtors' voluntary surrender of and transfer of title to the collateral mobile home to the sellers did not automatically waive their right to notice of its resale. Rather, any waiver of the notice would have had to take the form of an authenticated writing signed after the default. Because no authenticated writing was signed after the default, the debtors' right to notice remained intact and was violated. Christman v. Clause, 2019 MT 132, 396 Mont. 142, 443 P.3d 472.

30-9A-625. Remedies for secured party's failure to comply with chapter.

Official Comments

1. **Source.** Former Section 9-507 [30-9-507, now repealed].

2. **Remedies for Noncompliance; Scope.** Subsections (a) and (b) [subsections (1) and (2)] provide the basic remedies afforded to those aggrieved by a secured party's failure to comply with this Article [Title 30, chapter 9A]. Like all provisions that create liability, they are subject to Section 9-628 [30-9A-628], which should be read in conjunction with Section 9-605 [30-9A-605]. The principal limitations under this Part on a secured party's right to enforce its security interest against collateral are the requirements that it proceed in good faith (Section 1-203 [30-1-203]), in a commercially reasonable manner (Sections 9-607 and 9-610 [30-9A-607 and 30-9A-610]), and, in most cases, with reasonable notification (Sections 9-611 through 9-614 [30-9A-611 through 30-9A-614]). Following former Section 9-507 [30-9-507, now repealed], under subsection (a) [subsection (1)] an aggrieved person may seek injunctive relief, and under subsection (b) [subsection (2)] the person may recover damages for losses caused by noncompliance. Unlike former Section 9-507 [30-9-507, now repealed], however, subsections (a) and (b) [subsections (1) and (2)] are not limited to noncompliance with provisions of this Part of Article 9 [Title 30, chapter 9A, part 6]. Rather, they apply to noncompliance with any provision of this Article [Title 30, chapter 9A]. The change makes this section applicable to noncompliance with Sections 9-207 [30-9A-207] (duties of secured party in possession of collateral), 9-208 [30-9A-208] (duties of secured party having control over deposit account), 9-209 [30-9A-209] (duties of secured party if account debtor has been notified of an assignment), 9-210 [30-9A-210] (duty to comply with request for accounting, etc.), 9-509(a) [30-9A-509(1)] (duty to refrain from filing unauthorized financing statement), and 9-513(a) or (c) [30-9A-513(1) or (3)] (duty to provide termination statement). Subsection (a) [subsection 1] also modifies the first sentence of former Section 9-507(1) [30-9-507(1), now repealed] by adding the references to "collection" and "enforcement." Subsection (c)(2) [subsection (3)(b)], which gives a minimum damage recovery in consumer-goods transactions, applies only to noncompliance with the provisions of this Part [Title 30, chapter 9A, part 6].

3. **Damages for Noncompliance with this Article [Title 30, chapter 9A].** Subsection (b) [subsection 2] sets forth the basic remedy for failure to comply with the requirements of this Article [Title 30, chapter 9A]: a damage recovery in the amount of loss caused by the noncompliance. Subsection (c) [subsection (3)] identifies who may recover under subsection (b) [subsection (2)]. It affords a remedy to any aggrieved person who is a debtor or obligor. However, a principal obligor who is not a debtor may recover damages only for noncompliance with Section 9-616 [30-9A-616],

inasmuch as none of the other rights and duties in this Article [Title 30, chapter 9A] run in favor of such a principal obligor. Such a principal obligor could not suffer any loss or damage on account of noncompliance with rights or duties of which it is not a beneficiary. Subsection (c) [subsection (3)] also affords a remedy to an aggrieved person who holds a competing security interest or other lien, regardless of whether the aggrieved person is entitled to notification under Part 6 [Title 30, chapter 9A, part 6]. The remedy is available even to holders of senior security interests and other liens. The exercise of this remedy is subject to the normal rules of pleading and proof. A person who has delegated the duties of a secured party but who remains obligated to perform them is liable under this subsection. The last sentence of subsection (d) [subsection (4)] eliminates the possibility of double recovery or other over-compensation arising out of a reduction or elimination of a deficiency under Section 9-626 [30-9A-626], based on noncompliance with the provisions of this Part [Title 30, chapter 9A, part 6] relating to collection, enforcement, disposition, or acceptance. Assuming no double recovery, a debtor whose deficiency is eliminated under Section 9-626 [30-9A-626] may pursue a claim for a surplus. Because Section 9-626 [30-9A-626] does not apply to consumer transactions, the statute is silent as to whether a double recovery or other over-compensation is possible in a consumer transaction.

Damages for violation of the requirements of this Article [Title 30, chapter 9A], including Section 9-609 [30-9A-609], are those reasonably calculated to put an eligible claimant in the position that it would have occupied had no violation occurred. See Section 1-106 [30-1-106]. Subsection (b) [subsection 2] supports the recovery of actual damages for committing a breach of the peace in violation of Section 9-609 [30-9A-609], and principles of tort law supplement this subsection. See Section 1-103 [30-1-103]. However, to the extent that damages in tort compensate the debtor for the same loss dealt with by this Article [Title 30, chapter 9A], the debtor should be entitled to only one recovery.

4. **Minimum Damages in Consumer-Goods Transactions.** Subsection (c)(2) [subsection (3)(b)] provides a minimum, statutory, damage recovery for a debtor and secondary obligor in a consumer-goods transaction. It is patterned on former Section 9-507(1) [30-9-507(1), now repealed] and is designed to ensure that every noncompliance with the requirements of Part 6 [Title 30, chapter 9A, part 6] in a consumer-goods transaction results in liability, regardless of any injury that may have resulted. Subsection (c)(2) [subsection (3)(b)] leaves the treatment of statutory damages as it was under former Article 9 [Title 30, chapter 9, now repealed]. A secured party is not liable for statutory damages under this subsection more than once with respect to any one secured obligation (see Section 9-628(e) [30-9A-628(5)]), nor is a secured party liable under this subsection for failure to comply with Section 9-616 [30-9A-616] (see Section 9-628(d) [30-9A-628(4)]).

Following former Section 9-507(1) [30-9-507(1), now repealed], this Article [Title 30, chapter 9A] does not include a definition or explanation of the terms "credit service charge," "principal amount," "time-price differential," or "cash price," as used in subsection (c)(2) [subsection (3)(b)]. It leaves their construction and application to the court, taking into account the subsection's purpose of providing a minimum recovery in consumer-goods transactions.

5. **Supplemental Damages.** Subsections (e) and (f) [subsection (5) and (6)] provide damages that supplement the recovery, if any, under subsection (b) [subsection (2)]. Subsection (e) [subsection (5)] imposes an additional $500 liability upon a person who fails to comply with the provisions specified in that subsection, and subsection (f) [subsection (6)] imposes like damages on a person who, without reasonable excuse, fails to comply with a request for an accounting or a request regarding a list of collateral or statement of account under Section 9-210 [30-9A-210]. However, under subsection (f) [subsection (6)], a person has a reasonable excuse for the failure if the person never claimed an interest in the collateral or obligations that were the subject of the request.

6. **Estoppel.** Subsection (g) [subsection (7)] limits the extent to which a secured party who fails to comply with a request regarding a list of collateral or statement of account may claim a security interest.

Compiler's Comments

2001 Amendment: Chapter 179 near beginning of (2) substituted "person" for "secured party" and after "failure to comply" deleted "with a request under 30-9-220". Amendment effective July 1, 2001.

Case Notes

CASES DECIDED PRIOR TO 1999 REVISION

Commercial Reasonableness of Agisters' Lien Sale: Appellants claimed the sale of horses at an agisters' lien sale was not commercially reasonable because the horses were sold in lots at less than their value. Looking to 30-9-507 (now repealed, see 30-9A-625 and 30-9A-627) for guidance, the Supreme Court stated that the sale of horses at a low price in lots instead of individually did not make the sale commercially unreasonable. Testimony indicated that horses were often sold in this manner and could have been sold individually if a bidder had so requested. Rose v. Myers, 223 M 13, 724 P2d 176, 43 St. Rep. 1493 (1986).

Price Discrepancy Bearing on Commercial Reasonableness: Plaintiff bought a photography business and executed a promissory note with defendant. As collateral he assigned stock in the business. Plaintiff sold the business to Wolfe. Wolfe was to make payments to defendant to discharge his obligations, and these payments were to be directly applied to plaintiff's obligation under the promissory note. Defendant was escrow agent. Plaintiff later signed a financing statement granting defendant a security interest in the stock held in escrow. The defendant filed the security agreement. Wolfe became delinquent in his payments, and defendant notified plaintiff his payments were therefore delinquent. A later letter was sent by certified mail to the same address advising plaintiff the stock would be sold and applied to plaintiff's past-due loan. At the sale Wolfe bought the stock for the amount due on plaintiff's note. Plaintiff contended the sale of the collateral was not conducted in a commercially reasonable manner as indicated by the low price received. The Supreme Court held that a large discrepancy in price may be considered in determining commercial reasonableness but that the complaining party has the burden of showing the price received was less than the fair market value of the collateral. The court did not find substantial evidence to support the contention. Dulan v. Mont. Nat'l Bank of Roundup, 203 M 177, 661 P2d 28, 40 St. Rep. 376 (1983), followed in Owen v. Ostrum, 259 M 249, 855 P2d 1015, 50 St. Rep. 779 (1993). See also Auto Credit, Inc. v. Long, 1998 MT 327, 292 M 238, 971 P2d 1237, 55 St. Rep. 1326 (1998).

Commercially Reasonable: The reasonableness of the sale is determined not by the price that is ultimately received for the collateral, but by the manner in which the sale is conducted; and where defendant acted in good faith and even transported collateral to auction in another state hoping to find a better market, he conducted the sale in a commercially reasonable manner. James Talcott, Inc. v. Reynolds, 165 M 404, 529 P2d 352 (1974).

Compliance With Notice Provisions: Plaintiff complied with notice provisions of the Uniform Commercial Code when he sent notice of foreclosure sale to debtor by ordinary mail, since the receipt of mail is presumed if the procedure of the mailing is carried out in a regular manner. James Talcott, Inc. v. Reynolds, 165 M 404, 529 P2d 352 (1974).

30-9A-626. Action in which deficiency or surplus is in issue.

Official Comments

1. **Source.** New.

2. **Scope.** The basic damage remedy under Section 9-625(b) [30-9A-625(2)] is subject to the special rules in this section for transactions other than consumer transactions. This section addresses situations in which the amount of a deficiency or surplus is in issue, i.e., situations in which the secured party has collected, enforced, disposed of, or accepted the collateral. It contains special rules applicable to a determination of the amount of a deficiency or surplus. Because this section affects a person's liability for a deficiency, it is subject to Section 9-628 [30-9A-628], which should be read in conjunction with Section 9-605 [30-9A-605]. The rules in this section apply only to noncompliance in connection with the "collection, enforcement, disposition, or acceptance" under Part 6 [Title 30, chapter 9A, part 6]. For other types of noncompliance with Part 6 [Title 30, chapter 9A, part 6], the general liability rule of Section 9-625(b) [30-9A-625(2)]-recovery of actual damages-applies. Consider, for example, a repossession that does not comply with Section 9-609 [30-9A-609] for want of a default. The debtor's remedy is under Section 9-625(b) [30-9A-625(2)]. In a proper case, the secured party also may be liable for conversion under non-UCC law. If the secured party thereafter disposed of the collateral, however, it would violate Section 9-610 [30-9A-610] at that time, and this section would apply.

3. **Rebuttable Presumption Rule.** Subsection (a) [subsection 1] establishes the rebuttable presumption rule for transactions other than consumer transactions. Under paragraph (1) [subsection (1)(a)], the secured party need not prove compliance with the relevant provisions of this Part [Title 30, chapter 9A, part 6] as part of its prima facie case. If, however, the debtor or a secondary obligor raises the issue (in accordance with the forum's rules of pleading and practice),

then the secured party bears the burden of proving that the collection, enforcement, disposition, or acceptance complied. In the event the secured party is unable to meet this burden, then paragraph (3) [subsection (1)(c)] explains how to calculate the deficiency. Under this rebuttable presumption rule, the debtor or obligor is to be credited with the greater of the actual proceeds of the disposition or the proceeds that would have been realized had the secured party complied with the relevant provisions. If a deficiency remains, then the secured party is entitled to recover it. The references to "the secured obligation, expenses, and attorney's fees" in paragraphs (3) and (4) [subsections (1)(c) and (1)(d)] embrace the application rules in Sections 9-608(a) and 9-615(a) [30-9A-608(1) and 30-9A-615(1)].

Unless the secured party proves that compliance with the relevant provisions would have yielded a smaller amount, under paragraph (4) [subsection (1)(d)] the amount that a complying collection, enforcement, or disposition would have yielded is deemed to be equal to the amount of the secured obligation, together with expenses and attorney's fees. Thus, the secured party may not recover any deficiency unless it meets this burden.

4. **Consumer Transactions.** Although subsection (a) [subsection (1)] adopts a version of the rebuttable presumption rule for transactions other than consumer transactions, with certain exceptions Part 6 [Title 30, chapter 9A, part 6] does not specify the effect of a secured party's noncompliance in consumer transactions. (The exceptions are the provisions for the recovery of damages in Section 9-625 [30-9A-625].) Subsection (b) [subsection 2] provides that the limitation of subsection (a) [subsection (1)] to transactions other than consumer transactions is intended to leave to the court the determination of the proper rules in consumer transactions. It also instructs the court not to draw any inference from the limitation as to the proper rules for consumer transactions and leaves the court free to continue to apply established approaches to those transactions.

Courts construing former Section 9-507 [30-9-507, now repealed, see 30-9A-625 and 30-9A-627] disagreed about the consequences of a secured party's failure to comply with the requirements of former Part 5 [Title 30, chapter 9, part 5, now repealed]. Three general approaches emerged. Some courts have held that a noncomplying secured party may not recover a deficiency (the "absolute bar" rule). A few courts held that the debtor can offset against a claim to a deficiency all damages recoverable under former Section 9-507 [30-9-507, now repealed, see 30-9A-625 and 30-9A-627] resulting from the secured party's noncompliance (the "offset" rule). A plurality of courts considering the issue held that the noncomplying secured party is barred from recovering a deficiency unless it overcomes a rebuttable presumption that compliance with former Part 5 [Title 30, chapter 9, part 5, now repealed] would have yielded an amount sufficient to satisfy the secured debt. In addition to the nonuniformity resulting from court decisions, some States enacted special rules governing the availability of deficiencies.

5. **Burden of Proof When Section 9-615(f) [30-9A-615(6)] Applies.** In a non-consumer transaction, subsection (a)(5) [subsection (1)(e)] imposes upon a debtor or obligor the burden of proving that the proceeds of a disposition are so low that, under Section 9-615(f) [30-9A-615(6)], the actual proceeds should not serve as the basis upon which a deficiency or surplus is calculated. Were the burden placed on the secured party, then debtors might be encouraged to challenge the price received in every disposition to the secured party, a person related to the secured party, or a secondary obligor.

6. **Delay in Applying This Section.** There is an inevitable delay between the time a secured party engages in a noncomplying collection, enforcement, disposition, or acceptance and the time of a subsequent judicial determination that the secured party did not comply with Part 6 [Title 30, chapter 9A, part 6]. During the interim, the secured party, believing that the secured obligation is larger than it ultimately is determined to be, may continue to enforce its security interest in collateral. If some or all of the secured indebtedness ultimately is discharged under this section, a reasonable application of this section would impose liability on the secured party for the amount of any excess, unwarranted recoveries but would not make the enforcement efforts wrongful.

30-9A-627. Determination of whether conduct was commercially reasonable.

Official Comments

1. **Source.** Former Section 9-507(2) [30-9-507(2), now repealed].

2. **Relationship of Price to Commercial Reasonableness.** Some observers have found the notion contained in subsection (a) [subsection (1)] (derived from former Section 9-507(2) [30-9-507(2), now repealed]) (the fact that a better price could have been obtained does not establish lack of commercial reasonableness) to be inconsistent with that found in Section

9-610(b) [30-9A-610(2)] (derived from former Section 9-504(3) [30-9-504(3), now repealed] (every aspect of the disposition, including its terms, must be commercially reasonable). There is no such inconsistency. While not itself sufficient to establish a violation of this Part, a low price suggests that a court should scrutinize carefully all aspects of a disposition to ensure that each aspect was commercially reasonable.

The law long has grappled with the problem of dispositions of personal and real property which comply with applicable procedural requirements (e.g., advertising, notification to interested persons, etc.) but which yield a price that seems low. This Article [Title 30, chapter 9A] addresses that issue in Section 9-615(f) [30-9A-615(6)]. That section applies only when the transferee is the secured party, a person related to the secured party, or a secondary obligor. It contains a special rule for calculating a deficiency or surplus in a complying disposition that yields a price that is "significantly below the range of proceeds that a complying disposition to a person other than the secured party, a person related to the secured party, or a secondary obligor would have brought."

3. **Determination of Commercial Reasonableness; Advance Approval.** It is important to make clear the conduct and procedures that are commercially reasonable and to provide a secured party with the means of obtaining, by court order or negotiation with a creditors' committee or a representative of creditors, advance approval of a proposed method of enforcement as commercially reasonable. This section contains rules that assist in that determination and provides for advance approval in appropriate situations. However, none of the specific methods of disposition specified in subsection (b) [subsection (2)] is required or exclusive.

4. **"Recognized Market."** As in Sections 9-610(c) and 9-611(d) [30-9A-610(3) and 30-9A-611(4)], the concept of a "recognized market" in subsections (b)(1) and (2) [subsections (2)(a) and (2)(b)] is quite limited; it applies only to markets in which there are standardized price quotations for property that is essentially fungible, such as stock exchanges.

30-9A-628. Nonliability and limitation on liability of secured party — liability of secondary obligor.

Official Comments

1. **Source.** New.

2. **Exculpatory Provisions.** Subsections (a), (b), and (c) [subsections (1), (2), and (3)] contain exculpatory provisions that should be read in conjunction with Section 9-605 [30-9A-605]. Without this group of provisions, a secured party could incur liability to unknown persons and under circumstances that would not allow the secured party to protect itself. The broadened definition of the term "debtor" underscores the need for these provisions.

If a secured party reasonably, but mistakenly, believes that a consumer transaction or consumer-goods transaction is a non-consumer transaction or non-consumer-goods transaction, and if the secured party's belief is based on its reasonable reliance on a representation of the type specified in subsection (c)(1) or (c)(2) [subsection (3)(a) or (3)(b)], then this Article [Title 30, chapter 9A] should be applied as if the facts reasonably believed and reasonably relied upon were true. For example, if a secured party reasonably believed that a transaction was a non-consumer transaction and its belief was based on reasonable reliance on the debtor's misrepresentation that the collateral secured an obligation incurred for business purposes, the rebuttable presumption rule would apply under 9-626(b) [30-9A-626(2)]. Of course, if the secured party's belief is not reasonable or, even if reasonable, is not based on reasonable reliance on the debtor's misrepresentation, this limitation on liability is inapplicable.

3. **Inapplicability of Statutory Damages to Section 9-616 [30-9A-616].** Subsection (d) [subsection (4)] excludes noncompliance with Section 9-616 [30-9A-616] entirely from the scope of statutory damage liability under Section 9-625(c)(2) [30-9A-625(3)(b)].

4. **Single Liability for Statutory Minimum Damages.** Subsection (e) [subsection (5)] ensures that a secured party will incur statutory damages only once in connection with any one secured obligation.

Part 7
Transition

Part Official Comments

Source. Section 9-701 [Effective Date — Section 171, Ch. 305, L. 1999].

A uniform law as complex as Article 9 [Title 30, chapter 9A] necessarily gives rise to difficult problems and uncertainties during the transition to the new law. As is customary for uniform laws, this Article [Title 30, chapter 9A] is based on the general assumption that all States will have enacted substantially identical versions. While always important, uniformity is essential to the success of this Article [Title 30, chapter 9A]. If former Article 9 [Title 30, chapter 9, now repealed] is in effect in some jurisdictions, and this Article [Title 30, chapter 9A] is in effect in others, horrendous complications may arise. For example, the proper place in which to file to perfect a security interest (and thus the status of a particular security interest as perfected or unperfected) would depend on whether the matter was litigated in a State in which former Article 9 [Title 30, chapter 9, now repealed] was in effect or a State in which this Article [Title 30, chapter 9A] was in effect. Accordingly, this section [section 171, Ch. 305, L. 1999, not codified] contemplates that States will adopt a uniform effective date for this Article [Title 30, chapter 9A]. Any one State's failure to adopt the uniform effective date will greatly increase the cost and uncertainty surrounding the transition.

Other problems arise from transactions and relationships that were entered into under former Article 9 [Title 30, chapter 9, now repealed] or under non-UCC law and which remain outstanding on the effective date of this Article [Title 30, chapter 9A]. The difficulties arise primarily because this Article [Title 30, chapter 9A] expands the scope of former Article 9 [Title 30, chapter 9, now repealed] to cover additional types of collateral and transactions and because it provides new methods of perfection for some types of collateral, different priority rules, and different choice-of-law rules governing perfection and priority. This Section [section 171, Ch. 305, L. 1999, not codified] and the other sections in this Part [30-9A-703 through 30-9A-706, 30-9A-708, and 30-9A-709] address primarily this second set of problems.

Source. Section 9-702 [Savings Provisions — Section 169, Ch. 305, L. 1999].

1. **Pre-Effective-Date Transactions.** Subsection (a) [subsection 1] contains the general rule that this Article [Title 30, chapter 9A] applies to transactions, security interests, and other liens within its scope (see Section 9-109 [30-9A-109]), even if the transaction or lien was entered into or created before the effective date. Thus, secured transactions entered into under former Article 9 [Title 30, chapter 9, now repealed] must be terminated, completed, consummated, and enforced under this Article [Title 30, chapter 9A]. Subsection (b) [subsection 2] is an exception to the general rule. It applies to valid, pre-effective-date transactions and liens that were not governed by former Article 9 [Title 30, chapter 9, now repealed] but would be governed by this Article [Title 30, chapter 9A] if they had been entered into or created after this Article [Title 30, chapter 9A] takes effect. Under subsection (b) [subsection (2)], these valid transactions, such as the creation of agricultural liens and security interests in commercial tort claims, retain their validity under this Article [Title 30, chapter 9A] and may be terminated, completed, consummated, and enforced under this Article [Title 30, chapter 9A]. However, these transactions also may be terminated, completed, consummated, and enforced by the law that otherwise would apply had this Article [Title 30, chapter 9A] not taken effect.

2. **Judicial Proceedings Commenced Before Effective Date.** As is usual in transition provisions, subsection (c) [subsection (3)] provides that this Article [Title 30, chapter 9A] does not affect litigation pending on the effective date.

Part Compiler's Comments

Saving Clause: Section 169, Ch. 305, L. 1999, provided: "(1) Except as otherwise provided in [sections 164 through 169] [sections 162 through 167—30-9A-703 through 30-9A-706, 30-9A-708, and 30-9A-709], [this act] applies to a transaction or lien within its scope, even if the transaction or lien was entered into or created before [this act] takes effect.

(2) Except as otherwise provided in subsection (3) and [sections 164 through 169] [sections 162 through 167—30-9A-703 through 30-9A-706, 30-9A-708, and 30-9A-709]:

(a) transactions and liens that were not governed by [former chapter 9, now repealed] were validly entered into or created before [this act] takes effect and would be subject to [this act] if they had been entered into or created after [this act] takes effect, and the rights, duties, and interests flowing from those transactions and liens remain valid after [this act] takes effect; and

(b) the transactions and liens may be terminated, completed, consummated, or enforced as required or permitted by [this act] or by the law that otherwise would apply if [this act] did not take effect.

(3) [This act] does not affect an action, case, or proceeding commenced before [this act] takes effect."

30-9A-703. Security interest perfected before July 1, 2001.

Official Comments

Source. Section 9-703 [Security Interest Perfected Before Effective Date — 30-9A-703].

1. Perfected Security Interests Under Former Article 9 [Title 30, chapter 9, now repealed] and this Article [Title 30, chapter 9A]. This section deals with security interests that are perfected

(i.e., that are enforceable and have priority over the rights of a lien creditor) under former Article 9 [Title 30, chapter 9, now repealed] or other applicable law immediately before this Article [Title 30, chapter 9A] takes effect. Subsection (a) [subsection 1] provides, not surprisingly, that if the security interest would be a perfected security interest under this Article [Title 30, chapter 9A] (i.e., if the transaction satisfies this Article's [Title 30, chapter 9A] requirements for enforceability (attachment) and perfection), no further action need be taken for the security interest to be a perfected security interest.

2. **Security Interests Enforceable and Perfected Under Former Article 9 [Title 30, chapter 9, now repealed] but Unenforceable or Unperfected Under this Article [Title 30, chapter 9A].** Subsection (b) [subsection 2] deals with security interests that are enforceable and perfected under former Article 9 [Title 30, chapter 9, now repealed] or other applicable law immediately before this Article [Title 30, chapter 9A] takes effect but do not satisfy the requirements for enforceability (attachment) or perfection under this Article [Title 30, chapter 9A]. Except as otherwise provided in Section 9-705 [30-9A-705], these security interests are perfected security interests for one year after the effective date. If the security interest satisfies the requirements for attachment and perfection within that period, the security interest remains perfected thereafter. If the security interest satisfies only the requirements for attachment within that period, the security interest becomes unperfected at the end of the one-year period.

Example 1: A pre-effective-date security agreement in a consumer transaction covers "all securities accounts." The security interest is properly perfected. The collateral description was adequate under former Article 9 [Title 30, chapter 9, now repealed] (see former Section 9-115(3) [30-9-115(3), now repealed, see 30-9A-108]) but is insufficient under this Article [Title 30, chapter 9A] (see Section 9-108(e)(2) [30-9A-108(5)(b)]). Unless the debtor authenticates a new security agreement describing the collateral other than by "type" (or Section 9-203(b)(3) [30-9A-203(2)(c)] otherwise is satisfied) within the one-year period following the effective date, the security interest becomes unenforceable at the end of that period.

Other examples under former Article 9 [Title 30, chapter 9, now repealed] or other applicable law that may be effective as attachment or enforceability steps but may be ineffective under this Article [Title 30, chapter 9A] include an oral agreement to sell a payment intangible or possession by virtue of a notification to a bailee under former Section 9-305 [30-9-305, now repealed, see 30-9A-313]. Neither the oral agreement nor the notification would satisfy the revised Section 9-203 [30-9A-203] requirements for attachment.

Example 2: A pre-effective-date possessory security interest in instruments is perfected by a bailee's receipt of notification under former 9-305 [30-9-305, now repealed, see 30-9A-313]. The bailee has not, however, acknowledged that it holds for the secured party's benefit under revised Section 9-313 [30-9A-313]. Unless the bailee authenticates a record acknowledging that it holds for the secured party (or another appropriate perfection step is taken) within the one-year period following the effective date, the security interest becomes unperfected at the end of that period.

3. **Interpretation of Pre-Effective-Date Security Agreements.** Section 9-102 [30-9A-102] defines "security agreement" as "an agreement that creates or provides for a security interest." Under Section 1-201(3) [30-1-201(3)], an "agreement" is a "bargain of the parties in fact." If parties to a pre-effective-date security agreement describe the collateral by using a term defined in former Article 9 [Title 30, chapter 9, now repealed] in one way and defined in this Article [Title 30, chapter 9A] in another way, in most cases it should be presumed that the bargain of the parties contemplated the meaning of the term under former Article 9 [Title 30, chapter 9, now repealed].

Example 3: A pre-effective-date security agreement covers "all accounts" of a debtor. As defined under former Article 9 [Title 30, chapter 9, now repealed], an "account" did not include a right to payment for lottery winnings. These rights to payment are "accounts" under this Article [Title 30, chapter 9A], however. The agreement of the parties presumptively created a security interest in "accounts" as defined in former Article 9 [Title 30, chapter 9, now repealed]. A different result might be appropriate, for example, if the security agreement explicitly contemplated future changes in the Article 9 [Title 30, chapter 9A] definitions of types of collateral-e.g., "'Accounts' means 'accounts' as defined in the UCC Article 9 [Title 30, chapter 9A] of [State X], as that definition may be amended from time to time." Whether a different approach is appropriate in any given case depends on the bargain of the parties, as determined by applying ordinary principles of contract construction.

Compiler's Comments

Effective Date: Section 171, Ch. 305, L. 1999, provided that this section is effective July 1, 2001.

30-9A-704. Security interest unperfected before July 1, 2001.

Official Comments

Source. Section 9-704 [Security Interest Unperfected Before Effective Date — 30-9A-704].

This section deals with security interests that are enforceable but unperfected (i.e., subordinate to the rights of a person who becomes a lien creditor) under former Article 9 [Title 30, chapter 9, now repealed] or other applicable law immediately before this Article [Title 30, chapter 9A] takes effect. These security interests remain enforceable for one year after the effective date, and thereafter if the appropriate steps for attachment under this Article [Title 30, chapter 9A] are taken before the one-year period expires. (This section's treatment of enforceability is the same as that of Section 9-703 [30-9A-703].) The security interest becomes a perfected security interest on the effective date if, at that time, the security interest satisfies the requirements for perfection under this Article [Title 30, chapter 9A]. If the security interest does not satisfy the requirements for perfection until sometime thereafter, it becomes a perfected security interest at that later time.

Example: A security interest has attached under former Article 9 [Title 30, chapter 9, now repealed] but is unperfected because the filed financing statement covers "all of debtor's personal property" and controlling case law in the applicable jurisdiction has determined that this identification of collateral in a financing statement is insufficient. Upon the effective date of this Article [Title 30, chapter 9A], the financing statement becomes sufficient under Section 9-504(2) [30-9A-504(2)]. On that date the security interest becomes perfected. (This assumes, of course, that the financing statement is filed in the proper filing office under this Article [Title 30, chapter 9A].)

Compiler's Comments

Effective Date: Section 171, Ch. 305, L. 1999, provided that this section is effective July 1, 2001.

30-9A-705. Effectiveness of action taken before effective date of act.

Official Comments

Source. Section 9-705 [Effectiveness of Action Taken Before Effective Date of Act — 30-9A-705].

1. **General.** This section addresses primarily the situation in which the perfection step is taken under former Article 9 [Title 30, chapter 9, now repealed] or other applicable law before the effective date of this Article [Title 30, chapter 9A], but the security interest does not attach until after that date.

2. **Perfection Other Than by Filing.** Subsection (a) [subsection 1] applies when the perfection step is a step other than the filing of a financing statement. If the step that would be a valid perfection step under former Article 9 [Title 30, chapter 9, now repealed] or other law is taken before this Article [Title 30, chapter 9A] takes effect, and if a security interest attaches within one year after this Article [Title 30, chapter 9A] takes effect, then the security interest becomes a perfected security interest upon attachment. However, the security interest becomes unperfected one year after the effective date unless the requirements for attachment and perfection under this Article [Title 30, chapter 9A] are satisfied within that period.

3. **Perfection by Filing: Ineffective Filings Made Effective.** Subsection (b) [subsection 2] deals with financing statements that were filed under former Article 9 [Title 30, chapter 9, now repealed] and which would not have perfected a security interest under the former Article [Title 30, chapter 9, now repealed] (because, e.g., they did not accurately describe the collateral or were filed in the wrong place), but which would perfect a security interest under this Article [Title 30, chapter 9A]. Under subsection (b) [subsection (2)], such a financing statement is effective to perfect a security interest to the extent it complies with this Article [Title 30, chapter 9A]. Subsection (b) [subsection 2] applies regardless of the reason for the filing. For example, a secured party need not wait until the effective date to respond to the change this Article [Title 30, chapter 9A] makes with respect to the jurisdiction whose law governs perfection of certain security interests. Rather, a secured party may wish to prepare for this change by filing a financing statement before the effective date in the jurisdiction whose law governs perfection under this Article [Title 30, chapter 9A]. When this Article [Title 30, chapter 9A] takes effect, the filing becomes effective to perfect a security interest (assuming the filing satisfies the perfection requirements of this Article [Title 30, chapter 9A]). Note, however, that Section 9-706 [30-9A-706] determines whether a financing statement filed before the effective date operates to continue the effectiveness of a financing statement filed in another office before the effective date.

4. **Perfection by Filing: Change in Applicable Law.** Subsection (c) [subsection (3)] provides that a financing statement filed in the proper jurisdiction under former Section 9-103

[30-9-103, now repealed, see 30-9A-301 and 30-9A-316] remains effective for all purposes, despite the fact that Part 3 of this Article [Title 30, chapter 9A, part 3] would require filing of a financing statement in a different jurisdiction. This means that, during the early years of this Article's [Title 30, chapter 9A] effectiveness, it may be necessary to search the files not only in the jurisdiction whose law governs perfection under this Article [Title 30, chapter 9A] but also (if different) in the jurisdiction(s) whose law governed perfection under former Article 9 [Title 30, chapter 9, now repealed]. To limit this burden, subsection (c) [subsection (3)] provides that a financing statement filed in the jurisdiction determined by former Section 9-103 [30-9-103, now repealed, see 30-9A-301 and 30-9A-316] becomes ineffective at the earlier of the time it would become ineffective under the law of that jurisdiction or June 30, 2006. The June 30, 2006, limitation addresses some nonuniform versions of former Article 9 [Title 30, chapter 9, now repealed] that extended the effectiveness of a financing statement beyond five years. Note that a financing statement filed before the effective date may remain effective beyond June 30, 2006, if subsection (d) [subsections (3) and (4)] (concerning continuation statements) or (e) [not adopted in Montana] (concerning transmitting utilities) or Section 9-706 [30-9A-706] (concerning initial financing statements that operate to continue pre-effective-date financing statements) so provides.

Subsection (c) [subsection (3)] is an exception to Section 9-703(b) [30-9A-703(2)]. Under the general rule in Section 9-703(b) [30-9A-703(2)], a security interest that is enforceable and perfected on the effective date of this Article [Title 30, chapter 9A] is a perfected security interest for one year after this Article [Title 30, chapter 9A] takes effect, even if the security interest is not enforceable under this Article [Title 30, chapter 9A] and the applicable requirements for perfection under this Article [Title 30, chapter 9A] have not been met. However, in some cases subsection (c) [subsection (3)] may shorten the one-year period of perfection; in others, if the security interest is enforceable under Section 9-203 [30-9A-203], it may extend the period of perfection. A financing statement that remains effective under subsection (c) [subsection (3)] may be amended (but generally may not be continued) after this Article [Title 30, chapter 9A] takes effect by filing an amendment in the office where the financing statement was filed.

Example 1: On July 3, 1996, D, a State X corporation, creates a security interest in certain manufacturing equipment located in State Y. On July 6, 1996, SP perfects a security interest in the equipment under former Article 9 [Title 30, chapter 9, now repealed] by filing in the office of the State Y Secretary of State. See former Section 9-103(1)(b) [30-9-103(1)(b), now repealed, see 30-9A-301]. This Article [Title 30, chapter 9A] takes effect in States X and Y on July 1, 2001. Under Section 9-705(c) [subsection (3)], the financing statement remains effective for the first five days of July, 2001, after which it lapses. See former Section 9-403 [30-9-403, now repealed, see 30-9A-515 and 30-9A-516]. Had SP continued the effectiveness of the financing statement by filing a continuation statement in State Y under former Article 9 [Title 30, chapter 9, now repealed] before July 1, 2001, the financing statement would have remained effective to perfect the security interest through June 30, 2006. See subsection (c)(2) [subsection (3)(a)(ii)]. Alternatively, SP could have filed an initial financing statement in State X under subsection (b) [subsection (2)] or Section 9-706 [30-9A-706] before the State Y financing statement lapsed. Had SP done so, the security interest would have remained perfected without interruption until the State X financing statement lapsed.

5. **Continuing Effectiveness of Filed Financing Statement.** A financing statement filed before the effective date of this Article [Title 30, chapter 9A] may be continued only by filing in the State and office designated by this Article [Title 30, chapter 9A]. This result is accomplished in the following manner: Subsection (d) [subsection (5)(b)] indicates that, as a general matter, a continuation statement filed after the effective date of this Article [July 1, 2001] does not continue the effectiveness of a financing statement filed under the law designated by former Section 9-103 [30-9-103, now repealed, see 30-9A-301 and 30-9A-316]. Instead, an initial financing statement must be filed under Section 9-706 [30-9A-706]. The second sentence of subsection (d) [subsection (5)] contains an exception to the general rule. It provides that a continuation statement is effective to continue the effectiveness of a financing statement filed before this Article [Title 30, chapter 9A] takes effect if this Article [Title 30, chapter 9A] prescribes not only the same jurisdiction but also the same filing office.

Example 2: On November 8, 2000, D, a State X corporation, creates a security interest in certain manufacturing equipment located in State Y. On November 15, 2000, SP perfects a security interest in the equipment under former Article 9 [Title 30, chapter 9, now repealed] by filing in office of the State Y Secretary of State. See former Section 9-103(1)(b) [30-9-103(1)(b), now repealed, see 30-9A-301]. This Article [Title 30, chapter 9A] takes effect in States X and Y on July 1, 2001. Under Section 9-705(c) [subsection (3)(a)(ii)], the financing statement ceases to be effective in November, 2005, when it lapses. See Section 9-515 [30-9A-515]. Under this Article [Title 30, chapter 9A], the law of D's location (State X, see Section 9-307 [30-9A-307]) governs perfection. See Section 9-301 [30-9A-301]. Thus, the filing of a continuation statement in State Y after the effective date would not continue the effectiveness of the financing statement. See subsection (d) [subsection (4)]. However, the effectiveness of the financing statement could be continued under Section 9-706 [30-9A-706].

Example 3: The facts are as in Example 2, except that D is a State Y corporation. Assume State Y adopted former Section 9-401(1) [30-9-401(1), now repealed, see 30-9A-501] (second alternative). State Y law governs perfection under Part 3 of this Article [Title 30, chapter 9A, part 3]. (See Sections 9-301, 9-307 [30-9A-301 and 30-9A-307].) Under the second sentence of subsection (d) [subsection (4) (no second sentence)], the timely filing of a continuation statement in accordance with the law of State Y continues the effectiveness of the financing statement.

Example 4: The facts are as in Example 3, except that the collateral is equipment used in farming operations and, in accordance with former Section 9-401(1) [30-9-401(1), now repealed, see 30-9A-501] (second alternative) as enacted in State Y, the financing statement was filed in State Y, in the office of the Shelby County Recorder of Deeds. Under this Article [Title 30, chapter 9A], a continuation statement must be filed in the office of the State Y Secretary of State. See Section 9-501(a)(2) [30-9A-501(1)(b)]. Under the second sentence of subsection (d) [first sentence of subsection (5)], the timely filing of a continuation statement in accordance with the law of State Y operates to continue a pre-effective-date financing statement only if the continuation statement is filed in the same office as the financing statement. Accordingly, the continuation statement is not effective in this case, but the financing statement may be continued under Section 9-706 [30-9A-706].

Example 5: The facts are as in Example 3, except that State Y enacted former Section 9-401(1) [30-9-401(1), now repealed, see 30-9A-501] (third alternative). As required by former Section 9-401(1) [30-9-401(1), now repealed, see 30-9A-501], SP filed financing statements in both the office of the State Y Secretary of State and the office of the Shelby County Recorder of Deeds. Under this Article [Title 30, chapter 9A], a continuation statement must be filed in the office of the State Y Secretary of State. See Section 9-501(a)(2) [30-9A-501(1)(b)]. The timely filing of a continuation statement in that office after this Article [Title 30, chapter 9A] takes effect would be effective to continue the effectiveness of the financing statement (and thus continue the perfection of the security interest), even if the financing statement filed with the County Recorder lapses.

6. **Continuation Statements.** In some cases, this Article [Title 30, chapter 9A] reclassifies collateral covered by a financing statement filed under former Article 9 [Title 30, chapter 9, now repealed]. For example, collateral consisting of the right to payment for real property sold would be a "general intangible" under the former Article [Title 30, chapter 9, now repealed] but an "account" under this Article [Title 30, chapter 9A]. To continue perfection under those circumstances, a continuation statement must comply with the normal requirements for a continuation statement. See Section 9-515 [30-9A-515]. In addition, the pre-effective-date financing statement and continuation statement, taken together, must satisfy the requirements of this Article [Title 30, chapter 9A] concerning the sufficiency of the debtor's name, secured party's name, and indication of collateral. See subsection (f) [subsection (7)].

Example 6: A pre-effective-date financing statement covers "all general intangibles" of a debtor. As defined under former Article 9 [Title 30, chapter 9, now repealed], a "general intangible," would include rights to payment for lottery winnings. These rights to payment are "accounts" under this Article [Title 30, chapter 9A], however. A post-effective-date continuation statement will not continue the effectiveness of the pre-effective-date financing statement with respect to lottery winnings unless it amends the indication of collateral covered to include lottery winnings (e.g., by adding "accounts," "rights to payment for lottery winnings," or the like). If the continuation statement does not amend the indication of collateral, the continuation statement will be effective to continue the effectiveness of the financing statement only with respect to "general intangibles" as defined in this Article [Title 30, chapter 9A].

Example 7: The facts are as in Example 6, except that the pre-effective-date financing statement covers "all accounts and general intangibles." Even though rights to payment for lottery winnings are "general intangibles" under former Article 9 [Title 30, chapter 9, now repealed] and "accounts" under this Article [Title 30, chapter 9A], a post-effective-date continuation statement would continue the effectiveness of the pre-effective-date financing statement with respect to lottery winnings. There would be no need to amend the indication of collateral covered, inasmuch as the indication ("accounts") satisfies the requirements of this Article [Title 30, chapter 9A].

Compiler's Comments

2001 Amendment: Chapter 179 inserted (5) concerning application to statement filed by transmitting utility; and made minor changes in style. Amendment effective July 1, 2001.

30-9A-706. When initial financing statement suffices as continuation statement.

Official Comments

Source. Section 9-706 [When Initial Financing Statement Suffices as Continuation Statement — 30-9A-706].

1. **Continuation of Financing Statements Not Filed in Proper Filing Office Under this Article [Title 30, chapter 9A].** This section deals with continuing the effectiveness of financing statements that are filed in the proper State and office under former Article 9 [Title 30, chapter 9, now repealed], but which would be filed in the wrong State or in the wrong office of the proper State under this Article [Title 30, chapter 9A]. Section 9-705(d) [30-9A-705(5)(b)] provides that, under these circumstances, filing a continuation statement after the effective date of this Article [July 1, 2001] in the office designated by former Article 9 [Title 30, chapter 9, now repealed] would not be effective. This section provides the means by which the effectiveness of such a financing statement can be continued if this Article [Title 30, chapter 9A] governs perfection under the applicable choice-of-law rule: filing an initial financing statement in the office specified by Section 9-501 [30-9A-501].

Although it has the effect of continuing the effectiveness of a pre-effective-date financing statement, an initial financing statement described in this section is not a continuation statement. Rather, it is governed by the rules applicable to initial financing statements. (However, the debtor need not authorize the filing. See Section 9-707 [30-9A-708].) Unlike a continuation statement, the initial financing statement described in this section may be filed any time during the effectiveness of the pre-effective-date financing statement—even before this Article [Title 30, chapter 9A] is enacted—and not only within the six months immediately prior to lapse. In contrast to a continuation statement, which extends the lapse date of a filed financing statement for five years, the initial financing statement has its own lapse date, which bears no relation to the lapse date of the pre-effective-date financing statement whose effectiveness the initial financing statement continues. See subsection (b) [subsection (2)].

As subsection (a) [subsection (1)] makes clear, the filing of an initial financing statement under this section continues the effectiveness of a pre-effective-date financing statement. If the effectiveness of a pre-effective-date financing statement lapses before the initial financing statement is filed, the effectiveness of the pre-effective-date financing statement cannot be continued. Rather, unless the security interest is perfected otherwise, there will be a period during which the security interest is unperfected before becoming perfected again by the filing of the initial financing statement under this section.

If an initial financing statement is filed under this section before the effective date of this Article [Title 30, chapter 9A], it takes effect when this Article [Title 30, chapter 9A] takes effect (assuming that it is ineffective under former Article 9 [Title 30, chapter 9, now repealed]). Note, however, that former Article 9 [Title 30, chapter 9, now repealed] determines whether the filing office is obligated to accept such an initial financing statement. For the reason given in the preceding paragraph, an initial financing statement filed before the effective date of this Article [Title 30, chapter 9A] does not continue the effectiveness of a pre-effective-date financing statement unless the latter remains effective on the effective date of this Article [Title 30, chapter 9A]. Thus, for example, if the effectiveness of the pre-effective-date financing statement lapses before this Article [Title 30, chapter 9A] takes effect, the initial financing statement would not continue its effectiveness.

2. **Requirements of Initial Financing Statement Filed in Lieu of Continuation Statement.** Subsection (c) [subsection (2)] sets forth the requirements for the initial financing statement under subsection (a) [subsection (1)]. These requirements are needed to inform searchers that the initial financing statement operates to continue a financing statement filed elsewhere and to enable searchers to locate and discover the attributes of the other financing statement. The notice-filing policy of this Article applies to the initial financing statements described in this section. Accordingly, an initial financing statement that substantially satisfies the requirements of subsection (c) [subsection (3)] is effective, even if it has minor errors or omissions, unless the errors or omissions make the financing statement seriously misleading. See Section 9-506 [30-9A-506].

A single initial financing statement may continue the effectiveness of more than one financing statement filed before this Article's effective date [July 1, 2001]. See Section 1-106 [30-1-102] (words in the singular include the plural). If under this Article [Title 30, chapter 9A] the collateral is of a type different from its type under former Article 9 [Title 30, chapter 9, now repealed]—as would be the case, e.g., with a right to payment of lottery winnings (a "general intangible" under former Article 9 [Title 30, chapter 9, now repealed] and an "account" under this Article [Title 30, chapter 9A]), then subsection (c) [subsection (2)(a)] requires that the initial financing statement indicate the type under this Article [Title 30, chapter 9A].

Compiler's Comments

Effective Date: Section 171, Ch. 305, L. 1999, provided that this section is effective July 1, 2001.

30-9A-707. Amendment of preeffective-date financing statement.

Compiler's Comments

Effective Date: Section 26, Ch. 179, L. 2001, provided that this section is effective July 1, 2001.

30-9A-708. Persons entitled to file initial financing statement or continuation of statement.

Official Comments

Source. Section 9-707 [Persons Entitled to File Initial Financing Statement or Continuation of Statement — 30-9A-708].

This section permits a secured party to file an initial financing statement or continuation statement necessary under this Part [30-9A-703 through 30-9A-706, 30-9A-708, and 30-9A-709] to continue the effectiveness of a financing statement filed before this Article [Title 30, chapter 9A] takes effect or to perfect or otherwise continue the perfection of a security interest. Because a filing described in this section typically operates to continue the effectiveness of a financing statement whose filing the debtor already has authorized, this section does not require authorization from the debtor.

Compiler's Comments

Effective Date: Section 171, Ch. 305, L. 1999, provided that this section is effective July 1, 2001.

30-9A-709. Priority.

Official Comments

Source. Section 9-708 [Priority — 30-9A-709].

1. **Law Governing Priority.** Ordinarily, this Article [Title 30, chapter 9A] determines the priority of conflicting claims to collateral. However, when the relative priorities of the claims were established before this Article [Title 30, chapter 9A] takes effect, former Article 9 [Title 30, chapter 9, now repealed] governs.

Example 1: In 1999, SP-1 obtains a security interest in a right to payment for goods sold ("account"). SP-1 fails to file a financing statement. This Article [Title 30, chapter 9A] takes effect on July 1, 2001. Thereafter, on August 1, 2001, D creates a security interest in the same account in favor of SP-2, who files a financing statement. This Article [Title 30, chapter 9A] determines the relative priorities of the claims. SP-2's security interest has priority under Section 9-322(a)(1) [30-9A-322(1)(a)].

Example 2: In 1999, SP-1 obtains a security interest in a right to payment for goods sold ("account"). SP-1 fails to file a financing statement. In 2000, D creates a security interest in the same account in favor of SP-2, who likewise fails to file a financing statement. This Article [Title 30, chapter 9A] takes effect on July 1, 2001. Because the relative priorities of the security interests were established before the effective date of this Article [Title 30, chapter 9A], former Article 9 [Title 30, chapter 9, now repealed] governs priority, and SP-1's security interest has priority under former Section 9-312(5)(b) [30-9-312(5)(b), now repealed, see 30-9A-322(1)(a)].

Example 3: The facts are as in Example 2, except that, on August 1, 2001, SP-2 files a proper financing statement under this Article [Title 30, chapter 9A]. Until August 1, 2001, the relative priorities of the security interests were established before the effective date of this Article [Title 30, chapter 9A], as in Example 2. However, by taking the affirmative step of filing a financing statement, SP-2 established anew the relative priority of the conflicting claims after the effective date. Thus, this Article [Title 30, chapter 9A] determines priority. SP-2's security interest has priority under Section 9-322(a)(1) [30-9A-322(1)(a)].

As Example 3 illustrates, relative priorities that are "established" before the effective date do not necessarily remain unchanged following the effective date. Of course, unlike priority contests among unperfected security interests, some priorities are established permanently, e.g., the rights of a buyer of property who took free of a security interest under former Article 9 [Title 30, chapter 9, now repealed].

One consequence of the rule in subsection (a) [subsection (1)] is that the mere taking effect of this Article [Title 30, chapter 9A] does not of itself adversely affect the priority of conflicting claims to collateral.

Example 4: In 1999, SP-1 obtains a security interest in a right to payment for lottery winnings (a "general intangible" as defined in former Article 9 [Title 30, chapter 9, now repealed] but an "account" as defined in this Article [Title 30, chapter 9A]). SP-1's security interest is unperfected because its filed financing statement covers only "accounts." In 2000, D creates a security interest in the same right to payment in favor of SP-2, who files a financing statement covering "accounts and general intangibles." Before this Article [Title 30, chapter 9A] takes effect on July 1, 2001, SP-2's perfected security interest has priority over SP-1's unperfected security interest under former 9-312(5) [30-9-312(5), now repealed, see 30-9A-322]. Because the relative priorities of the security interests were established before the effective date of this Article [Title 30, chapter 9A], former Article 9 [Title 30, chapter 9, now repealed] continues to govern priority after this Article [Title 30, chapter 9A] takes effect. Thus, SP-2's priority is not adversely affected by this Article's [Title 30, chapter 9A] having taken effect.

Note that were this Article [Title 30, chapter 9A] to govern priority, SP-2 would become subordinated to SP-1 under Section 9-322(a)(1) [30-9A-322(1)(a)], even though nothing changes other than this Article's [Title 30, chapter 9A] having taken effect. Under Section 9-704 [30-9A-704], SP-1's security interest would become perfected; the financing statement covering "accounts" adequately covers the lottery winnings and complies with the other perfection requirements of this Article [Title 30, chapter 9A], e.g., it is filed in the proper office.

Example 5: In 1999, SP-1 obtains a security interest in a right to payment for lottery winnings-a "general intangible" (as defined under former Article 9 [Title 30, chapter 9, now repealed]). SP-1's security interest is unperfected because its filed financing statement covers only "accounts." In 2000, D creates a security interest in the same right to payment in favor of SP-2, who makes the same mistake and also files a financing statement covering only "accounts." Before this Article [Title 30, chapter 9A] takes effect on July 1, 2001, SP-1's unperfected security interest has priority over SP-2's unperfected security interest, because SP-1's security interest was the first to attach. See former Section 9-312(5)(b) [30-9-312(5)(b), now repealed, see 30-9A-322]. Because the relative priorities of the security interests were established before the effective date of this Article [Title 30, chapter 9A], former Article 9 [Title 30, chapter 9, now repealed] continues to govern priority after this Article [Title 30, chapter 9A] takes effect. Although Section 9-704 [30-9A-704] makes both security interests perfected for purposes of this Article [Title 30, chapter 9A], both are unperfected under former Article 9 [Title 30, chapter 9, now repealed], which determines their relative priorities.

2. **Financing Statements Ineffective Under Former Article 9 [Title 30, chapter 9, now repealed] but Effective Under this Article [Title 30, chapter 9A].** If this Article [Title 30, chapter 9A] determines priority, subsection (b) [subsection (2)] may apply. It deals with the case in which a filing that occurs before the effective date of this Article [Title 30, chapter 9A] would be ineffective to perfect a security interest under former Article 9 [Title 30, chapter 9, now repealed] but effective under this Article [Title 30, chapter 9A]. For purposes of Section 9-322(a) [30-9A-322(1)], the priority of a security interest that attaches after this Article [Title 30, chapter 9A] takes effect and is perfected in this manner dates from the time this Article [Title 30, chapter 9A] takes effect.

Example 6: In 1999, SP-1 obtains a security interest in D's existing and after-acquired instruments and files a financing statement covering "instruments." In 2000, D grants a security interest in its existing and after-acquired accounts in favor of SP-2, who files a financing statement covering "accounts." After this Article [Title 30, chapter 9A] takes effect on July 1, 2001, one of D's account debtors gives D a negotiable note to evidence its obligation to pay an overdue account. Under the first-to-file-or-perfect rule in Section 9-322(a) [30-9A-322(1)], SP-1 would have priority in the instrument, which constitutes SP-2's proceeds. SP-1's filing in 1999 was earlier than SP-2's in 2000. However, subsection (b) [subsection (2)] provides that, for purposes of Section 9-322(a) [30-9A-322(1)], SP-1's priority dates from the time this Article [Title 30, chapter 9A] takes effect (July 1, 2001). Under Section 9-322(b) [30-9A-322(2)], SP-2's priority with respect to the proceeds (instrument) dates from its filing as to the original collateral (accounts). Accordingly, SP-2's security interest would be senior.

Subsection (b) [subsection 2] does not apply to conflicting security interests each of which is perfected by a pre-effective-date filing that was not effective under former Article 9 [Title 30, chapter 9, now repealed] but is effective under this Article [Title 30, chapter 9A].

Example 7: In 1999, SP-1 obtains a security interest in D's existing and after-acquired instruments and files a financing statement covering "instruments." In 2000, D grants a security interest in its existing and after-acquired instruments in favor of SP-2, who files a financing statement covering "instruments." After this Article [Title 30, chapter 9A] takes effect on July 1, 2001, one of D's account debtors gives D a negotiable note to evidence its obligation to pay an overdue account. Under the first-to-file-or-perfect rule in Section 9-322(a) [30-9A-322(1)], SP-1 would have priority in the instrument. Both filings are effective under this Article [Title 30, chapter 9A], see Section 9-705(b) [30-9A-705(2)], and SP-1's filing in 1999 was earlier than SP-2's in 2000. Subsection (b) [subsection 2] does not change this result.

Compiler's Comments

Effective Date: Section 171, Ch. 305, L. 1999, provided that this section is effective July 1, 2001.

Part 8
Transition

Part Official Comments

These transition provisions largely track the provisions of Part 7, which govern the transition to the 1998 revision of this Article [Title 30, chapter 9A]. The Comments to the sections of Part 7 generally are relevant to the corresponding sections of Part 8. The 2010 amendments are less far-reaching than the 1998 revision. Although Part 8 does not carry forward those Part 7 provisions that clearly would have no application to the transition to the amendments, as a matter of prudence Part 8 does carry forward all Part 7 provisions that are even arguably relevant to the transition.

The most significant transition problem raised by the 2010 amendments arises from changes to Section 9-503(a) [30-9A-503(1)], concerning the name of the debtor that must be provided for a financing statement to be sufficient. Sections 9-805 [30-9A-805] and 9-806 [30-9A-806] address this problem.

Example: On November 8, 2012, Debtor, an individual whose "individual name" is "Lon Debtor" and whose principal residence is located in State A, creates a security interest in certain manufacturing equipment. On November 15, 2012, SP perfects a security interest in the equipment under Article 9 [Title 30, chapter 9A] (as in effect prior to the 2010 amendments) by filing a financing statement against "Lon Debtor" in the State A filing office. On July 1, 2013, the 2010 amendments, including Alternative A to Section 9-503(a) [30-9A-503(1)], take effect in State A. Debtor's unexpired State A driver's [license] indicates that Debtor's name is "Polonius Debtor." Assuming that a search under "Polonius Debtor" using the filing office's standard search logic would not disclose the filed financing statement, the financing statement would be insufficient under amended Section 9-503(a)(4) [30-9A-503(1)(d)] (Alt. A). However, Section 9-805(b) [30-9A-805(2)] provides that the 2010 amendments do not render the financing statement ineffective. Rather, the financing statement remains effective—even if it has become seriously misleading—until it would have ceased to be effective had the amendments not taken effect. See Section 9-805(b)(1) [30-9A-805(2)(a)]. SP can continue the effectiveness of the financing statement by filing a continuation statement with the State A filing office. To do so, however, SP must amend Debtor's name on the financing statement to provide the name that is sufficient under Section 9-503(a)(4) [30-9A-503(1)(d)] (Alt. A) at the time the continuation statement is filed. See Section 9-805(c), (e) [30-9A-805(3), (5)].

The most significant transition problem addressed by the 1998 revision arose from the change in the choice-of-law rules governing where to file a financing statement. The 2010 amendments do not change the choice-of-law rules. Even so, the amendments will change the place to file in a few cases, because certain entities that were not previously classified as "registered organizations" would fall within that category under the amendments.

Part Compiler's Comments

Effective Date: This part is effective July 1, 2013.

Saving Clause: Section 26, Ch. 75, L. 2013, provided: "(1) Except as otherwise provided in [sections 19 through 25] [this part], this chapter applies to a transaction or lien within its scope, even if the transaction or lien was entered into or created before [the effective of this act] [July 1, 2013].

(2) This chapter does not affect an action, case, or proceeding commenced before [the effective date of this act] [July 1, 2013]."

CHAPTER 10
SECURITIES REGULATION

Chapter Compiler's Comments

Source: The Securities Act of Montana is a substantial adoption of the major provisions of the Uniform Securities Act promulgated by the Conference of Commissioners on Uniform State Laws, but it contains numerous variations, omissions, and additional matter.

Chapter Collateral References

Office of the Montana State Auditor: Commissioner of Securities and Insurance, https://csimt.gov/.

Part 1
General Application

30-10-102. Policy.

Compiler's Comments

1983 Amendment: Substituted language stating policies of protecting the investor and others, promoting uniformity, and encouraging, promoting, and facilitating capital investment in Montana for "Parts 1 through 3 of this chapter shall be so construed as to effectuate its general purpose to make uniform the law of those states which enact it".

30-10-103. Definitions.

Compiler's Comments

2023 Amendment: See 2023 Session Law for amendment made by sec. 6, Ch. 166, L. 2023. Amendment effective October 1, 2023.

2021 Amendment: Chapter 127 in definition of salesperson in (a) inserted second sentence concerning a supervisor and in last sentence near middle substituted "falls within" for "comes within"; and made minor changes in style. Amendment effective July 1, 2021.

Termination Provision Removed: Sections 3 and 4, Ch. 404, L. 2021, amended sec. 16, Ch. 58, L. 2011, and sec. 55, Ch. 151, L. 2017, to remove the termination of the amendments made to this sections by sec. 10, Ch. 58, L. 2011. Effective May 7, 2021.

Code Commissioner Correction: In the definition of salesperson, the Code Commissioner inserted the bracketed sentence, which was included in the definition of salesperson in the former temporary version of this section and was also intended to be included in the version effective July 1, 2021.

2017 Amendment: Chapter 84 inserted definitions of financial exploitation and qualified individual; in definition of vulnerable person inserted (d) referring to person with mental disorder and providing definition of mental disorder; in version effective July 1, 2017, in definition of federal covered advisor substituted "A federal covered advisor is not an investment advisor as defined in subsection (12)" for "The term does not include a person who would be exempt from the definition of investment adviser pursuant to subsection (11)(c)(i), (11)(c)(ii), (11)(c)(iii), (11)(c)(iv), (11)(c)(v), (11)(c)(vi), (11)(c)(vii), or (11)(c)(ix)"; and made minor changes in style. Amendment effective March 22, 2017.

Extension of Termination Date: Section 55, Ch. 151, L. 2017, amended sec. 16, Ch. 58, L. 2011, by extending the termination date imposed by Ch. 58 to June 30, 2021. Effective April 4, 2017.

2015 Amendment: Chapter 28 inserted definition of vulnerable person; and made minor changes in style. Amendment effective February 18, 2015.

Saving Clause: Section 6, Ch. 28, L. 2015, was a saving clause.

Severability: Section 7, Ch. 28, L. 2015, was a severability clause.

2011 Amendments — Composite Section: Chapter 19 in definition of person at beginning deleted "for the purpose of parts 1 through 3 of this chapter"; in definition of Securities Act of 1933 substituted "Energy Policy Act of 2005" for "Public Utility Holding Company Act of 1935"; and made minor changes in style. Amendment effective October 1, 2011.

Chapter 58 in introductory clause inserted reference to part 10; in definition of commissioner after "securities commissioner" substituted "provided for in 2-15-1901" for "of this state"; in definition of federal covered adviser in (b) substituted "A federal covered adviser is not an investment adviser as defined in subsection (11)" for "The term does not include a person who would be exempt from the definition of investment adviser pursuant to subsection (11)(c)(i), (11)(c)(ii), (11)(c)(iii), (11)(c)(iv), (11)(c)(v), (11)(c)(vi), (11)(c)(vii), or (11)(c)(ix)"; in definition of investment adviser representative in (b) at end after "chapter" inserted reference to part 10; in definition of person before "means" deleted "for the purpose of parts 1 through 3 of this chapter"; and made minor changes in style. Amendment effective March 25, 2011, and terminates June 30, 2017.

Style changes were slightly different in the chapters. In each case, the codifier chose appropriate text.

Severability: Section 13, Ch. 58, L. 2011, was a severability clause.

Applicability: Section 15, Ch. 58, L. 2011, provided: "[This act] applies to final orders issued on or after [the effective date of this act]." Effective March 25, 2011.

2003 Amendments — Composite Section: Chapter 156 in definition of salesperson in (b)(i)(C) at end substituted "if a commission or other remuneration is not paid or given directly or indirectly for soliciting a prospective buyer" for "for a qualified purchaser as defined in section 18(b)(3) of the Securities Act of 1933". Amendment effective October 1, 2003.

Chapter 493 in definition of security in (a) inserted "viatical settlement purchase agreement"; and made minor changes in style. Amendment effective April 24, 2003.

Applicability: Section 14, Ch. 493, L. 2003, provided: "[This act] applies to viatical settlement contracts entered into on or after [the effective date of this act]." Effective April 24, 2003.

1999 Amendment: Chapter 472 in definition of federal covered adviser in (b) substituted listing of exclusions for former text that read: "excluded from the definition of "investment adviser" under section 202(a)(11) of the Investment Advisers Act of 1940"; in definition of investment adviser representative inserted (a)(ii) to include a person who is an investment adviser representative with a place of business in this state and in (b) at end inserted "or of a federal covered adviser who has made a notice filing under parts 1 through 3 of this chapter"; and made minor changes in style. Amendment effective April 27, 1999.

Severability: Section 71, Ch. 472, L. 1999, was a severability clause.

Saving Clause: Section 72, Ch. 472, L. 1999, was a saving clause.

1997 Amendments: Chapter 42 in definition of Commodity Exchange Act, at end after "name", deleted "as amended on the effective date of this subsection"; in definition of offer or offer to sell deleted subsection (c) that read: "(c) Any security given or delivered with or as a bonus on account of any purchase of securities or any other thing is considered to constitute part of the subject of the purchase and to have been offered and sold for value. A purported gift of assessable stock is considered to involve an offer and sale. Each sale or offer of a warrant or right to purchase or subscribe to another security of the same or another issuer, as well as each sale or offer of a security that gives the holder a present or future right or privilege to convert into another security of the same or another issuer, is considered to include an offer of the other security"; in definition of Securities Act of 1933, at end, deleted "as amended before or after July 1, 1961"; and made minor changes in style. Amendment effective March 12, 1997.

Chapter 533 inserted definitions of federal covered adviser and federal covered security; in definition of investment adviser inserted (c)(viii) regarding a federal covered adviser; in definition of salesperson inserted (a)(iii) exempting a person who represents an issuer in affecting transactions in a federal covered security and inserted (b) exempting a person who represents a broker-dealer; in definition of Securities Act of 1933, at end, deleted "as amended before or after July 1, 1961"; adjusted subsection references; and made minor changes in style.

Severability: Section 14, Ch. 533, L. 1997, was a severability clause.

1995 Amendment: Chapter 239 in definition of investment adviser, in (c)(iii) after "accountant", deleted "engineer, or teacher" and after "person's profession" inserted remainder of subsection referring to receipt of payment, recommendation of securities, and custody of funds and inserted (c)(vii) relating to engineer or teacher; and made minor changes in style.

1993 Amendment: Chapter 162 in (9)(c)(iv), near beginning after "broker-dealer", inserted "whose performance of services described in subsection (9)(a) is solely incidental to the conduct of business and for which the broker-dealer does not receive special compensation"; in (10)(b), near beginning after "pursuant to", substituted "30-10-201(1) whose performance of the services described in subsection (10)(a) is solely incidental to the conduct of business as a salesperson and for which the salesperson does not receive special compensation other than fees relating to the solicitation or offering of investment advisory services of a registered investment adviser" for "30-10-201"; and made minor changes in style.

Registration of Previous Filing — Temporary: Section 3, Ch. 162, L. 1993, provided: "A registered salesperson who has filed with the commissioner as an investment adviser representative as of October 1, 1993, shall register as an investment adviser representative by October 1, 1994." Because the registration requirement was a temporary provision, the section was not codified.

1991 Amendments: Chapter 2 in definition of salesman, in (2)(b), inserted exception clause; in definition of commodity investment contract inserted second sentence of (b) regarding effect of commodities held as collateral or subject to lien on physical delivery; in definition of security, in first sentence after "instrument commonly known as a security", inserted "any put, call, straddle, option, or privilege on any security, certificate of deposit, or group or index of securities, including any interest in a security or based on the value of a security"; and made minor change in style. Amendment effective January 29, 1991.

Chapter 228 in definition of security, in last sentence before "sum", inserted "fixed".

1989 Amendment: In definition of investment adviser, before "broker-dealer", inserted "registered". Amendment effective March 22, 1989.

1987 Amendments: Chapters 269, 270, 272, and 370 in (11)(c)(vii) substituted reference to subsection (11) for reference to subsection (5).

Chapter 269 in definition of investment adviser excluded an investment adviser representative; and inserted definition of investment adviser representative.

Chapter 270 inserted definitions of commodity, Commodity Exchange Act, commodity futures trading commission, commodity investment contract, commodity option, and precious metal; and in definition of security, after "bond", inserted "commodity investment contract; commodity option".

Chapter 272 in (2)(a) substituted reference to subsection (8) of 30-10-104 for reference to subsection (12); included in definition of investment adviser a person who provides, or represents himself as providing, investment advisory services to others for compensation; in definition of investment adviser substituted exclusion of a publisher of any media that does not give personally based financial advice for "a publisher of any bona fide newspaper, news magazine, or business or financial publication of general, regular, and paid circulation"; deleted former (6)(f) that read: "(f) a person who has no place of business in this state if his only clients in this state are other investment advisers, broker-dealers, banks, savings institutions, trust companies, insurance companies, investment companies as defined in the Investment Company Act of 1940, pension or profit-sharing trusts, or other financial institutions or institutional buyers, whether acting for themselves or as trustees"; in (18) inserted ""Investment Advisors Act of 1940""; and inserted definition of transact.

Sources: The source of the amendments to this section made by Ch. 269, L. 1987, is the North American Securities Administrators Association guidelines.

The sources of the amendments to this section made by Ch. 270, L. 1987, are the Model State Commodity Code and Arizona Revised Statutes 44-1801 and 44-1844.

1985 Amendment: Inserted definition of registered broker-dealer.

1983 Amendment: Inserted second sentence of (2) stating circumstances in which a partner, officer, or director of a broker-dealer or issuer is a salesman and deleted the same sentence from the end of (2)(c) and made a minor change in phraseology; and in (2)(a) inserted the reference to (12).

Source: Section 401, Uniform Securities Act.

Federal Statutes: The Securities Act of 1933, referred to in this section, is compiled in the United States Code as Title 15, sec. 77a through 77aa.

The Securities Exchange Act of 1934 is compiled as Title 15, sec. 78a through 78jj.

The Public Utility Holding Company Act of 1935 is compiled as Title 15, sec. 79 through 79z-6.

The Investment Company Act of 1940 is compiled as Title 15, sec. 80a-1 through 80a-52.

Case Notes

Adequate Definition of "Security" for Jury — Willful Conduct Standard Applicable to Securities Act Violations — Omission of Investment Prospectus Not Fraudulent at Time — Securities Restitution Properly Awarded: The defendant, a pastor, was approached by the plaintiff, a member of his congregation, about investing money. The defendant convinced the plaintiff to purchase stock in the defendant's Mexico-domiciled company. Ultimately, the investment promises never materialized and the defendant was convicted of failure to register as a securities salesperson, failure to register a security, and fraudulent practices under the Securities Act of Montana. On appeal, the defendant argued that the term "security" was not adequately or specifically defined for the jury, that the "willful" standard was inappropriate to attach to the charges, that the conviction of fraudulent practices was improper because neither the statute nor administrative rule required an investment prospectus at the time of the violation, and that the award of restitution was improper. The Supreme Court held that the evidence showed that the jury reasonably concluded that the defendant had sold a security because the shares in the company constituted a stock, that the Legislature specifically included a willful standard for

Securities Act violations, that the fraudulent practices conviction was improper because failure to provide a prospectus was not part of the statute at the time, and that the award of restitution was proper because the loss stemmed directly from the defendant's conduct. St. v. Himes, 2015 MT 91, 378 Mont. 419, 345 P.3d 297.

Tenants-in-Common Investments Constitute Securities — Common Venture Established: The petitioner alleged an accounting firm unlawfully sold certain tenants-in-common investments as securities as part of what was later determined to be a Ponzi scheme. Because a common venture can be established by satisfying the elements of horizontal, broad vertical, or narrow vertical commonality and the investment profits were derived through the entrepreneurial or managerial efforts of others, the investments constituted securities under a broad application of 30-10-103(22)(a)(xii). Redding v. District Court, 2012 MT 144, 365 Mont. 316, 281 P.3d 189.

30-10-104. Exempt securities.

Compiler's Comments

2017 Amendment: Chapter 151 in (6)(a) substituted "federal surface transportation board" for "interstate commerce commission". Amendment effective October 1, 2017.

Severability: Section 57, Ch. 151, L. 2017, was a severability clause.

2011 Amendment: Chapter 19 in (6)(b) substituted "Energy Policy Act of 2005" for "Public Utility Holding Company Act of 1935"; in (6)(d) near middle inserted "A security referred to under this subsection (6)(d) includes"; and made minor changes in style. Amendment effective October 1, 2011.

1999 Amendment: Chapter 472 in introductory clause and in (1) near middle after "30-10-207" inserted "and 30-10-211"; and made minor changes in style. Amendment effective April 27, 1999.

Severability: Section 71, Ch. 472, L. 1999, was a severability clause.

Saving Clause: Section 72, Ch. 472, L. 1999, was a saving clause.

1997 Amendment: Chapter 533 in (12), near beginning of first sentence after "the Midwest stock exchange", inserted "the Chicago board of options exchange, the Philadelphia stock exchange, the Boston stock exchange" and inserted second sentence allowing the Commissioner to condition security terms by rule; in (13) inserted second sentence allowing the Commissioner to condition security terms by rule; inserted (15) exempting any security for which an offer or sale is not directed to or received by a person in this state if the issuer does not maintain a place of business in the state; adjusted subsection references; and made minor changes in style.

Severability: Section 14, Ch. 533, L. 1997, was a severability clause.

1991 Amendment: Inserted (14) relating to securities issued by insurers.

1989 Amendment: In (9) made minor change in phraseology. Amendment effective March 22, 1989.

1987 Amendment: At end of (1) substituted reference to subsection (13) for reference to subsection (9); deleted former (5) that read: "(5) any insurance or endowment policy or annuity contract or optional annuity contract issued by a corporation subject to the supervision of the insurance commissioner"; and in (7)(d) substituted reference to subsection (7)(d) for reference to subsection (8)(d).

Source: The sources of the amendments to this section made by Ch. 270, L. 1987, are the Model State Commodity Code and Arizona Revised Statutes 44-1801 and 44-1844.

1985 Amendment: In (3) near end, after "organized", substituted "and supervised under the laws of any state" for "or chartered as such and under the jurisdiction and supervision of the superintendent of banks of any state"; in (12) substituted last sentence stating the exemption fee is as set in 30-10-209(4) for "The commissioner may charge a fee of $50 for granting the exemption by order"; and inserted (14) exempting certain national market system securities.

1983 Amendment: In (12), substituted first sentence exempting a security for which the commissioner determines an exemption would better serve the purposes of 30-10-102 than would registration for "any security for which registration is not necessary for protection of investors, as determined by the commissioner by order"; and inserted (13) exempting certain securities listed or approved for listing on any exchange registered with the federal commission.

Source: Section 402, Uniform Securities Act.

Federal Statute: The Public Utility Holding Company Act of 1935, referred to in subsection (7) of this section, is compiled in the United States Code as Title 15, sec. 79 through 79z-6.

Administrative Rules

ARM 6.10.102 Definitions.
ARM 6.10.301 Montana limited offering exemption.
ARM 6.10.305 Foreign security exemption.
ARM 6.10.403 Sanctions against fraudulent foreign securities and their dealers.

30-10-105. Exempt transactions — rulemaking.

Compiler's Comments

2019 Amendments — Composite Section: Chapter 104 in (20) at end inserted CFR reference. Amendment effective April 1, 2019.

Chapter 386 inserted (23) regarding utility token transaction requirements and definitions. Amendment effective July 1, 2019, and terminates September 30, 2023.

Preamble: The preamble attached to Ch. 104, L. 2019, provided: "WHEREAS, in Redding v. McCarter, 2012 MT 144, 365 Mont. 316, the Montana Supreme Court stated that the Securities Act of Montana was drafted broadly to be in harmony with federal securities law, which recognizes the virtually limitless scope of human ingenuity, especially in the creation of the countless and variable schemes devised by those who seek the use of money of others on the promise of profits; and

WHEREAS, recent enforcement actions by the Montana State Auditor have encountered securities schemes promising investors with profits through payment of items of no value but of purported value.

THEREFORE, this act seeks to definitively clarify that the Montana Securities Act applies to the virtually limitless scope of securities schemes, including those not involving strictly the payment of money."

Saving Clause: Section 3, Ch. 104, L. 2019, was a saving clause.

Severability: Section 4, Ch. 104, L. 2019, was a severability clause.

2015 Amendment: Chapter 163 inserted (22) providing registration exemption for securities issuers to engage in certain securities transactions if conducted within the state. Amendment effective July 1, 2015.

2011 Amendment: Chapter 9 deleted former (16) that read: "(16) a transaction in the securities of a certified Montana capital company or a certified Montana small business investment capital company, as defined in 90-8-104, if the company first files all disclosure documents, along with a consent to service of process, with the commissioner. The commissioner may not charge a fee for the filing"; and made minor changes in style. Amendment effective October 1, 2011.

Saving Clause: Section 8, Ch. 9, L. 2011, was a saving clause.

2003 Amendment: Chapter 202 inserted (8)(c) concerning exemption for Montana-based businesses; and made minor changes in style. Amendment effective October 1, 2003.

1999 Amendments — Composite Section: Chapter 130 in (22)(a) in two places and in (22)(b) near end inserted reference to chapter 17 of Title 35; and made minor changes in style. Amendment effective October 1, 1999.

Chapter 472 in introductory clause after "30-10-207" inserted "and 30-10-211"; in (2)(a)(i) near middle after "inc." deleted "(NASDAQ)"; in (13) in three places substituted references to security for references to stock and in two places substituted references to security holder for references to stockholder; in (15) in second sentence after "30-10-207" inserted "and 30-10-211"; and made minor changes in style. Amendment effective April 27, 1999.

Severability: Section 71, Ch. 472, L. 1999, was a severability clause.

Saving Clause: Section 72, Ch. 472, L. 1999, was a saving clause.

1997 Amendment: Chapter 395 inserted (22) concerning offer or sale of securities by cooperative association, requiring cooperative to furnish written description of transaction, and requiring Commissioner to adopt rules; and made minor changes in style. Amendment effective July 1, 1997.

1991 Amendments: Chapter 46 in (2)(a)(ii), after "3 years", inserted "and there has been no default"; inserted (19)(c) requiring that quantities of precious metals purchased and delivered to a depository institution be physically located within Montana at all times after delivery; at end of (21), after "Code", deleted "of 1986"; and made minor changes in style.

Chapter 263 in (16), at beginning of subsection, substituted "a transaction in the securities of" for "any transaction by" and inserted reference to a certified Montana small business investment capital company; and made minor changes in style. Amendment effective March 29, 1991.

Chapter 278 inserted (8)(b) creating a limited offering exemption directed to not more than 25 persons; in (8)(c) changed subsection reference; in (9)(b) increased number of subscribers from 10 to 25; and made minor changes in style.

Retroactive Applicability: Section 20, Ch. 263, L. 1991, provided: "[This act] applies retroactively, within the meaning of 1-2-109, to events occurring after December 31, 1990."

1989 Amendment: Inserted (21) relating to stock ownership plans; and inserted (22) relating to employee cooperative corporations. Section 7, Ch. 671, L. 1989, was a coordination instruction providing that if Senate Bill No. 246 was not passed and approved, subsection 22 was void.

Senate Bill No. 246 was not passed and approved, so the amendment inserting subsection (22) was void and therefore not codified. Amendment effective May 16, 1989.

1987 Amendments: Chapter 270 inserted (17) through (20) (see 1987 Session Law for text).

Chapter 272 in (1) inserted second sentence providing that a transaction is presumed isolated if one of no more than three in a 12-month period; near middle of (11) substituted "no stop, refusal, denial, suspension, or revocation order" for "no stop order or refusal order"; in (15) inserted second sentence allowing the Commissioner to require that 30-10-201 through 30-10-207 apply to transactional exemptions adopted by rule; and in (16), near beginning after "transaction", substituted remainder of sentence exempting any transaction by a capital company upon filing of disclosure documents for "pursuant to the Montana Capital Company Act, Title 90, chapter 8, provided that a Montana capital company must first file all disclosure documents, along with a consent to service of process, with the state securities commissioner" and in second sentence, at end, deleted "or deposit".

Source: The sources of the amendments to this section made by Ch. 270, L. 1987, are the Model State Commodity Code and Arizona Revised Statutes 44-1801 and 44-1844.

1985 Amendments: Chapter 478 renumbered former (2)(a) and (2)(b) as (2)(a)(i) and (2)(a)(ii); renumbered former (3) as (2)(b); renumbered former (9)(a) and (9)(b) as (8)(a)(i) and (8)(a)(ii); in (8)(a), in introductory clause, substituted "any transaction pursuant to an offer made in this state directed by the offeror to not more than 10 persons (other than those designated in subsection (7)) during any period of 12 consecutive months, if:" for former text that read: "any transaction pursuant to an offer directed by the offeror to not more than 10 persons (other than those designated in subsection (8) of this section) in this state during any period of 12 consecutive months, whether or not the offeror or any of the offerees is then present in this state, if"; and inserted (8)(b) stating when an offer is made in this state.

Chapter 479 inserted (16) exempting a transaction pursuant to the Montana Capital Company Act if the company files disclosure documents and prohibiting Commissioner from charging a fee for such filing.

1983 Amendment: In (2) deleted "registered" before "broker-dealer" and after "broker-dealer" inserted "registered pursuant to 30-10-201"; deleted former (2)(a)(i), which read: "a recognized securities manual contains the names of the issuer's officers and directors, a balance sheet of the issuer as of a date within 18 months, and a profit and loss statement for either the fiscal year preceding that date or the most recent year of operations; or"; inserted (2)(a) exempting a nonissuer distribution if quotations are reported by certain systems; in (9) changed "offerer" to "offeror" in two places and corrected an internal reference; in (9)(b) substituted "federal Securities Act of 1933" for "Federal Securities and Exchange Act of 1933"; and inserted (16) exempting a transaction that complies with rules adopted by Commissioner.

Statement of Intent: The statement of intent attached to SB 184 (Ch. 322, L. 1983) provided: "A Statement of Intent is required for this bill because it grants the Securities Commissioner the authority to adopt rules exempting certain securities transactions from registration and to establish fees for granting such exemption. There is to be no exemption from the antifraud provisions of the Securities Act.

(1) The legislature intends that the exemption rules:

(a) provide limited relief from the registration provisions of the Act for small and existing businesses that are attempting to raise a limited amount of funds; and

(b) provide an exemption from the registration provisions of the Securities Act for transactions in securities when the securities involved are adequately regulated by other bodies.

(2) The Legislature intends that the fee rules would establish a fee schedule to match the cost and complexity of the exemption. The Legislature does not intend that the state either lose or gain any revenue because of any exemption under 30-10-105(16)."

Federal Statutes: The Investment Company Act of 1940, referred to in subsection (7) of this section, is compiled in the United States Code as Title 15, sec. 80a-1 through 80a-52.

The Securities Act of 1933, referred to in subsection (11) of this section, is compiled in the United States Code as Title 15, sec. 77a through 77aa.

Administrative Rules

ARM 6.10.133 Internet.
ARM 6.10.206 Stock subscription agreement — no default or penalty provision.
ARM 6.10.302 Foreign savings and loan association exemption.
ARM 6.10.303 Second tier limited offering exemption.
ARM 6.10.306 Transactional exemptions for cooperative associations.

ARM 6.10.307 Filings requirement for transactional exemption pursuant to 30-10-105(15), MCA.

ARM 6.10.308 Merger and acquisition broker exemption.

Case Notes

Jury Instructions Regarding Exemptions Disallowed — Defendant Not Eligible for Exemptions — No Applicability to Case: The defendant was charged with securities fraud. At trial, he sought to include language in the jury instructions that referred to exemptions to 30-10-201 and 30-10-202. The District Court did not allow the defendant's language because the exemptions had no application to the defendant's case since the defendant was not eligible for them in the first place. On appeal, the Supreme Court affirmed, ruling that the final jury instructions provided by the District Court did not fail to fully instruct the jury on the law applicable to the defendant's case. St. v. Reynolds, 2017 MT 25, 386 Mont. 267, 389 P.3d 243.

30-10-107. Administration.

Compiler's Comments

2003 Amendment: Chapter 156 in (6) near beginning of first sentence after "at a" substituted "charge of 50 cents for each page" for "reasonable charge"; and made minor changes in style. Amendment effective October 1, 2003.

1999 Amendments — Composite Section: Chapter 416 at end of (4) after "public" deleted "unless the commissioner grants a request joined in by all the respondents that the hearing be conducted privately"; and made minor changes in style. Amendment effective October 1, 1999.

Chapter 472 in (7) near middle after "corporation" inserted "the securities registration depository"; and made minor changes in style. Amendment effective October 1, 1999.

Severability: Section 71, Ch. 472, L. 1999, was a severability clause.

Saving Clause: Section 72, Ch. 472, L. 1999, was a saving clause.

1997 Amendment: Chapter 533 inserted (8) regarding giving of an order or notice; and made minor changes in style.

Severability: Section 14, Ch. 533, L. 1997, was a severability clause.

1983 Amendment: Inserted (7) providing that Commissioner may cooperate with certain commissions and other entities to serve the policies of 30-10-102.

Source: Sections 406, 412, and 413, Uniform Securities Act.

Administrative Rules

ARM 6.2.120 through 6.2.122 Procedural rules for contested case hearings.

ARM 6.10.101 Applicability of subchapter.

ARM 6.10.102 Definitions.

ARM 6.10.201 Sales materials.

ARM 6.10.202 Promotional securities — escrow.

ARM 6.10.203 Promotional securities — required waivers.

ARM 6.10.205 Notice of termination of offering — change of officers.

ARM 6.10.206 Stock subscription agreement — no default or penalty provision.

ARM 6.10.207 Warrants and options.

ARM 6.10.209 Notice filings for offerings of federal covered securities under 18(b)(3) or (4) of the Securities Act of 1933.

ARM 6.10.305 Foreign security exemption.

ARM 6.10.503 Minimum financial requirements and financial reporting of broker-dealers.

ARM 6.10.506 Minimum financial requirements for investment advisers.

ARM 6.10.507 Bonding requirements for certain investment advisers.

ARM 6.10.508 Custody of client funds or securities by investment advisers.

ARM 6.10.403 Sanctions against fraudulent foreign securities and their dealers.

Case Notes

Suitability Analysis Requirement Reasonable Interpretation of Securities Act: The Commissioner of Securities determined that in order to protect investors in situations where a salesperson does not have a preexisting relationship with a customer, a suitability analysis is critical once a customer indicates a desire to make a securities transaction in order to ensure that the transaction is suitable. Knowles contended that this requirement was an unreasonable extension of the meaning of unethical practices, but the Supreme Court disagreed. The Commissioner's interpretation was consistent with the spirit of the Securities Act of Montana and with ARM 6.10.401(1)(c) and was within the range of reasonable interpretation permitted by the administrative rule. Knowles v. State ex rel. Lindeen, 2009 MT 415, 353 M 507, 222 P3d 595 (2009).

30-10-110. Scope.

Compiler's Comments

1997 Amendments: Chapter 42 inserted (7) relating to security given as a bonus; and made minor changes in style. Amendment effective March 12, 1997.

Chapter 533 in (3), at end, deleted "but for the purpose of 30-10-202, an offer to sell which is not directed to or received by the offeree in this state is not made in this state"; and made minor changes in style.

Severability: Section 14, Ch. 533, L. 1997, was a severability clause.

1987 Amendment: In (6), after "advisers", inserted "and investment adviser representatives".

Source: The source of the amendments to this section made by Ch. 269, L. 1987, is the North American Securities Administrators Association guidelines.

Source: Chapter 285, L. 1985, is based on Section 414 of the Uniform Securities Act, 7A U.L.A. 690.

30-10-115. Deposits to general fund — exceptions.

Compiler's Comments

2021 Amendment: Chapter 404 in (2)(c) in first sentence after "after July 1, 2019" substituted "3%" for "4.5%" and in third sentence after "On or after July 1," substituted "2027" for "2021"; and made minor changes in style. Amendment effective May 7, 2021.

Severability: Section 5, Ch. 404, L. 2021, was a severability clause.

Extension of Termination Date — Code Commissioner Explanation: Section 1, Ch. 395, L. 2019, amended sec. 28, Ch. 6, Sp. L. November 2017, by extending the termination date imposed by that section to June 30, 2021. Effective July 1, 2019.

Chapter 395 takes effect on July 1, 2019, which is after the June 30, 2019, termination date, so the 2017 amendments could potentially be construed to have terminated. Because the sole purpose of sec. 1, Ch. 395, L. 2019, was to revise the termination date for the 2017 amendments, the code commissioner has not terminated the 2017 amendments. Instead, the code commissioner has revised the termination date of the amendments.

2017 Special Session Amendment: Chapter 6 in (2)(a) at beginning of second sentence inserted "Subject to legislative fund transfer"; and made minor changes in style. Amendment effective December 15, 2017, and terminates June 30, 2019.

Severability: Section 26, Ch. 6, Sp. L. November 2017, was a severability clause.

2017 Amendment: Chapter 151 in (2)(c) in first sentence substituted "On or after July 1, 2019" for "From March 7, 2013, through June 30, 2017" and in second sentence substituted "July 1, 2021" for "July 1, 2017"; and made minor changes in style. Amendment effective April 4, 2017.

Severability: Section 57, Ch. 151, L. 2017, was a severability clause.

2013 Amendment: Chapter 66 in (1) inserted exception clause and after "chapter" deleted "except for notice filing fees described in 30-10-209(1)(d) and examination costs collected under 30-10-210"; in (2)(a) in second sentence substituted "this subsection (2)(a)" for "this section"; in (2)(b) substituted "any fees in excess of the amount required for the purposes listed in subsection (2)(a)" for "any excess fees"; inserted (2)(c) concerning deposit of collected annual fees; and made minor changes in style. Amendment effective March 7, 2013.

Severability: Section 4, Ch. 66, L. 2013, was a severability clause.

2011 Amendment: Chapter 227 in three places before "notice" deleted "portfolio"; near end of (2) after "filing" inserted "under 33-10-209(1)(d)"; and made minor changes in style. Amendment effective April 20, 2011.

Severability: Section 25, Ch. 227, L. 2011, was a severability clause.

2005 Amendment: Chapter 469 in (1) near end after "30-10-209(1)(d)" inserted "and examination costs collected under 30-10-210"; and in (2) in first sentence after "revenue" inserted "fund in an". Amendment effective October 1, 2005.

1999 Amendments — Composite Section: Chapter 51 in (1) near end and in (2) near beginning of first sentence and at end of second sentence after "portfolio" substituted "notice filing" for "registration". Amendment effective March 15, 1999.

Chapter 472 in (1) near beginning after "fees" deleted "examination charges"; and in (2) in first sentence after "30-10-209(1)(d)" inserted "and examination costs collected under 30-10-210" and in second sentence at end inserted "and examinations". Amendment effective October 1, 1999.

Severability: Section 71, Ch. 472, L. 1999, was a severability clause.

Saving Clause: Section 72, Ch. 472, L. 1999, was a saving clause.

1993 Amendment: Chapter 462 in (1), after "chapter", inserted "except for portfolio registration fees described in 30-10-209(1)(d)"; and inserted (2) regarding deposit of portfolio registration fees.

1989 Amendment: At beginning substituted "All" for "There is created in the state special revenue fund an account designated as the "securities regulatory trust account" into which all", at end inserted "in the general fund", and deleted former (2) and (3) that read: "(2) The money received and deposited in the securities regulatory trust account may be paid out of the treasury only on appropriation made by the legislature, as provided in 17-8-101, and may be used only to defray the expenses of the commissioner and his staff in the discharge of their administrative and regulatory powers and duties as prescribed by law, subject to the applicable laws relating to the appropriation of state funds and to the deposit and expenditure of state money. The commissioner is responsible for the proper expenditure of this money as provided by law.

(3) Any cash balance remaining in the securities regulatory trust account after all current fiscal year expenditures are met must be transferred to the general fund." Amendment effective July 1, 1989.

Source: Section 30-10-115 is based on the National Association of Insurance Commissioners (NAIC) Model State Insurance Department Funding Act. Sections 30-10-116 through 30-10-118, which are now repealed, also were based on that act.

30-10-119. Records.

Compiler's Comments

Effective Date: Section 8, Ch. 84, L. 2017, provided: "[This act] is effective on passage and approval." Approved March 22, 2017.

Part 2
Registration

30-10-201. Registration and notice filing requirements of broker-dealers, salespersons, investment advisers, and investment adviser representatives.

Compiler's Comments

2021 Amendment: Chapter 28 in (3)(c) inserted last sentence regarding applicability to broker-dealers and investment advisers; and made minor changes in style. Amendment effective February 26, 2021.

1999 Amendment: Chapter 472 in (4) near middle after "(3)(b)" inserted "or who meet the requirements of subsection (3)(c)"; in (6)(b) near beginning of first sentence after "(3)(b) or" inserted "who meet the requirements of subsection", near middle after "state" substituted "submit a notice filing to the commissioner consisting of" for "pay", and after "30-10-209 and" deleted "shall file with the commissioner" and inserted second sentence providing that a notice filing is effective upon receipt by the commissioner; in (9) at end of introductory clause inserted "or a notice filing by a federal covered adviser"; in (9)(a) after "registration" inserted "or notice filing"; in (10)(b) in first sentence after "associated with" inserted "either" and after "act" inserted "or a federal covered adviser with an effective notice filing"; and made minor changes in style. Amendment effective October 1, 1999.

Severability: Section 71, Ch. 472, L. 1999, was a severability clause.

Saving Clause: Section 72, Ch. 472, L. 1999, was a saving clause.

1997 Amendment: Chapter 533 deleted former (3)(b) that read: "(b) the person is registered as a broker-dealer under parts 1 through 3 of this chapter"; in (3)(b), at beginning, inserted "the person does not have a place of business in the state and"; inserted (3)(b)(iii) regarding federal covered advisers; in (3)(c), at end, substituted "the preceding 12-month period the person has not had more than five clients who are residents of this state, other than those clients specified in subsection (3)(b)" for "any 12 consecutive months does not direct business communications in this state in any manner to more than five present or prospective clients, other than those specified in subsection (3)(c), whether or not the person or any of the persons to whom the communications are directed are then present in this state"; inserted (4) prohibiting certain federal covered advisers from conducting advisory business unless the provisions of subsection (6)(b) are met; inserted (5) prohibiting employment of investment adviser representatives in certain cases; in (6)(a) deleted second and third sentences that read: "A salesperson acting as agent for an issuer or broker-dealer who is not currently in compliance with the financial responsibility requirements prescribed by the Securities Exchange Act of 1934 and by regulations adopted under it, may, in the discretion of the commissioner, be required to file with the commissioner a bond of a surety company duly authorized to transact business in this state. The bond must be in an amount determined by the commissioner, payable to the state of Montana and conditioned upon the faithful compliance with the provisions of parts 1 through 3 of this chapter, and provide that upon failure to comply, the salesperson is liable to any and all persons who may suffer loss by reason of a failure to comply"; inserted (6)(b) requiring payment of a fee by a federal covered adviser; in (9), at beginning, deleted "Except as provided in subsection (6)"; in (9)(b), at end, inserted "pursuant to subsection (11)"; in (10)(b) inserted third sentence requiring notification when a connection with a federal covered adviser is terminated; in (11), in first sentence after "representative", inserted "or notice filing for a federal covered adviser", after first "registration" inserted "or notice filing", after second "registration" substituted "or notice filing" for "as a broker-dealer, salesperson, investment adviser, or investment adviser representative filed by the applicant", and at end substituted "fee prescribed by 30-10-209" for "prescribed fee" and in second sentence, after "inc.", substituted "is required to file" for "by filing", after "statement" deleted "showing the financial condition", after "broker-dealer" deleted "as of a date", and after "90 days" inserted "of the end of the broker-dealer's fiscal year, except as provided in section 15 of the Securities Exchange Act of 1934"; in (12)(a), at beginning of first sentence, inserted "Except as provided in section 15 of the Securities Exchange Act of 1934 in the case of a broker-dealer and section 222 of the Investment Advisers Act of 1940 in the case of an investment adviser" and at end inserted "by rule or order" and in second sentence, after "records", inserted "of an investment adviser", after "preserved for" substituted "the period" for "3 years unless", and after "prescribes" substituted "by rule or order" for "otherwise for particular types of records"; inserted (12)(b) allowing the Commissioner to require the dissemination of certain information; inserted (12)(c) regarding filing a correcting amendment; adjusted subsection references and made minor changes in style.

Severability: Section 14, Ch. 533, L. 1997, was a severability clause.

1995 Amendment: Chapter 261 inserted (19) excusing person who passed general securities principal's examination from taking uniform investment adviser law examination and requiring form to be provided for by rule; and made minor changes in style. Amendment effective March 27, 1995.

1993 Amendment: Chapter 162 in (12)(h) expanded reference to all of subsection (12) from reference to subsection (12)(h); in (12)(j) expanded reference to all of subsection (12) from reference to subsection (12)(j); inserted (18) precluding certain sole proprietors from registering as both a broker-dealer and a salesperson or as an investment adviser and an investment adviser representative; and made minor changes in style.

Registration of Previous Filing— Temporary: Section 3, Ch. 162, L. 1993, provided: "A registered salesperson who has filed with the commissioner as an investment adviser representative as of October 1, 1993, shall register as an investment adviser representative by October 1, 1994." Because the registration requirement was a temporary provision, the section was not codified.

1991 Amendment: In (12)(k), after "salesmen or employees", deleted "if he is a broker-dealer" and after "representatives or employees" deleted "if he is an investment adviser". Amendment effective January 29, 1991.

1989 Amendment: In (1), after "except", substituted "as provided in" for "in transactions exempt under"; in second sentence of (6), after "withdrawn", inserted "or terminated"; at beginning of (7) inserted exception clause; near end of introductory clause in (12) inserted "person occupying a similar status or performing similar functions, or person directly or indirectly controlling the broker-dealer or investment adviser"; and made minor changes in phraseology and form. Amendment effective March 22, 1989.

1987 Amendments: Chapter 269 throughout section inserted references to "investment adviser representative"; designated second and third sentences of (7) as (8); inserted (9) providing that an investment advisor representative's registration is ineffective when he is not associated with an investment and requiring notice if his status changes; in (15) substituted reference to subsection (12) for reference to subsection (10); and made minor changes in phraseology.

Chapter 272 inserted (3)(c)(ii) through (3)(d) exempting a person from registration if he has only certain types of clients or if he has no place of business in the state and limits his business communications in this state; in (4), after first sentence, deleted former language that read: "Except for persons in the employ of brokerage firms governed by the regulations of the securities and exchange commission, all salesmen must be legal residents of this state and must have actually resided in this state for a period of at least 1 year next prior to the date of application for registration. The commissioner may, upon request and for good cause shown by an applicant, waive the residency requirement. Payment of the waiver fee shall be as prescribed in 30-10-209"; in (5) inserted second sentence requiring the Commissioner's consent to withdrawal of registration application prior to Commissioner's response; in (6) substituted first sentence requiring the Commissioner to make the registration effective when registration requirements are met for "When the registration requirements are complied with, the commissioner shall approve the registration" and inserted second sentence requiring Commissioner's consent to withdrawal of registration; in (12)(f) substituted language (see 1987 Session Law for text) for "is the subject of an order entered within the past 5 years by the securities administrator of any other state or by the federal securities and exchange commission denying or revoking registration as a broker-dealer, salesman, or investment adviser or the substantial equivalent of those terms as defined in parts 1 through 3 of this chapter or is the subject of an order of the federal securities and exchange commission suspending or expelling him from a national securities exchange or national securities association registered under the Securities Exchange Act of 1934 or is the subject of a United States post office fraud order, but:

(i) the commissioner may not institute a revocation or suspension proceeding under this subsection (f) more than 1 year from the date of the order relied on; and

(ii) he may not enter any order under this subsection (f) on the basis of an order unless that order was based on facts which would currently constitute a ground for an order under this section"; inserted (12)(k) allowing disciplinary action for failure to supervise employees; inserted (13) requiring the Commissioner to take disciplinary action within 30 days of registration for facts known at the time of registration; inserted (14) allowing the Commissioner to postpone or suspend registration pending a determination under this section; and at end of (15), after "opportunity for hearing", substituted "may modify or vacate the order or extend it until final determination" for "may affirm, modify, or vacate the order".

Coordination Instruction: Section 13, Ch. 272, L. 1987, provided: "If SB Bill No. 186 is not passed and approved, section 4 of this act, amending 30-10-201, is amended so that 30-10-201(5) and (6) read as follows:

"(5) The application shall contain whatever information the commissioner requires. No registration application of a broker-dealer, salesman, or investment adviser may be withdrawn before the commissioner approves or denies such registration, without the express written consent of the commissioner.

(6) When the registration requirements are met, the commissioner shall make the registration effective. No effective registration of a broker-dealer, salesman, or investment adviser may be withdrawn without the express written consent of the commissioner."" Senate Bill No. 186 passed as Ch. 269, L. 1987.

Source: The source of the amendments to this section made by Ch. 269, L. 1987, is the North American Securities Administrators Association guidelines.

1985 Amendments: Chapter 407 inserted (13) allowing Commissioner to impose civil fine, providing for collection and allocation of fine, and stating effects of registrant's failure to pay a fine.

Chapter 478 in (4), near beginning after "filing", deleted "with the commissioner" and inserted fourth sentence relating to payment of the waiver fee; and in (8) near beginning after "filing" and near middle after "filed", deleted "with the commissioner", and near middle after "broker-dealer", inserted "who is not a member of NASD, inc."

1981 Amendment: Deleted former (6) relating to effective dates of registration and added (6) providing for registration approval when requirements are met; substituted "December 31" for "March 1" near the beginning of (7); added "or such other time as the commissioner may by rule adopt" in the first sentence of (7); inserted "or investment adviser" following "a broker-dealer, salesman" in (10)(f); deleted "The commissioner may by order summarily postpone or suspend registration pending final determination of any proceeding under this section." at the end of (10)(j).

Source: Sections 201 and 204, Uniform Securities Act.

Federal Statutes: The Investment Company Act of 1940, referred to in subsection (3) of this section, is compiled in the United States Code as Title 15, sec. 80a-1 through 80a-52.

The Securities Exchange Act of 1934, referred to in subsection (4) of this section, is compiled in the United States Code as Title 15, sec. 78a through 78jj.

Administrative Rules

ARM 6.2.120 through 6.2.122 Procedural rules for contested case hearings.

ARM 6.10.150 Incorporation by reference consents to service of process previously filed.

ARM 6.10.209 Notice filings for offerings of federal-covered securities under 18(b)(3) or (4) of the Securities Act of 1933.

ARM 6.10.401 Fraudulent and unethical practices prohibited by broker-dealers and salespersons.

ARM 6.10.402 Fraudulent and unethical practices prohibited by investment advisers and investment adviser representatives.

Title 6, chapter 10, subchapter 5, ARM Broker-dealers and investment advisers.

ARM 6.10.601 Senior specific certifications and designations generally unlawful.

ARM 6.10.602 Rebuttable presumption regarding certain disqualifications.

ARM 6.10.604 Factors considered to determine unlawful certifications or designations.

ARM 6.10.605 Certifications or designations not considered unlawful.

ARM 6.10.607 Rules not limiting authority.

Case Notes

Other Charges Not Included Within or Specific Instances of Fraudulent Practices Charge — No Violation of Prohibition on Multiple Charges: In District Court, the defendant was convicted of six felonies related to his operation of a Ponzi scheme. On appeal to the Supreme Court, he argued that fraudulent practices (common scheme), as set forth in 30-10-301(1), subsumed the remaining five counts as lesser included offenses. The Supreme Court found that failure to register as a securities salesperson as set forth in 30-10-201 and failure to register a security as set forth in 30-10-202 require proof of failure to register, which is not an element of the offense of fraudulent practices, so the Supreme Court affirmed the defendant's convictions on these counts. St. v. Brandt, 2020 MT 79, 399 Mont. 415, 460 P.3d 427.

Jury Instructions Regarding Exemptions Disallowed — Defendant Not Eligible for Exemptions — No Applicability to Case: The defendant was charged with securities fraud. At trial, he sought to include language in the jury instructions that referred to exemptions to 30-10-201 and 30-10-202. The District Court did not allow the defendant's language because the exemptions had no application to the defendant's case since the defendant was not eligible for them in the first place. On appeal, the Supreme Court affirmed, ruling that the final jury instructions provided by the District Court did not fail to fully instruct the jury on the law applicable to the defendant's case. St. v. Reynolds, 2017 MT 25, 386 Mont. 267, 389 P.3d 243.

Significant Delay in Turning Self in After Security Fraud Charges Filed — No Speedy Trial Violation: The defendant was charged with securities fraud and eventually turned himself over to authorities 134 days after the charges were filed. In all, a total of 650 days passed between the state filing an information until the defendant's trial. The defendant filed a motion to dismiss for lack of a speedy trial, which the District Court denied. On appeal, the Supreme Court affirmed, holding that the Ariegwe factors did not weigh in favor of granting the motion and that the 134 days of avoiding the authorities seeking his arrest weighed heavily against him. St. v. Reynolds, 2017 MT 25, 386 Mont. 267, 389 P.3d 243.

Sufficient Evidence of Securities and Insurance Violation: The District Court did not err in concluding that substantial evidence supported the finding that Bower violated securities and insurance law by acting as an investment adviser without registering as required by 30-10-201. In re Bower, 2010 MT 19, 355 Mont. 108, 225 P.3d 784.

Securities Act Violation — Petition for Judicial Review Improperly Granted: The Commissioner of Securities concluded that Knowles violated various provisions of the Securities Act of Montana. Knowles petitioned for judicial review, which was granted. The District Court reversed the Commissioner's decision. On appeal, the Supreme Court affirmed the Commissioner's decision that Knowles employed a scheme or artifice to defraud, failed to state material facts, and engaged in a course of conduct and practice that operated as a fraud or deceit, constituting unethical securities practices. Even if there had been no temporary cease and desist order in place, Knowles was still subject to the Act by transacting business as a securities salesperson without being registered. The record fully supported the Commissioner's conclusion that Knowles' conduct demonstrated a willful failure to comply with the Act, and Knowles presented no basis for concluding that the Commissioner's analysis was incorrect. Because the record supported the Commissioner's conclusion both factually and legally, the petition for judicial review should have been denied in its entirety, and the District Court's conclusion that Knowles did not commit a securities violation was reversed. Knowles v. State ex rel. Lindeen, 2009 MT 415, 353 M 507, 222 P3d 595 (2009).

Suitability Analysis Requirement Reasonable Interpretation of Securities Act: The Commissioner of Securities determined that in order to protect investors in situations where a salesperson does not have a preexisting relationship with a customer, a suitability analysis is critical once a customer indicates a desire to make a securities transaction in order to ensure that the transaction is suitable. Knowles contended that this requirement was an unreasonable extension of the meaning of unethical practices, but the Supreme Court disagreed. The Commissioner's interpretation was consistent with the spirit of the Securities Act of Montana and with ARM 6.10.401(1)(c) and was within the range of reasonable interpretation permitted by the administrative rule. Knowles v. State ex rel. Lindeen, 2009 MT 415, 353 M 507, 222 P3d 595 (2009).

30-10-202. Registration of securities.

Compiler's Comments

1997 Amendment: Chapter 533 inserted (2) regarding a federal covered security; and made minor changes in style.

Severability: Section 14, Ch. 533, L. 1997, was a severability clause.

1981 Amendment: Substituted "offer or sell" for "offer to sell" near the beginning of the section.

Source: Section 301, Uniform Securities Act.

Administrative Rules

ARM 6.10.150 Incorporation by reference consents to service of process previously filed.
ARM 6.10.208 Notice filings for offerings of investment company securities.
ARM 6.10.210 Notice filing procedures for Rule 506 offerings.
ARM 6.10.301 Montana limited offering exemption.

Case Notes

Other Charges Not Included Within or Specific Instances of Fraudulent Practices Charge — No Violation of Prohibition on Multiple Charges: In District Court, the defendant was convicted of six felonies related to his operation of a Ponzi scheme. On appeal to the Supreme Court, he argued that fraudulent practices (common scheme), as set forth in 30-10-301(1), subsumed the remaining five counts as lesser included offenses. The Supreme Court found that failure to register as a securities salesperson as set forth in 30-10-201 and failure to register a security as set forth in 30-10-202 require proof of failure to register, which is not an element of the offense of fraudulent practices, so the Supreme Court affirmed the defendant's convictions on these counts. St. v. Brandt, 2020 MT 79, 399 Mont. 415, 460 P.3d 427.

Jury Instructions Regarding Exemptions Disallowed — Defendant Not Eligible for Exemptions — No Applicability to Case: The defendant was charged with securities fraud. At trial, he sought to include language in the jury instructions that referred to exemptions to 30-10-201 and 30-10-202. The District Court did not allow the defendant's language because the exemptions had no application to the defendant's case since the defendant was not eligible for them in the first place. On appeal, the Supreme Court affirmed, ruling that the final jury instructions provided by the District Court did not fail to fully instruct the jury on the law applicable to the defendant's case. St. v. Reynolds, 2017 MT 25, 386 Mont. 267, 389 P.3d 243.

Securities Law — When Broker-Dealer Not Liable for Actions of Stockbroker Under Control Person Theory: Davis was a stockbroker for defendant broker-dealer. Davis advised plaintiffs to invest in a Ponzi scheme involving unregistered securities, and after plaintiffs lost their money, plaintiffs sued the broker-dealer on grounds that the broker-dealer was the control person for Davis and was therefore liable for plaintiffs' loss. The District Court concluded that the broker-dealer was not a control person and dismissed plaintiffs' action. The Supreme Court affirmed. Liability is imposed for directly or indirectly controlling the primary violator, but the control person avoids liability under 30-10-307(2) if the control person did not know, or in the exercise of reasonable care could not have known, of the facts upon which the violator's liability is premised and if the control person acted in good faith and did not directly or indirectly induce the act constituting the violation or cause of action. As a general rule, a broker-dealer controls its registered representatives, whether directly or indirectly, but is not an insurer of its representatives. However, certain actions by a stockbroker may be outside the broker-dealer's control, in which case the broker-dealer is not a control person and is thus not liable for the acts of the stockbroker, and that was the situation here. Davis did not act as a representative of the broker-dealer when he sold the assignments to plaintiffs, and the broker-dealer had no knowledge of or financial interest in the transaction. The assignments were separate arrangements between Davis and plaintiffs, and the broker-dealer did not control Davis's actions and was thus not liable for plaintiffs' loss. Mosley v. Am. Express Fin. Advisors, Inc., 2010 MT 78, 356 Mont. 27, 230 P.3d 479. See also Hollinger v. Titan Capital Corp., 914 F2d 1564 (9th Cir 1990), and Hauser v. Farrell, 14 F3d 1338 (9th Cir. 1994).

Specific Statute of Limitations Related to Fraudulent Sale of Securities Controlling Over General Statute of Limitations on Filing Claim: The District Court dismissed plaintiffs' Ponzi scheme claim concerning sale of unregistered securities in violation of 30-10-202, based on the statute of limitations in 30-10-307. The Supreme Court affirmed. The specific provisions of 30-10-307, requiring that a securities fraud claim be brought within 2 years after the violation occurs, control over the general statute of limitations in 27-2-102, requiring that a fraud action be brought within 2 years after discovery of the fraud or not more than 5 years after the transaction on which the claim is based. Plaintiffs' claim was not brought within 2 years after the unregistered security was offered or sold, so the statute of limitations in 30-10-307 was not met and the claim was properly dismissed. Mosley v. Am. Express Fin. Advisors, Inc., 2010 MT 78, 356 Mont. 27, 230 P.3d 479.

Test for Determining the Existence of an Investment Contract Security: Montana adopts the Forman test for determining the existence of an "investment contract security". "The touchstone [of an investment contract] is the presence of an investment in a common venture premised on a reasonable expectation of profits to be derived from the entrepreneurial or managerial efforts of others." 421 U.S. at 852. St. v. Duncan, 181 M 382, 593 P2d 1026 (1979). See also Redding v. District Court, 2012 MT 144, 365 Mont. 316, 281 P.3d 189.

30-10-203. Registration by notification.

Compiler's Comments

1981 Amendment: Added (2)(l) compelling submission of other information required by Commissioner; substituted "noon the 10th business day" for "3 p.m. mountain standard time the second full business day" in (3).

Source: Section 302, Uniform Securities Act.

30-10-204. Registration by coordination.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

1987 Amendments: Chapter 272 at beginning of (1)(a) reduced copies from three to one; and in (4), in first and second sentences, substituted "denial order" for "stop order".

Chapter 370 in first sentence of (4), near beginning, changed "(2)" to "(3)", near end inserted reference to (3), and made minor change in phraseology.

1981 Amendment: Added (1)(i) compelling submission of other information required by Commissioner; added "business" between "at least 10" and "days" in (2)(b); deleted "full" before "business days" in (2)(c).

Source: Section 303, Uniform Securities Act.

Federal Statute: The Securities Act of 1933, referred to in subsection (1) of this section, is compiled in the United States Code as Title 15, sec. 77a through 77aa.

30-10-205. Registration by qualification.

Compiler's Comments

2015 Amendment: Chapter 63 in (1)(m) substituted current text concerning ownership for "a specimen or copy of the security being registered"; and made minor changes in style. Amendment effective February 27, 2015.

Severability: Section 36, Ch. 63, L. 2015, was a severability clause.

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

1981 Amendment: Added (1)(p) compelling submission of other information required by Commissioner.

Source: Section 304, Uniform Securities Act.

Federal Statute: The Securities Act of 1933, referred to in subsection (3) of this section, is compiled in the United States Code as Title 15, sec. 77a through 77aa.

30-10-206. General provisions regarding registration of securities.

Compiler's Comments

1997 Amendment: Chapter 533 deleted (4)(a) that read: "(a) are issued by a face-amount certificate company or a redeemable security issued by an open-end management company or unit investment trust as those terms are defined in the Investment Company Act of 1940"; and made minor changes in style.

Severability: Section 14, Ch. 533, L. 1997, was a severability clause.

1993 Code Commissioner Correction — Name Change: Section 4, Ch. 162, L. 1993, provided: "Wherever the term "salesman" or its equivalent appears in Title 30, chapter 10, parts 1 through 3, or in legislation enacted by the 1993 legislature, the code commissioner shall substitute the term "salesperson" or its equivalent and make any necessary grammatical changes to reflect the name change." The term appeared in this section, and the change was subsequently made by the Code Commissioner.

1991 Amendment: In (1) deleted second sentence that read: "Any document filed under parts 1 through 3 of this chapter or a predecessor law within 3 years preceding the filing of a registration statement may be incorporated by reference in the registration statement to the extent that the document is currently accurate"; and in (3) inserted last sentence requiring registration of securities salesman. Amendment effective January 29, 1991.

1987 Amendments: Chapter 107 in (2)(a)(i), after "that", inserted "the following securities be deposited in escrow"; in (2)(a)(i)(A)(II), at end, deleted "be deposited in escrow"; inserted (2)(a)(i)(B) allowing the Commissioner to require that a security issued when a corporation is in a promotional or developmental stage be deposited in escrow; and made minor changes in phraseology.

Chapter 272 in (1), near middle of second sentence, reduced reference period from 5 years to 3 years; and inserted (5) requiring the Commissioner's consent to withdrawal of a registration statement.

Source: The source of the 1987 amendments to subsection (2) is the North American Securities Administrators Association guidelines.

1985 Amendment: Deleted former (5) that read: "During the period in which there is an offering of securities registered under the provisions of parts 1 through 3 of this chapter, and for which there is no exemption under 30-10-104 or 30-10-105, financial data for the issuer's fiscal year and such other statements as the commissioner may require shall be filed with the commissioner annually, not less than 90 days after the end of each such year. If such statements are not certified, the commissioner may verify them by examining the issuer's books and records."

1981 Amendment: Substituted "for a period of 1 year unless it is revoked" for "until revoked" near the beginning of (3); deleted "or until" before "terminated upon request" in (3); added "or renewed under 30-10-209(1)(b)" after "with the consent of the commissioner" in (3); substituted "in which there is an offering" for "of public offering in the initial distribution" near the beginning of (5); substituted "and for which there is no exemption under 30-10-104 or 30-10-105, financial data for the issuer's fiscal year and such other statements as the commissioner may require shall be filed" for "by notification or qualification, financial data or statements corresponding to those required under the provisions of 30-10-203(2) and 30-10-205 and to the insurer's fiscal year shall be filed" in (5).

Federal Statute: The Investment Company Act of 1940, referred to in subsection (4) of this section, is compiled in the United States Code as Title 15, sec. 80a-1 through 80a-52.

Administrative Rules

ARM 6.10.202 Promotional securities — escrow.

30-10-207. Denial, suspension, and revocation of registration of securities.

Compiler's Comments

1997 Amendment: Chapter 533 in (1)(b), at end after "violated", deleted "in connection with the offering"; in (1)(f), at end, inserted "by notification"; and made minor changes in style.

Severability: Section 14, Ch. 533, L. 1997, was a severability clause.

1987 Amendment: Near beginning of (2) substituted "suspension or revocation order" for "stop order".

Source: Section 306, Uniform Securities Act.

Administrative Rules

ARM 6.2.120 through 6.2.122 Procedural rules for contested case hearings.

ARM 6.10.207 Warrants and options.

Case Notes

Commencement of Statute of Limitations When Fraud Is Discovered, Not When Security Is Sold: Investors in a mining venture were notified by a letter dated October 19, 2007, that the purported assays that were used to solicit their investment were inaccurate. Suit was filed on October 14, 2009, within 2 years of notification of the inaccurate assays. The Supreme Court held that the claim accrued on date of notification, not some previous time when the investors may have known about problems with the mining venture but could not reasonably have discovered the assays were false before being notified on October 19, 2007. Garza v. Forquest Ventures, Inc., 2015 MT 284, 381 Mont. 189, 358 P.3d 189.

30-10-208. Consent to service of process — manner of service.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

1993 Code Commissioner Correction — Name Change: Section 4, Ch. 162, L. 1993, provided: "Wherever the term "salesman" or its equivalent appears in Title 30, chapter 10, parts 1 through 3, or in legislation enacted by the 1993 legislature, the code commissioner shall substitute the term "salesperson" or its equivalent and make any necessary grammatical changes to reflect the name change." The term appeared in this section, and the change was subsequently made by the Code Commissioner.

1991 Amendment: Near beginning of (1), after "salesman", inserted "or investment adviser representative" and deleted last sentence that read: "A person who has filed such a consent in connection with a previous registration need not file another"; and made minor changes in style. Amendment effective January 29, 1991.

30-10-209. Fees.

Compiler's Comments

2021 Amendment: Chapter 404 in (6)(b) in first sentence after "June 30" substituted "2027" for "2021" and in second sentence after "July 1" substituted "2027" for "2021"; and made minor changes in style. Amendment effective May 7, 2021.

Severability: Section 5, Ch. 404, L. 2021, was a severability clause.

2019 Amendment: Chapter 396 in (2)(a) in two places substituted "$400" for "$200"; in (2)(b)(i)(A) at beginning inserted "for an out-of-state salesperson or investment adviser representative" and in three places substituted "$100" for "$50"; inserted (2)(b)(i)(B) concerning the registration fee for an in-state salesperson or investment adviser representative; in (2)(b)(ii) near end substituted "fee in subsection (2)(b)(i)(A) or (2)(b)(i)(B)" for "$50 fee"; in (2)(c) in two places substituted "$400" for "$200"; in (4) at end substituted "$100" for "$50"; and made minor changes in style. Amendment effective May 8, 2019.

2017 Amendment: Chapter 151 in (6)(b) in first sentence substituted "June 30, 2021" for "June 30, 2017" and in second sentence substituted "July 1, 2021" for "July 1, 2017"; and made minor changes in style. Amendment effective April 4, 2017.

Severability: Section 57, Ch. 151, L. 2017, was a severability clause.

2013 Amendment: Chapter 66 in (6)(a) substituted "Except as provided in subsection (6)(b)" for "Except for notice filing fees established in subsection (1)(d) and examination costs collected under 30-10-210"; inserted (6)(b) concerning deposit of renewal or notice filing fees and collected examination costs; and made minor changes in style. Amendment effective March 7, 2013.

Severability: Section 4, Ch. 66, L. 2013, was a severability clause.

2011 Amendment: Chapter 227 in (1)(d) in two places and in (6) before "notice" deleted "portfolio"; in (6) substituted "subsection (1)(d)" for "this section"; and made minor changes in style. Amendment effective April 20, 2011.

Severability: Section 25, Ch. 227, L. 2011, was a severability clause.

2005 Amendment: Chapter 469 in (6) near beginning after "section" inserted "and examination costs collected under 30-10-210" and after "fees" deleted "examination charges"; and made minor changes in style. Amendment effective October 1, 2005.

2003 Amendment: Chapter 156 in (1)(d) inserted fourth sentence providing that the issuer shall pay a fee of $50 for each filing made for the purpose of changing the name of a series, portfolio, or other subdivision of an investment company or similar issuer; and made minor changes in style. Amendment effective October 1, 2003.

1999 Amendment: Chapter 51 in (6) near beginning after "portfolio" substituted "notice filing" for "registration". Amendment effective March 15, 1999.

1997 Amendment: Chapter 533 in (1)(a), after "qualification", inserted "or for notice filing of a federal covered security", before "year" substituted "initial" for "first", after "registration" inserted "or notice filing", before "fee" deleted "registration", and after "maximum" inserted "fee"; in (1)(b), near beginning of first sentence after "securities", inserted "or a notice filing of a federal covered security", after "payment of" substituted "a renewal" for "an additional registration", and at end deleted "even though the maximum fee was paid the preceding year", at beginning of second sentence, after "The", substituted "renewal" for "additional registration", and in third sentence, after "registration", substituted "or the notice filing" for "statement for the securities"; in (1)(c), near beginning of first sentence after "registrant", inserted "or issuer of federal covered securities", after "state" inserted "or for which a notice filing has been submitted", after second "registrant" inserted "or issuer", and after "statement" inserted "or notice filing", in second sentence, after first "registrant", inserted "or issuer of a federal covered security", after "order" inserted "or notice", and after second "registrant" inserted "or issuer", and in two places in third sentence, after "registration", inserted "or notice"; in (1)(d), in second and third sentences after "portfolio", substituted "notice filing" for "registration"; inserted (2)(c) regarding fees for a federal covered adviser; and made minor changes in style.

Severability: Section 14, Ch. 533, L. 1997, was a severability clause.

1995 Amendment: Chapter 261 in (2)(b) inserted second sentence excusing certain salespersons from paying investment adviser representative registration fee; and made minor changes in style. Amendment effective March 27, 1995.

1993 Amendment: Chapter 462 inserted (1)(d) requiring that each series, portfolio, or subdivision of an investment company be treated as a separate issuer and providing that portfolio registration fees be deposited in the state special revenue account; at beginning of (6) inserted exception clause; and made minor changes in style.

1993 Code Commissioner Correction — Name Change: Section 4, Ch. 162, L. 1993, provided: "Wherever the term "salesman" or its equivalent appears in Title 30, chapter 10, parts 1 through 3, or in legislation enacted by the 1993 legislature, the code commissioner shall substitute the term "salesperson" or its equivalent and make any necessary grammatical changes to reflect the name change." The term appeared in this section, and the change was subsequently made by the Code Commissioner.

1991 Amendment: In (3), after "certified", inserted "or uncertified". Amendment effective January 29, 1991.

1989 Amendment: In (6), after "charges", deleted "except" and after "deposited" deleted "into the securities regulatory trust account, pursuant to 30-10-115 through 30-10-118"; deleted former (7) that read: "(7) All fines and penalties collected by the commissioner pursuant to parts 1 through 3 of this chapter and the rules adopted hereunder must be deposited into the general fund"; and made minor changes in punctuation and phraseology. Amendment effective July 1, 1989.

1987 Amendments: Chapter 269 in (2)(b), after "salesman", inserted "or investment adviser representative".

Chapter 272 deleted former (5) that read: "(5) For waiver of the residency requirement of 30-10-201(4), the fee shall be $50 for each original registration."

Source: The source of the amendments to this section made by Ch. 269, L. 1987, is the North American Securities Administrators Association guidelines.

1985 Amendments: Chapter 385 inserted (7) providing for allocation of fees and charges; and inserted (8) providing for allocation of fines and penalties.

Chapter 478 in (1)(c) substituted language relating to filing of amendment to registration statement when excess amount of securities is sold for "A registration of securities may be renewed after its termination date upon payment of the additional registration fee and a late renewal fee of $50. The late renewal fee may be waived by the commissioner upon a showing of good cause"; deleted (1)(d) and (1)(e) that read: "(d) For filing an annual statement, a posteffective amendment to a registration of securities, or a name change, the fee shall be $10.

(e) When an application for registration of securities is denied or withdrawn, the commissioner shall retain the fee"; deleted (2)(c) and (2)(d) that read: "(c) When an application for registration as a broker-dealer, salesman, or investment adviser is denied or withdrawn, the commissioner shall retain the fee.

(d) For filing posteffective amendments to a registration of a broker-dealer, salesman, or investment adviser, the fee shall be $10, except that there is no fee for filing an address change of a salesman or a notice of disciplinary action"; in (4) substituted "30-10-105(15)" for "30-10-105(16)" and near end, after "exemption", inserted "or an exception to the provisions of parts 1 through 3 of this chapter"; inserted (5) providing fee for waiver of residency requirement; and inserted (6) providing that fees are earned when received and allowing partial refund for overpayment.

1983 Amendment: At end of (2)(b) inserted "and $50 for each transfer"; in (4) after "an exemption" inserted "under 30-10-105(16), the fee shall be established by the commissioner by rule, for a request for any other exemption".

Statement of Intent: The statement of intent attached to SB 184 (Ch. 322, L. 1983) provided: "A Statement of Intent is required for this bill because it grants the Securities Commissioner the authority to adopt rules exempting certain securities transactions from registration and to establish fees for granting such exemption. There is to be no exemption from the antifraud provisions of the Securities Act.

(1) The legislature intends that the exemption rules:

(a) provide limited relief from the registration provisions of the Act for small and existing businesses that are attempting to raise a limited amount of funds; and

(b) provide an exemption from the registration provisions of the Securities Act for transactions in securities when the securities involved are adequately regulated by other bodies.

(2) The Legislature intends that the fee rules would establish a fee schedule to match the cost and complexity of the exemption. The Legislature does not intend that the state either lose or gain any revenue because of any exemption under 30-10-105(16)."

1981 Amendment: Redesignated all subsections; increased the registration fee from $100 to $200 in (1)(a) and (1)(b); increased the percentages from 1/20 to 1/10 of 1% in (1)(a) and (1)(b); substituted "a registration of securities may be renewed, prior to its termination date, for an additional year upon consent of the commissioner and payment of an additional registration fee" for "a registration remains in effect for securities with respect to which reports are required to be filed under 30-10-206(4), an additional registration fee shall be paid to the commissioner" in (1)(b); deleted "When an application for registration of securities is denied or withdrawn, the commissioner shall retain the fee." from the end of (1)(b), (2)(a), and (2)(b); inserted (1)(c) allowing for late renewal upon payment of fees and permitting waiver of late fee; inserted (1)(e) allowing for retention of fee upon denial or withdrawal of application of securities registration; inserted (2)(c) allowing for retention of fee upon denial or denial of registrant's application; and inserted (2)(d) setting fee for filing posteffective amendments to registrant's registration; inserted "a post-effective amendment to a registration of securities, or a name change" in (1)(d); increased the fees in (2)(b) and (4) from $25 to $50; deleted "or exception to the provisions of this chapter" after "exemption" in (4).

Administrative Rules

ARM 6.10.150 Incorporation by reference consents to service of process previously filed.

30-10-210. Examination costs.

Compiler's Comments

1999 Amendment: Chapter 472 in (2) in first sentence after "shall" substituted "deposit examination costs collected under this section in the special revenue account provided for in 30-10-115" for "pay to the state treasurer to the credit of the general fund all moneys received hereunder"; and made minor changes in style. Amendment effective October 1, 1999.

Severability: Section 71, Ch. 472, L. 1999, was a severability clause.

Saving Clause: Section 72, Ch. 472, L. 1999, was a saving clause.

1989 Amendment: Near beginning of (1) and in three places in (3), after "broker-dealer", inserted "or investment adviser"; and made minor changes in phraseology and punctuation. Amendment effective March 22, 1989.

1981 Amendment: Deleted "investigated or" after "broker-dealer who is" at the beginning of (1); deleted "all at reasonable rates customary therefor and as established and adopted by the commissioner upon July 1, 1961, and annually thereafter" before "upon presentation of a detailed account" in (1); added "however, no reimbursement of expenses may be required for routine examinations performed in connection with an application for registration" near the end of (1).

30-10-211. Federal covered securities.

Compiler's Comments

2003 Amendment: Chapter 156 in (1) at beginning of introductory clause substituted "An issuer is required to file the following documents" for "The commissioner may require an issuer to file any or all of the following documents"; and in (2) substituted language requiring the issuer to file notice within 15 days after first sale and to pay the notice filing fee for former language allowing the commissioner to require the issuer to file notice within 15 days after first sale and to pay the notice filing fee. Amendment effective October 1, 2003.

Severability: Section 14, Ch. 533, L. 1997, was a severability clause.

Administrative Rules

ARM 6.10.150 Incorporation by reference consents to service of process previously filed.
ARM 6.10.208 Notice filings for offerings of investment company securities.
ARM 6.10.210 Notice filing procedures for Rule 506 offerings.
ARM 6.10.301 Montana limited offering exemption.

Part 3
Offenses, Penalties, and Immunities

30-10-301. Fraudulent and other prohibited practices.

Compiler's Comments

2015 Amendment: Chapter 318 in (7) in two places substituted "multilevel marketing company" for "multilevel distribution company". Amendment effective October 1, 2015.

Saving Clause: Section 7, Ch. 318, L. 2015, was a saving clause.

2013 Amendment: Chapter 286 inserted (7) concerning prohibitions on multilevel distribution companies. Amendment effective April 24, 2013.

1997 Amendment: Chapter 533 in (4), after "adviser", inserted "who is registered or required to be registered"; and made minor changes in style.

Severability: Section 14, Ch. 533, L. 1997, was a severability clause.

1987 Amendment: Near beginning of (2)(a) inserted "directly or indirectly"; inserted (2)(a)(iii) through (2)(b) making it an offense to sell a security without disclosing certain information except if the broker-dealer is not being compensated; inserted (3) making it an offense to solicit advisory clients by making false statements or by omitting material facts; in (4), at beginning, inserted exception clause and at end of introductory clause inserted "in writing"; in (5) changed references to subsections (a) and (b) to subsections (4)(a) and (4)(b); and inserted (6) making it an offense to take or have securities or funds if the Commissioner by rule prohibits such custody or, in the absence of a rule, the adviser does not notify the Commissioner of such custody.

1981 Amendment: Added "in, into, or from this state" to the introductory clause of (1).

Source: Sections 101 and 102, Uniform Securities Act.

Administrative Rules

ARM 6.10.307 Filings requirement for transactional exemption pursuant to 30-10-105(15), MCA.

ARM 6.10.401 Fraudulent and unethical practices prohibited by broker-dealers and salespersons.

ARM 6.10.402 Fraudulent and unethical practices prohibited.

Title 6, chapter 10, subchapter 6, ARM Senior specific certifications and designations.

Case Notes

Other Charges Not Included Within or Specific Instances of Fraudulent Practices Charge — No Violation of Prohibition on Multiple Charges: In District Court, the defendant was convicted of six felonies related to his operation of a Ponzi scheme. On appeal to the Supreme Court, he argued that fraudulent practices (common scheme), as set forth in 30-10-301(1), subsumed the remaining five counts as lesser included offenses. The Supreme Court found that one of the charges should have been subsumed, but that each of the remaining four counts required at least one element that was not contained in the offense of fraudulent practices. Exploitation of an older person as set forth in 52-3-825 requires proof that the victim is a person 65 years or older, which is not an element of the offense of fraudulent practices. Failure to register as a securities salesperson as set forth in 30-10-201 and failure to register a security as set forth in 30-10-202 require proof of failure to register, which is not an element of the offense of fraudulent practices. Operating a Ponzi scheme as set forth under 30-10-324 and 30-10-325 requires proof that the operator has made payments to earlier investors using funds obtained from later investors, which is not an element of the offense of fraudulent practices. The Supreme Court affirmed the defendant's convictions on these four counts. St. v. Brandt, 2020 MT 79, 399 Mont. 415, 460 P.3d 427. (Annotator's note: Section 28, Ch. 12, L. 2023, replaced the term "older person" in 30-10-301 with the newly defined term "vulnerable adult".)

Prohibition on Multiple Charges Violated by Failure to Charge Embezzlement as Lesser Included Offense of Fraudulent Practices — Ineffective Assistance of Counsel: In District Court, the defendant was convicted of six felonies related to his operation of a Ponzi scheme. On appeal, he argued that fraudulent practices (common scheme), as set forth in 30-10-301(1), subsumed the remaining five counts as lesser included offenses. The Supreme Court found that the theft by embezzlement (common scheme) charge should have been included because embezzlement was an element of the fraudulent practices charge. The court vacated the embezzlement conviction and found that the defendant's counsel provided ineffective assistance by failing to object to the charging, conviction, and sentencing on the multiple offenses. St. v. Brandt, 2020 MT 79, 399 Mont. 415, 460 P.3d 427.

Adequate Definition of "Security" for Jury — Willful Conduct Standard Applicable to Securities Act Violations — Omission of Investment Prospectus Not Fraudulent at Time — Securities Restitution Properly Awarded: The defendant, a pastor, was approached by the plaintiff, a member of his congregation, about investing money. The defendant convinced the plaintiff to purchase stock in the defendant's Mexico-domiciled company. Ultimately, the investment promises never materialized and the defendant was convicted of failure to register as a securities salesperson, failure to register a security, and fraudulent practices under the Securities Act of Montana. On appeal, the defendant argued that the term "security" was not adequately or specifically defined for the jury, that the "willful" standard was inappropriate to attach to the charges, that the conviction of fraudulent practices was improper because neither the statute nor administrative rule required an investment prospectus at the time of the violation, and that the award of restitution was improper. The Supreme Court held that the evidence showed that the jury reasonably concluded that the defendant had sold a security because the shares in the company constituted a stock, that the Legislature specifically included a willful standard for Securities Act violations, that the fraudulent practices conviction was improper because failure to provide a prospectus was not part of the statute at the time, and that the award of restitution was proper because the loss stemmed directly from the defendant's conduct. St. v. Himes, 2015 MT 91, 378 Mont. 419, 345 P.3d 297.

Defendant's Conduct Constituting Same Transaction When Motivated By Goal of Accomplishing Single Criminal Objective: The single goal of enticing a victim to invest in the defendant's enterprise motivated the defendant's conduct. The fact that the victim invested multiple times did not mean the defendant was liable for multiple criminal counts when the investment was motivated by a single criminal objective. Furthermore, because the statutory elements of the charged counts are the same, they are included offenses. St. v. Parks, 2013 MT 280, 372 Mont. 88, 310 P.3d 1088.

Securities Act Violation — Petition for Judicial Review Improperly Granted: The Commissioner of Securities concluded that Knowles violated various provisions of the Securities Act of Montana. Knowles petitioned for judicial review, which was granted. The District Court reversed the Commissioner's decision. On appeal, the Supreme Court affirmed the Commissioner's decision that Knowles employed a scheme or artifice to defraud, failed to state material facts, and engaged in a course of conduct and practice that operated as a fraud or deceit, constituting unethical securities practices. Even if there had been no temporary cease and desist order in place, Knowles was still subject to the Act by transacting business as a securities salesperson without being registered. The record fully supported the Commissioner's conclusion that Knowles' conduct demonstrated a willful failure to comply with the Act, and Knowles presented no basis for concluding that the Commissioner's analysis was incorrect. Because the record supported the Commissioner's conclusion both factually and legally, the petition for judicial review should have been denied in its entirety, and the District Court's conclusion that Knowles did not commit a securities violation was reversed. Knowles v. State ex rel. Lindeen, 2009 MT 415, 353 M 507, 222 P3d 595 (2009).

Suitability Analysis Requirement Reasonable Interpretation of Securities Act: The Commissioner of Securities determined that in order to protect investors in situations where a salesperson does not have a preexisting relationship with a customer, a suitability analysis is critical once a customer indicates a desire to make a securities transaction in order to ensure that the transaction is suitable. Knowles contended that this requirement was an unreasonable extension of the meaning of unethical practices, but the Supreme Court disagreed. The Commissioner's interpretation was consistent with the spirit of the Securities Act of Montana and with ARM 6.10.401(1)(c) and was within the range of reasonable interpretation permitted by the administrative rule. Knowles v. State ex rel. Lindeen, 2009 MT 415, 353 M 507, 222 P3d 595 (2009).

Predispute Arbitration Provisions Unenforceable — Motion to Compel Arbitration Properly Denied: Plaintiff opened several Piper Automatic Transfer Accounts and later brought an action alleging defendants' mismanagement of the accounts. Defendants sought to compel arbitration based on predispute arbitration clauses in the account agreements requiring that any dispute be resolved by arbitration. The motion to compel arbitration was denied, and defendants appealed. The Supreme Court held that because the agreements granted defendants' brokers the discretion to buy and sell securities, a fiduciary duty was created that defendants breached by failing to explain the consequences of the arbitration provision prior to formation of the contract. The predispute arbitration provisions were therefore unenforceable, and denial of the motion to compel arbitration was affirmed. Willems v. U.S. Bancorp Piper Jaffray, Inc., 2005 MT 37, 326 M

103, 107 P3d 465 (2005), following Kloss v. Edward D. Jones & Co., 2002 MT 129, 310 M 123, 54 P3d 1 (2002). See also Chor v. Piper, Jaffray & Hopwood, 261 M 143, 862 P2d 26 (1993).

Security Brokerage Contracts — Contract of Adhesion Rendering Arbitration Clause Unenforceable: Kloss opened a full-service brokerage account with defendant, which permitted Kloss to purchase securities and maintain a money market account and which included a living trust account. The account did well, and Kloss decided to set up a charitable trust with the bond proceeds. The initial account and the living trust agreement contained a mandatory arbitration clause, and the charitable trust incorporated the arbitration clause by reference. Kloss then had second thoughts about the charitable trust and petitioned to revoke it. Defendant moved to compel arbitration, and the District Court granted the motion, citing Chor v. Piper, Jaffray & Hopwood, 261 M 143, 862 P2d 26 (1993), and Iwen v. U.S. W. Direct, 1999 MT 63, 293 M 512, 977 P2d 989 (1999), for the holding that defendant had no obligation to explain the terms of the contract because it was within Kloss's reasonable expectations and that even if the contract was considered a contract of adhesion, it was not unenforceable because it was not unconscionable. Kloss appealed, arguing that the arbitration clause was part of a contract of adhesion and that waiver of the constitutional right to jury trial should not be presumed from the signing of a contract of adhesion. Defendant maintained that form contracts prepared by securities brokers are not contracts of adhesion dictated by one party to another who has no voice in its formulation, and that arbitration clauses contained in the contracts are not unconscionable. The Supreme Court examined Passage v. Prudential-Bache Sec., Inc., 223 M 60, 727 P2d 1298 (1986), for an explanation of contracts of adhesion in the securities context and the circumstances under which they are unenforceable. The court distinguished both Chor and Passage, finding that the contracts in this case were clearly contracts of adhesion because they were standardized forms containing terms that Kloss had no opportunity to negotiate if wishing to invest with defendant. Further, the arbitration clause by which Kloss waived the right to access to state courts, the right to jury trial, the right to reasonable discovery, the right to findings of fact based on the evidence, and the right to enforce the law by way of appeal was clearly not within Kloss's reasonable expectations. The arbitration clause was never explained by defendant, and Kloss was not aware of the arbitration provision in the contract. Thus, the District Court committed reversible error when it concluded that the arbitration clause was enforceable. Kloss v. Edward D. Jones & Co., 2002 MT 129, 310 M 123, 54 P3d 1 (2002), followed in Larsen v. W. St. Ins. Agency, Inc., 2007 MT 270, 339 M 407, 170 P3d 956 (2007), with regard to factors to be applied in determining a contract of adhesion.

Implied Code of Stockbroker Conduct — When Fiduciary Relationship Created: This section creates an implied code of conduct for stockbrokers, violation of which may constitute a breach of the duty that a stockbroker owes to a customer. However, in the absence of discretionary authority by a stockbroker to buy and sell in a customer's account, a fiduciary relationship is not created in a stockbroker-customer relationship. Chor v. Piper, Jaffray & Hopwood, 261 M 143, 862 P2d 26, 50 St. Rep. 1234 (1993), citing Caravan Mobile Home Sales v. Lehman Bros. Kuhn Loeb, 769 F2d 561 (9th Cir. 1985), and Cohen v. Wedbush, Noble, Cooke, Inc., 841 F2d 282 (9th Cir. 1988), and followed in Kloss v. Edward D. Jones & Co., 2002 MT 129, 310 M 123, 54 P3d 1 (2002).

Breach of Duty: This section implicitly establishes a code of conduct to be followed by a broker. A violation of this code of conduct may constitute a breach of the duty owed by the broker to his customer and presents a genuine issue of material fact. Brown v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 197 M 1, 640 P2d 453, 39 St. Rep. 305 (1982), distinguished in Chor v. Piper, Jaffray & Hopwood, 261 M 143, 862 P2d 26, 50 St. Rep. 1234 (1993). See also Cohen v. Wedbush, Noble, Cooke, Inc., 841 F2d 282 (9th Cir. 1988).

Prosecution When Conduct Violates Two Statutes: When defendant argues that he should have been charged under 30-10-301, the specific fraudulent securities practice statute, rather than 45-6-317, the general deceptive practices statute, the Supreme Court said that in the rule of statutory construction a more specific statute controls over an inconsistent general statute and does not apply to criminal prosecutions where defendant's conduct violated two or more criminal statutes. The fact that two statutes overlap does not mean that the defendant can only be prosecuted under the statute providing the lesser penalty. St. v. Duncan, 181 M 382, 593 P2d 1026 (1979).

30-10-302. Misleading filings.

Compiler's Comments

Source: Section 404, Uniform Securities Act.

30-10-303. Unlawful representation concerning registration or exemption.

Compiler's Comments

2015 Amendment: Chapter 318 in (1) after "30-10-201(6)" deleted "or 30-10-216" and after "30-10-211" inserted "or 30-10-327". Amendment effective October 1, 2015.

Saving Clause: Section 7, Ch. 318, L. 2015, was a saving clause.

2013 Amendment: Chapter 286 in (1) inserted "or 30-10-216"; in (2) substituted "person, security, or transaction" for "security or a transaction". Amendment effective April 24, 2013.

1997 Amendment: Chapter 533 in (1), near beginning substituted "30-10-201(6), a notice filing under 30-10-211" for "30-10-201(4)" and near middle, after "registered", inserted "or a complete notice filing has been made"; in (2), at beginning after "fact", inserted "that an application for registration or a notice filing has been filed or a person or security is effectively registered or a complete notice filing has been made as provided in subsection (1) or"; and made minor changes in style.

Severability: Section 14, Ch. 533, L. 1997, was a severability clause.

Source: Section 405, Uniform Securities Act.

30-10-304. Investigations and subpoenas.

Compiler's Comments

1993 Amendment: Chapter 540 in (4), near middle, substituted "However, testimony or evidence that is compelled following a claim of privilege against self-incrimination" for "but no compelled testimony or evidence"; and made minor changes in style. Amendment effective July 1, 1993.

1989 Amendment: Inserted (5) making Office of Securities Commissioner a criminal justice agency. Amendment effective March 15, 1989.

1987 Amendment: Inserted (2)(b) allowing the Commissioner to issue and enforce subpoenas for another state's regulator.

1983 Amendment: In (4), in first sentence after "but no" substituted language prohibiting use of compelled testimony, evidence, or information in a criminal proceeding for "individual may be prosecuted or subjected to any penalty or forfeiture for or on account of any transaction, matter, or thing concerning which he is compelled, after claiming his privilege against self-incrimination, to testify or produce evidence (documentary or otherwise), except that the individual so testifying shall not be exempt from prosecution and punishment for perjury committed in so testifying."

Source: Section 407, Uniform Securities Act.

30-10-305. Injunctions and other remedies — limitations on actions.

Compiler's Comments

Extension of Termination Date: Sections 3 and 4, Ch. 404, L. 2021, amended sec. 16, Ch. 58, L. 2011, and sec. 55, Ch. 151, L. 2017, by extending the termination date imposed by those sections to June 30, 2027. Effective May 7, 2021.

Extension of Termination Date: Section 55, Ch. 151, L. 2017, amended sec. 16, Ch. 58, L. 2011, by extending the termination date imposed by Ch. 58 to June 30, 2021. Effective April 4, 2017.

2015 Amendment: Chapter 28 inserted (3)(b) concerning willful acts or practices affecting a vulnerable person; in (3)(c) inserted "under this subsection (3)"; and made minor changes in style. Amendment effective February 18, 2015.

Saving Clause: Section 6, Ch. 28, L. 2015, was a saving clause.

Severability: Section 7, Ch. 28, L. 2015, was a severability clause.

2011 Amendment: Chapter 58 inserted (5) authorizing a contribution to the securities restitution assistance fund; and made minor changes in style. Amendment effective March 25, 2011, and terminates June 30, 2017.

Severability: Section 13, Ch. 58, L. 2011, was a severability clause.

Applicability: Section 15, Ch. 58, L. 2011, provided: "[This act] applies to final orders issued on or after [the effective date of this act]." Effective March 25, 2011.

1993 Amendment: Chapter 540 in (1)(a)(i), at end, substituted "examiner issues proposed findings of fact and conclusions of law and a proposed order" for "on the allegations contained in the cease and desist order is held"; and made minor changes in style. Amendment effective July 1, 1993.

1989 Amendment: In (4)(a) and (4)(b) substituted reference to 30-10-201(1) through (3) and 30-10-202 for reference to 30-10-201 through 30-10-205; and made minor changes in phraseology. Amendment effective March 22, 1989.

1987 Amendment: After (1) substituted "If" for "Whenever"; and inserted (4) stating statutes of limitations for administrative and civil actions brought under this section.

Retroactive Application: Section 4, Ch. 231, L. 1987, provided: "Sections 1 and 2 apply retroactively, within the meaning of 1-2-109, to a securities transaction occurring prior to the effective date of this act for which no action has been commenced within 1 year from the effective date of this act." Effective March 27, 1987.

1985 Amendments: Chapter 407 inserted (3) relating to imposition of civil fine for violation of parts 1 through 3 of this chapter and rules adopted thereunder.

Chapter 478 in (1)(a) in second sentence, after "10 days after", substituted "the hearing on the allegations contained in the cease and desist order" for "any hearing".

Source: Section 408, Uniform Securities Act.

Administrative Rules

ARM 6.2.120 through 6.2.122 Procedural rules for contested case hearings.

30-10-306. Criminal liabilities.

Compiler's Comments

2015 Amendment: Chapter 28 inserted (2) concerning willful violations with knowledge that the violation would affect a vulnerable person; and made minor changes in style. Amendment effective February 18, 2015.

Saving Clause: Section 6, Ch. 28, L. 2015, was a saving clause.

Severability: Section 7, Ch. 28, L. 2015, was a severability clause.

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

1981 Amendment: Increased imprisonment from 3 to 10 years in first sentence of subsection (1); increased time limitation from 5 to 8 years in second sentence of subsection (1); and added clause providing for extension of time period at the end of subsection (1).

Source: Section 409, Uniform Securities Act.

Case Notes

Adequate Definition of "Security" for Jury — Willful Conduct Standard Applicable to Securities Act Violations — Omission of Investment Prospectus Not Fraudulent at Time — Securities Restitution Properly Awarded: The defendant, a pastor, was approached by the plaintiff, a member of his congregation, about investing money. The defendant convinced the plaintiff to purchase stock in the defendant's Mexico-domiciled company. Ultimately, the investment promises never materialized and the defendant was convicted of failure to register as a securities salesperson, failure to register a security, and fraudulent practices under the Securities Act of Montana. On appeal, the defendant argued that the term "security" was not adequately or specifically defined for the jury, that the "willful" standard was inappropriate to attach to the charges, that the conviction of fraudulent practices was improper because neither the statute nor administrative rule required an investment prospectus at the time of the violation, and that the award of restitution was improper. The Supreme Court held that the evidence showed that the jury reasonably concluded that the defendant had sold a security because the shares in the company constituted a stock, that the Legislature specifically included a willful standard for Securities Act violations, that the fraudulent practices conviction was improper because failure to provide a prospectus was not part of the statute at the time, and that the award of restitution was proper because the loss stemmed directly from the defendant's conduct. St. v. Himes, 2015 MT 91, 378 Mont. 419, 345 P.3d 297.

Test for Determining the Existence of an Investment Contract Security: Montana adopts the Forman test for determining the existence of an "investment contract security". "The touchstone [of an investment contract] is the presence of an investment in a common venture premised on a reasonable expectation of profits to be derived from the entrepreneurial or managerial efforts of others." 421 U.S. at 852. St. v. Duncan, 181 M 382, 593 P2d 1026 (1979). See also Redding v. District Court, 2012 MT 144, 365 Mont. 316, 281 P.3d 189.

30-10-307. Civil liabilities — limitations on actions.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

1993 Code Commissioner Correction — Name Change: Section 4, Ch. 162, L. 1993, provided: "Wherever the term "salesman" or its equivalent appears in Title 30, chapter 10, parts 1 through 3, or in legislation enacted by the 1993 legislature, the code commissioner shall substitute the term "salesperson" or its equivalent and make any necessary grammatical changes to reflect the name change." The term appeared in this section, and the change was subsequently made by the Code Commissioner.

1987 Amendments: Chapter 231 inserted (5) stating statutes of limitations for civil actions brought under this section.

Chapter 272 near beginning of (1) substituted "violation of 30-10-202" for "violation of any provisions of 30-10-202 through 30-10-205".

Retroactive Application: Section 4, Ch. 231, L. 1987, provided: "Sections 1 and 2 apply retroactively, within the meaning of 1-2-109, to a securities transaction occurring prior to the effective date of this act for which no action has been commenced within 1 year from the effective date of this act." Effective March 27, 1987.

1981 Amendment: Increased the interest rate from 6% to 10% near the middle of (1) and in (1)(b), (3)(a), and (3)(b)(ii).

Source: Section 410, Uniform Securities Act.

Case Notes

Commencement of Statute of Limitations When Fraud Is Discovered, Not When Security Is Sold: Investors in a mining venture were notified by a letter dated October 19, 2007, that the purported assays that were used to solicit their investment were inaccurate. Suit was filed on October 14, 2009, within 2 years of notification of the inaccurate assays. The Supreme Court held that the claim accrued on date of notification, not some previous time when the investors may have known about problems with the mining venture but could not reasonably have discovered the assays were false before being notified on October 19, 2007. Garza v. Forquest Ventures, Inc., 2015 MT 284, 381 Mont. 189, 358 P.3d 189.

Securities Law — When Broker-Dealer Not Liable for Actions of Stockbroker Under Control Person Theory: Davis was a stockbroker for defendant broker-dealer. Davis advised plaintiffs to invest in a Ponzi scheme involving unregistered securities, and after plaintiffs lost their money, plaintiffs sued the broker-dealer on grounds that the broker-dealer was the control person for Davis and was therefore liable for plaintiffs' loss. The District Court concluded that the broker-dealer was not a control person and dismissed plaintiffs' action. The Supreme Court affirmed. Liability is imposed for directly or indirectly controlling the primary violator, but the control person avoids liability under 30-10-307(2) if the control person did not know, or in the exercise of reasonable care could not have known, of the facts upon which the violator's liability is premised and if the control person acted in good faith and did not directly or indirectly induce the act constituting the violation or cause of action. As a general rule, a broker-dealer controls its registered representatives, whether directly or indirectly, but is not an insurer of its representatives. However, certain actions by a stockbroker may be outside the broker-dealer's control, in which case the broker-dealer is not a control person and is thus not liable for the acts of the stockbroker, and that was the situation here. Davis did not act as a representative of the broker-dealer when he sold the assignments to plaintiffs, and the broker-dealer had no knowledge of or financial interest in the transaction. The assignments were separate arrangements between Davis and plaintiffs, and the broker-dealer did not control Davis's actions and was thus not liable for plaintiffs' loss. Mosley v. Am. Express Fin. Advisors, Inc., 2010 MT 78, 356 Mont. 27, 230 P.3d 479. See also Hollinger v. Titan Capital Corp., 914 F2d 1564 (9th Cir 1990), and Hauser v. Farrell, 14 F3d 1338 (9th Cir. 1994).

Specific Statute of Limitations Related to Fraudulent Sale of Securities Controlling Over General Statute of Limitations on Filing Claim: The District Court dismissed plaintiffs' Ponzi scheme claim concerning sale of unregistered securities in violation of 30-10-202, based on the statute of limitations in 30-10-307. The Supreme Court affirmed. The specific provisions of 30-10-307, requiring that a securities fraud claim be brought within 2 years after the violation occurs, control over the general statute of limitations in 27-2-102, requiring that a fraud action be brought within 2 years after discovery of the fraud or not more than 5 years after the transaction on which the claim is based. Plaintiffs' claim was not brought within 2 years after the unregistered security was offered or sold, so the statute of limitations in 30-10-307 was not met and the claim was properly dismissed. Mosley v. Am. Express Fin. Advisors, Inc., 2010 MT 78, 356 Mont. 27, 230 P.3d 479.

Recovery Limited in Fraudulent Sale of Securities — Punitive Damages Claim Dismissed: In a case alleging breach of contract for sale of a security by means of fraud, recovery was limited under this section to consideration paid for the security plus interest, costs, and attorney fees. A claim for punitive damages was properly dismissed. State ex rel. Vranish v. District Court, 228 M 59, 741 P2d 412, 44 St. Rep. 1341 (1987).

Eight-Year Statute of Limitations for Civil Action Under Securities Act of Montana: The U.S. District Court for the District of Montana certified a question to the Supreme Court on the applicable Statute of Limitations for a civil action brought pursuant to 30-10-307. In deciding that the 8-year limitation period rather than the 2-year period applied, the court traced the legislative history of the civil enforcement limitation period under the Securities Act of Montana. In 1967, the Legislature eliminated the relevant 2-year limitation and left a void. The court reviewed the legislative intent, underlying purposes of the Act, and characterization of the essence of the claim. Finding that each count of plaintiff's complaint could be interpreted as sounding in tort, contract, or statutory violation, the court resolved the case in favor of the longest limitation period. Thiel v. Taurus Drilling Ltd. 1980-II, 218 M 201, 710 P2d 33, 42 St. Rep. 1520 (1985), followed in Ritland v. Rowe, 260 M 453, 861 P2d 175, 50 St. Rep. 1183 (1993). (See Ch. 231, L. 1987, that inserted subsection (5) establishing statutes of limitations.) See also State ex rel. Vranish v. District Court, 228 M 59, 741 P2d 412, 44 St. Rep. 1341 (1987).

30-10-308. Judicial review of orders.

Compiler's Comments

2011 Amendment: Chapter 227 substituted current language for former text (see 2011 Session Law for former text). Amendment effective April 20, 2011.

Severability: Section 25, Ch. 227, L. 2011, was a severability clause.

Source: Section 411, Uniform Securities Act.

30-10-310. Reporting requirements.

Compiler's Comments

1999 Amendment: Chapter 267 inserted (2) concerning disclosure of information required by national association; in (3) at beginning deleted "In the absence of malice", near middle substituted "is not liable for any civil claim, including counterclaims, third-party claims, or cross-claims, related to" for "may not be subjected to civil liability", and at end inserted final clause relating to clear and convincing evidence; inserted (3)(a) concerning knowing false statement; inserted (3)(b) concerning reckless disregard concerning statement; and made minor changes in style. Amendment effective October 1, 1999.

30-10-315. Requirements for securities fraud actions — definition.

Compiler's Comments

Severability: Section 11, Ch. 468, L. 1997, was a severability clause.

Effective Date: Section 12, Ch. 468, L. 1997, provided: "[This act] is effective on passage and approval." Approved May 1, 1997.

30-10-316. Sanctions.

Compiler's Comments

Severability: Section 11, Ch. 468, L. 1997, was a severability clause.

Effective Date: Section 12, Ch. 468, L. 1997, provided: "[This act] is effective on passage and approval." Approved May 1, 1997.

30-10-317. Defendant's right to written interrogatories.

Compiler's Comments

Severability: Section 11, Ch. 468, L. 1997, was a severability clause.

Effective Date: Section 12, Ch. 468, L. 1997, provided: "[This act] is effective on passage and approval." Approved May 1, 1997.

30-10-318. Limitation on damages.

Compiler's Comments

Severability: Section 11, Ch. 468, L. 1997, was a severability clause.

Effective Date: Section 12, Ch. 468, L. 1997, provided: "[This act] is effective on passage and approval." Approved May 1, 1997.

30-10-319. Applicability of safe harbor for forward-looking statements.

Compiler's Comments

Severability: Section 11, Ch. 468, L. 1997, was a severability clause.

Effective Date: Section 12, Ch. 468, L. 1997, provided: "[This act] is effective on passage and approval." Approved May 1, 1997.

30-10-320. Prohibition of referral fees.

Compiler's Comments

Severability: Section 11, Ch. 468, L. 1997, was a severability clause.

Effective Date: Section 12, Ch. 468, L. 1997, provided: "[This act] is effective on passage and approval." Approved May 1, 1997.

30-10-321. Prosecution of persons aiding violations.

Compiler's Comments

Severability: Section 11, Ch. 468, L. 1997, was a severability clause.

Effective Date: Section 12, Ch. 468, L. 1997, provided: "[This act] is effective on passage and approval." Approved May 1, 1997.

30-10-322. Loss causation.

Compiler's Comments

Severability: Section 11, Ch. 468, L. 1997, was a severability clause.

Effective Date: Section 12, Ch. 468, L. 1997, provided: "[This act] is effective on passage and approval." Approved May 1, 1997.

30-10-323. Construction.

Compiler's Comments

Severability: Section 11, Ch. 468, L. 1997, was a severability clause.

Effective Date: Section 12, Ch. 468, L. 1997, provided: "[This act] is effective on passage and approval." Approved May 1, 1997.

30-10-324. Definitions.

Compiler's Comments

2019 Amendment: Chapter 104 in (1)(a) after "thing of value" inserted "or purported value"; in (7)(b) near middle substituted "anything of value, including anything of purported value" for "money"; and in (8)(b) substituted "multilevel marketing company" for "multilevel distribution company". Amendment effective April 1, 2019.

Preamble: The preamble attached to Ch. 104, L. 2019, provided: "WHEREAS, in Redding v. McCarter, 2012 MT 144, 365 Mont. 316, the Montana Supreme Court stated that the Securities Act of Montana was drafted broadly to be in harmony with federal securities law, which recognizes the virtually limitless scope of human ingenuity, especially in the creation of the countless and variable schemes devised by those who seek the use of money of others on the promise of profits; and

WHEREAS, recent enforcement actions by the Montana State Auditor have encountered securities schemes promising investors with profits through payment of items of no value but of purported value.

THEREFORE, this act seeks to definitively clarify that the Montana Securities Act applies to the virtually limitless scope of securities schemes, including those not involving strictly the payment of money."

Saving Clause: Section 3, Ch. 104, L. 2019, was a saving clause.

Severability: Section 4, Ch. 104, L. 2019, was a severability clause.

2015 Amendment: Chapter 318 at beginning before "30-10-301" deleted "30-10-216" and after "30-10-325" inserted "and 30-10-327"; substituted "multilevel marketing company" for "multilevel distribution company" as defined term and in definition inserted (a)(ii) concerning formula, in (b) substituted "permits participants to" for "may", and in (c) substituted "provides for" for "is eligible for"; in definition of pyramid promotional scheme in (c)(i) after "consumed by the participant" inserted "or other participants" and at end after "operation" deleted "and that provides compensation to the participant based upon the sale of goods or services by persons whose participation in the sales plan or operation has been obtained by the participant" and deleted former (c)(iii) that read: "(iii) is authorized to use a federally registered trademark or servicemark that identifies the company promoting the sales plan or operation, the goods or services sold, or the sales plan or operation"; and made minor changes in style. Amendment effective October 1, 2015.

Saving Clause: Section 7, Ch. 318, L. 2015, was a saving clause.

2013 Amendment: Chapter 286 near beginning substituted "30-10-216, 30-10-301, 30-10-324, and 30-10-325" for "30-10-324 through 30-10-326"; inserted definition of direct selling association; in definition of multilevel distribution company deleted former (b) that read: "(b) The term does not include an insurance producer, real estate broker, or salesperson or an investment adviser, investment adviser representative, broker-dealer, or salesperson, as defined in 30-10-103, operating in compliance with this chapter"; in (7)(c)(iv)(C) substituted "items given to the person to assist in marketing goods or services under the plan" for "required items"; inserted definition of transacting business; and made minor changes in style. Amendment effective April 24, 2013.

2009 Amendment: Chapter 2 in definition of pyramid promotional scheme in (c)(i) near beginning and in (c)(v)(B) in second sentence after "subsection" substituted "(6)(c)(v)" for "(6)(b)(v)"; and made minor changes in style. Amendment effective October 1, 2009.

2003 Amendment: Chapter 446 in definition of pyramid promotional scheme inserted (b) providing that pyramid promotional scheme includes Ponzi scheme; and made minor changes in style. Amendment effective October 1, 2003.

2001 Amendment: Chapter 322 in definition of pyramid promotional scheme deleted former (b)(i) that read: "(i) does not compensate a participant solely for obtaining the participation of other persons in the sales plan or operation" and near middle of (b)(i) inserted "and not primarily for obtaining the participation of other persons in the sales plan or operation"; and made minor changes in style. Amendment effective October 1, 2001.

Effective Date: This section is effective October 1, 1999.

Case Notes

Other Charges Not Included Within or Specific Instances of Fraudulent Practices Charge — No Violation of Prohibition on Multiple Charges: In District Court, the defendant was convicted of six felonies related to his operation of a Ponzi scheme. On appeal to the Supreme Court, he argued that fraudulent practices (common scheme), as set forth in 30-10-301(1), subsumed the remaining five counts as lesser included offenses. The Supreme Court found that operating a Ponzi scheme as set forth under 30-10-324 and 30-10-325 requires proof that the operator has made payments to earlier investors using funds obtained from later investors, which is not an element of the offense of fraudulent practices. The Supreme Court affirmed the defendant's convictions on this count. St. v. Brandt, 2020 MT 79, 399 Mont. 415, 460 P.3d 427.

30-10-325. Operating pyramid promotional scheme unlawful.

Compiler's Comments

2003 Amendment: Chapter 446 in (2) near beginning after "who" inserted "willfully", after "shall" inserted "for each participant giving consideration", and increased fine from $10,000 to $100,000; and inserted (3) imposing civil penalty of up to $10,000 against person conducting or promoting pyramid promotional scheme. Amendment effective October 1, 2003.

Effective Date: This section is effective October 1, 1999.

Case Notes

Other Charges Not Included Within or Specific Instances of Fraudulent Practices Charge — No Violation of Prohibition on Multiple Charges: In District Court, the defendant was convicted of six felonies related to his operation of a Ponzi scheme. On appeal to the Supreme Court, he argued that fraudulent practices (common scheme), as set forth in 30-10-301(1), subsumed the remaining five counts as lesser included offenses. The Supreme Court found that operating a Ponzi scheme as set forth under 30-10-324 and 30-10-325 requires proof that the operator has made payments to earlier investors using funds obtained from later investors, which is not an element of the offense of fraudulent practices. The Supreme Court affirmed the defendant's convictions on this count. St. v. Brandt, 2020 MT 79, 399 Mont. 415, 460 P.3d 427.

30-10-327. Multilevel marketing company — notice of activity — consent to service.

Compiler's Comments

Effective Date: This section is effective October 1, 2015.

Saving Clause: Section 7, Ch. 318, L. 2015, was a saving clause.

30-10-340. Governmental disclosure — immunity.

Compiler's Comments

Effective Date: Section 8, Ch. 84, L. 2017, provided: "[This act] is effective on passage and approval." Approved March 22, 2017.

30-10-341. Third-party disclosure — immunity.

Compiler's Comments

2023 Amendment: See 2023 Session Law for amendment made by sec. 2, Ch. 157, L. 2023. Amendment effective April 19, 2023.

Effective Date: Section 8, Ch. 84, L. 2017, provided: "[This act] is effective on passage and approval." Approved March 22, 2017.

30-10-342. Delaying disbursements — immunity.

Compiler's Comments

Effective Date: Section 8, Ch. 84, L. 2017, provided: "[This act] is effective on passage and approval." Approved March 22, 2017.

Part 9
Montana Living Trust Act

Part Compiler's Comments

Termination: Section 18, Ch. 348, L. 1997, provided: "[This act] terminates October 1, 1999."

Part Administrative Rules

Title 6, chapter 12, ARM Securities Department — living trusts.

30-10-901. Short title.

Compiler's Comments

Termination Provision Repealed: Section 1, Ch. 149, L. 1999, repealed sec. 18, Ch. 348, L. 1997, which terminated this section October 1, 1999.

Administrative Rules

ARM 6.12.1201 Applicability of subchapter.
ARM 6.12.1202 Definitions.

30-10-902. Purpose.

Compiler's Comments

Termination Provision Repealed: Section 1, Ch. 149, L. 1999, repealed sec. 18, Ch. 348, L. 1997, which terminated this section October 1, 1999.

Administrative Rules

ARM 6.12.1201 Applicability of subchapter.
ARM 6.12.1202 Definitions.

30-10-903. Definitions.

Compiler's Comments

Termination Provision Repealed: Section 1, Ch. 149, L. 1999, repealed sec. 18, Ch. 348, L. 1997, which terminated this section October 1, 1999.

Administrative Rules

ARM 6.12.1201 Applicability of subchapter.
ARM 6.12.1202 Definitions

30-10-904. Licensure — exemption.

Compiler's Comments

Termination Provision Repealed: Section 1, Ch. 149, L. 1999, repealed sec. 18, Ch. 348, L. 1997, which terminated this section October 1, 1999.

Administrative Rules

ARM 6.12.1201 Applicability of subchapter.
ARM 6.12.1202 Definitions.
ARM 6.12.1203 Licensure.

30-10-905. Administration.

Compiler's Comments

Termination Provision Repealed: Section 1, Ch. 149, L. 1999, repealed sec. 18, Ch. 348, L. 1997, which terminated this section October 1, 1999.

1997 Statement of Intent: The statement of intent attached to Ch. 348, L. 1997, provided: "A statement of intent is required for this bill because [section 5] [30-10-905] requires the state auditor to adopt forms and rules to implement [sections 1 through 15] [Title 30, ch. 10, part 9]. A form or rule may not be adopted unless there is a determination that it is in the public interest or necessary and appropriate for the protection of consumers and consistent with the purpose of [sections 1 through 15] [Title 30, ch. 10, part 9]."

Administrative Rules

ARM 6.12.1201 Applicability of subchapter.
ARM 6.12.1202 Definitions.
ARM 6.12.1204 Living trust representative books and records.

30-10-906. Scope.

Compiler's Comments

Termination Provision Repealed: Section 1, Ch. 149, L. 1999, repealed sec. 18, Ch. 348, L. 1997, which terminated this section October 1, 1999.

Administrative Rules

ARM 6.12.1201 Applicability of subchapter.
ARM 6.12.1202 Definitions.
ARM 6.12.1206 Internet.

30-10-907. Fines and fees — deposit to general fund.

Compiler's Comments

Termination Provision Repealed: Section 1, Ch. 149, L. 1999, repealed sec. 18, Ch. 348, L. 1997, which terminated this section October 1, 1999.

Administrative Rules

ARM 6.12.1201 Applicability of subchapter.
ARM 6.12.1202 Definitions.

30-10-908. Consent to service of process — manner of service.

Compiler's Comments

Termination Provision Repealed: Section 1, Ch. 149, L. 1999, repealed sec. 18, Ch. 348, L. 1997, which terminated this section October 1, 1999.

Administrative Rules

ARM 6.12.1201 Applicability of subchapter.
ARM 6.12.1202 Definitions.

30-10-909. Fraudulent and other prohibited practices.

Compiler's Comments

2005 Amendment: Chapter 513 deleted former (2) that read: "(2) It is unlawful for a person to sell a living trust to a person for whom a living trust is not suitable"; and made minor changes in style. Amendment effective April 28, 2005.

Termination Provision Repealed: Section 1, Ch. 149, L. 1999, repealed sec. 18, Ch. 348, L. 1997, which terminated this section October 1, 1999.

Administrative Rules

ARM 6.12.1201 Applicability of subchapter.
ARM 6.12.1202 Definitions.
ARM 6.12.1205 Sales and promotional material.

30-10-910. Misleading filings.

Compiler's Comments

Termination Provision Repealed: Section 1, Ch. 149, L. 1999, repealed sec. 18, Ch. 348, L. 1997, which terminated this section October 1, 1999.

Administrative Rules

ARM 6.12.1201 Applicability of subchapter.
ARM 6.12.1202 Definitions.

30-10-911. Unlawful representation concerning approval of application.

Compiler's Comments

Termination Provision Repealed: Section 1, Ch. 149, L. 1999, repealed sec. 18, Ch. 348, L. 1997, which terminated this section October 1, 1999.

Administrative Rules

ARM 6.12.1201 Applicability of subchapter.
ARM 6.12.1202 Definitions.

30-10-912. Investigations and subpoenas.

Compiler's Comments

Termination Provision Repealed: Section 1, Ch. 149, L. 1999, repealed sec. 18, Ch. 348, L. 1997, which terminated this section October 1, 1999.

Administrative Rules

ARM 6.12.1201 Applicability of subchapter.
ARM 6.12.1202 Definitions.

30-10-913. Injunctions and other remedies — limitations on actions — criminal sanctions.

Compiler's Comments

Termination Provision Repealed: Section 1, Ch. 149, L. 1999, repealed sec. 18, Ch. 348, L. 1997, which terminated this section October 1, 1999.

Administrative Rules

ARM 6.12.1201 Applicability of subchapter.
ARM 6.12.1202 Definitions.
ARM 6.12.1205 Sales and promotional material.

30-10-914. Judicial review of orders.

Compiler's Comments

Termination Provision Repealed: Section 1, Ch. 149, L. 1999, repealed sec. 18, Ch. 348, L. 1997, which terminated this section October 1, 1999.

Administrative Rules

ARM 6.12.1201 Applicability of subchapter.
ARM 6.12.1202 Definitions.

30-10-915. Civil liabilities — limitations on actions.

Compiler's Comments

Termination Provision Repealed: Section 1, Ch. 149, L. 1999, repealed sec. 18, Ch. 348, L. 1997, which terminated this section October 1, 1999.

Administrative Rules

ARM 6.12.1201 Applicability of subchapter.
ARM 6.12.1202 Definitions.

Part 10
Securities Restitution Assistance Fund

Part Compiler's Comments

Extension of Termination Date: Sections 3 and 4, Ch. 404, L. 2021, amended sec. 16, Ch. 58, L. 2011, and sec. 55, Ch. 151, L. 2017, by extending the termination date imposed by those sections to June 30, 2027. Effective May 7, 2021.

Extension of Termination Date: Section 55, Ch. 151, L. 2017, amended sec. 16, Ch. 58, L. 2011, by extending the termination date imposed by Ch. 58 to June 30, 2021. Effective April 4, 2017.

Severability: Section 13, Ch. 58, L. 2011, was a severability clause.

Effective Date: Section 14, Ch. 58, L. 2011, provided that this part is effective on passage and approval. Approved March 25, 2011.

Applicability: Section 15, Ch. 58, L. 2011, provided: "[This act] applies to final orders issued on or after [the effective date of this act]."

Termination: Section 16, Ch. 58, L. 2011, provided that this part terminates June 30, 2017.

30-10-1003. Definitions.

Compiler's Comments

2017 Amendment: Chapter 84 in definition of vulnerable person inserted (d) referring to person with mental disorder and providing definition of mental disorder; and made minor changes in style. Amendment effective March 22, 2017.

2015 Amendment: Chapter 28 inserted definition of vulnerable person. Amendment effective February 18, 2015.

Saving Clause: Section 6, Ch. 28, L. 2015, was a saving clause.

Severability: Section 7, Ch. 28, L. 2015, was a severability clause.

30-10-1004. Creation of securities restitution assistance fund.

Compiler's Comments

2023 Amendment: See 2023 Session Law for amendment made by sec. 3, Ch. 157, L. 2023. Amendment effective April 19, 2023.

2013 Amendments — Composite Section: Chapter 66 inserted (2)(a)(iii) concerning renewal or notice filing fees and collected examination costs; and made minor changes in style. Amendment effective March 7, 2013.

Chapter 286 in (2)(a)(i) substituted "violated any provision of parts 1 through 3 of this chapter" for "committed securities violations". Amendment effective April 24, 2013.

Severability: Section 4, Ch. 66, L. 2013, was a severability clause.

30-10-1006. Application for restitution assistance — maximum amount of restitution assistance award.

Compiler's Comments

2015 Amendment: Chapter 28 in (3) inserted exception clause; inserted (4) concerning vulnerable persons; and made minor changes in style. Amendment effective February 18, 2015.

Saving Clause: Section 6, Ch. 28, L. 2015, was a saving clause.

Severability: Section 7, Ch. 28, L. 2015, was a severability clause.

Administrative Rules

ARM 6.10.701 Securities restitution fund.
ARM 6.10.707 Application review requirements.

30-10-1008. Rulemaking authority.

Administrative Rules

ARM 6.10.702 Definitions.
ARM 6.10.703 Method for calculating percentages as the fund approaches zero.
ARM 6.10.705 Composition of committee.
ARM 6.10.706 Committee procedures.

Part 11
Whistleblower Award and Protection Act

Part Official Comments

The official comments for the Model Whistleblower Award and Protection Act are available at https://nasaa.org.

Part Compiler's Comments

Effective Date: Section 14, Ch. 76, L. 2021, provided: "[This act] is effective on passage and approval." Approved March 24, 2021.

Applicability: Section 15, Ch. 76, L. 2021, provided: "[This act] applies to original information provided by a whistleblower on or after October 1, 2021."

Severability: Section 13, Ch. 76, L. 2021, was a severability clause.

30-10-1103. Definitions.

Compiler's Comments

2023 Amendment: See 2023 Session Law for amendment made by sec. 7, Ch. 166, L. 2023. Amendment effective October 1, 2023.

CHAPTER 11
SALES

Chapter Case Notes

Sale With Option to Repurchase Not Considered Loan — Factors Not Met: Dillree initially requested a loan from Devoe, but Devoe stated he did not make loans and the request was denied. Dillree then suggested he could sell Devoe certain property with an option to repurchase within 6 months. Two such transactions occurred, but the obligations were not timely repaid and Devoe demanded surrender of the property. District Court awarded the property to Devoe, but on appeal Dillree contended the transactions were not sales, pointing out the four factors listed in Murray v. Butte-Monitor Tunnel Mining Co., 41 M 449, 110 P 497 (1910), which tend to confirm that a transaction is a security arrangement or mortgage and not a sale. The factors are: (1) the transaction in its inception had for its purpose a loan, not a sale; (2) the grantor was in financial distress at the time of the transaction; (3) the price appears to have been grossly inadequate; and (4) according to the grantee's own theory, the transaction did not amount to an absolute sale but to a conditional sale. The Supreme Court affirmed the trial court's findings that factors (1) and (3) were not present and that therefore the transactions could not be considered loans but were contracts for sale of property with the opportunity for repurchase. Dillree v. Devoe, 223 M 47, 724 P2d 171, 43 St. Rep. 1521 (1986). See also Campbell v. Campbell, 223 M 124, 725 P2d 207, 43 St. Rep. 1584 (1986).

Bank's Fiduciary Duty to Customers It Gives Financial Advice — Real Estate Sales: Wife, whose husband had recently died, signed a contract for a deed to her ranch with Dittman, who signed as "trustee". There were two other purchasers, who did not sign: a person to whom, according to the evidence, wife would not have knowingly sold and the marketing officer of the bank used by the wife and husband for some 24 years. Wife was unfamiliar with real estate and financial affairs and relied upon the advice of various bank officers with regard to the sale of the ranch. This put the bank in a prima facie fiduciary relationship as to the wife. The relationship and its attendant duties extended to the advising officers in their dealings with the wife in regard to sale of the ranch. The marketing officer thus had a duty to fully inform the wife and protect her interests. This duty he breached, and the breach amounted to constructive fraud, where evidence showed that: (1) the contract price and terms were disadvantageous to the wife; (2) the true purchasers were not disclosed to her either by the contract or the marketing officer; (3) the purchasers intended to and began to subdivide and sell the ranch, though the marketing officer knew wife apparently did not wish this, having refused an earlier offer to purchase with right to subdivide; (4) the marketing officer had extensive financial interests involving loans to him from his bank, and an audit of the bank recommended that in view of this his lending authority should be eliminated or curtailed; and (5) the lower court was unimpressed with the way in which wife's attorney in the negotiations represented her interests. The lower court properly ordered the contract for deed rescinded. Deist v. Wachholz, 208 M 207, 678 P2d 188, 41 St. Rep. 286 (1984).

Part 1
Sales and Exchanges

30-11-101. Sale defined.

Case Notes

Transfer of Title in Lieu of Foreclosure Not Sale: Where a party to an exclusive realtor's listing contract transferred title back to sellers in lieu of foreclosure, giving up the entire interest in the property and forfeiting all payments made to sellers, such transfer of title did not constitute a sale pursuant to this section. Ellingson Agency, Inc. v. Baltrusch, 228 M 360, 742 P2d 1009, 44 St. Rep. 1598 (1987).

Date Contract Enforceable — Effect of Absence of Collateral Terms to Be Added: In an action by a real estate broker against a seller for a brokerage commission, it was argued that if the sale of the property was enforceable on January 31, 1978, the broker would be entitled to his commission. If the sale was not enforceable until August 18, 1978 (90 days after expiration of broker's contract), he would not be entitled to his commission. The buy-sell was executed on January 31, 1978, but two financial terms within the contract were left out. The terms left out involve the method of payment, a collateral issue to the contract. The contract for deed was valid and enforceable on January 31, 1978, and the broker is entitled to his commission. Nardi v. Smalley, 197 M 321, 643 P2d 228, 39 St. Rep. 606 (1982).

Agreement to Sell Distinguished:

A sale, as distinguished from an agreement to sell, is the actual transfer of title from the grantor to the grantee, an agreement to sell being a contract to be performed in the future which, if fulfilled, results in a sale. Franzke v. Fergus County, 76 M 150, 245 P 962 (1926).

Where property is sold under a contract providing that title shall remain in the seller until the purchase price is paid, the transaction is not a sale within this section. State ex rel. Malin-Yates Co. v. Justice of Peace Court, 51 M 133, 149 P 709 (1915).

30-11-104. Agreement to sell.

Case Notes

Passage of Title: A seller ordinarily may not sue for the purchase price of the property until title has passed to the buyer. The actual passing of a title, as between the parties to a contract of sale of personal property, depends upon the intention of the parties. DeMers v. O'Leary, 126 M 528, 254 P2d 1080 (1953).

Sale Distinguished:

A sale, as distinguished from an agreement to sell, is the actual transfer of title from the grantor to the grantee, an agreement to sell being a contract to be performed in the future which, if fulfilled, results in a sale. Franzke v. Fergus County, 76 M 150, 245 P 962 (1926).

Where personalty is sold under a contract providing that title remain in the seller until the purchase price is paid, the transaction is a mere executory agreement of sale, accompanied by the delivery of possession to the intending purchaser to be held by him pending payment of the purchase price, and title remains in the vendor until payment has been made. State ex rel. Malin-Yates Co. v. Justice of Peace Court, 51 M 133, 149 P 709 (1915).

30-11-105. Agreement to buy.

Case Notes

When Contract of Sale Not Mere Option: The vendee, in an action to recover the balance due on the purchase price, may not contend that the contract of purchase and sale was merely an option in the face of a provision that the vendor has agreed "and does hereby agree" to sell, and the vendee "agrees to purchase from the vendor" the property described, and that the consideration, naming it, shall be paid to the vendor "at the times and in the manner following". Petitt v. F. V. H. Collins Co., 112 M 12, 113 P2d 340 (1941).

30-11-106. Agreement to sell and buy.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Inability to Obtain Real Estate Financing — Return of Earnest Money Proper: Defendants secured prequalification on a real estate loan and, pursuant to the buy-sell agreement, paid $53,000 in earnest money to purchase a condominium from plaintiff. The buy-sell agreement required the defendants to obtain financing for the remaining $946,000 of the purchase price. However, the economic climate later changed and required the need for a larger down payment, which defendants did not have. Defendants notified plaintiff and requested the return of the earnest money, but plaintiff refused and filed a fraud action, contending that defendants falsely represented their borrowing status and failed to obtain the required financing. The District Court summarily dismissed the fraud claims because the purchase agreement provided that if conventional financing could not be obtained, the agreement was void. On appeal, plaintiff asserted that a genuine issue of material fact remained regarding the fraud claims, precluding summary judgment. The Supreme Court disagreed. It was undisputed that defendants applied for loans and were prequalified for financing, so defendants did not misrepresent their borrowing status. Summary dismissal of the fraud claims was appropriate as a matter of law, particularly because plaintiff had the opportunity to be heard on the issue. The District Court properly terminated the purchase agreement when defendants could not obtain financing, and plaintiff was correctly ordered to return the earnest money. Mill Creek Ltd. Partnership v. Lodge, 2010 MT 65, 355 Mont. 478, 228 P.3d 1144.

Sale Distinguished:

An agreement to sell is a contract to be performed in the future; it is preliminary to a sale and not a sale. Hence, where the owner of an oil and gas lease agreed to sell it on condition that upon default in making deferred payments the owner should have the right to take possession of the premises and default was made and the agreement canceled, a finding of the court in a mechanics' foreclosure suit that the defaulting purchaser was the owner of the leasehold was error. Callender v. Crossfield Oil Syndicate, 84 M 263, 275 P 273 (1929), overruled on other grounds in Pioneer Eng'r Works, Inc. v. McConnell, 113 M 392, 132 P2d 160 (1942).

A sale, as distinguished from an agreement to sell, is the actual transfer of title from the grantor to the grantee, an agreement to sell being a contract to be performed in the future which, if fulfilled, results in a sale. Franzke v. Fergus County, 76 M 150, 245 P 962 (1926).

An agreement to sell and buy is preliminary to a sale, resulting in a sale only if the terms thereof are fulfilled. Wright Land & Inv. Co. v. Even, 57 M 1, 186 P 681 (1919).

Option to Purchase: This section was not applicable to transaction based on instrument clearly granting to purchaser an option only, where purchaser did not obligate himself to accept title to property or to pay a price therefor. N. Min. Corp. v. Cooke Min. Co., 123 F2d 9 (1941).

30-11-109. When usual common-law covenants required by contracts.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

Case Notes

Covenant of Warranty: Where a deed to real property purports to convey the realty itself and not merely the grantor's right, title, and interest in it, the covenant of warranty that "the grantor hereby covenants that he will forever warrant and defend" the grantee's "right, title and interest in and to the said premises . . . against all and every person", etc., is one of general warranty and quiet enjoyment. Green v. Baker, 66 M 568, 214 P 88 (1923).

30-11-110. Form of covenants.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

No Award of Damages and Attorney Fees Unless Covenant of Warranty Breached: The Ecklunds sued the Stevensons, claiming that they owned part of the Stevensons' property. In defending the claim, the Stevensons also sued the Woods on the basis of a breach of the covenant of warranty in transferring the property to them. The lower court found that the Ecklunds had no claim to the property because the doctrine of apportionment had been properly applied to correct the 1910 plat. The Stevensons asserted that they were entitled to damages and attorney fees from the Woods because of having to defend against the Ecklunds' suit. The Supreme Court held that the Woods were not liable because the application of the doctrine of apportionment meant that the Ecklunds had no basis for a lawful claim to the property and that therefore no breach of the covenant of warranty had occurred. Stevenson v. Ecklund, 263 M 61, 865 P2d 296, 50 St. Rep. 1706 (1993).

30-11-111. Contract for sale of real property.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Sufficient Indica of Mutual Assent to Find Written Contract — Compensatory Damages — Constructive Fraud — Statute of Frauds — Statute of Limitations: The defendants sold a tract of land from their parents' estate despite the fact that the plaintiffs had an oral agreement with the parents for the purchase of a portion of the property. The District Court properly determined that the plaintiffs had an enforceable contract to buy the property under 70-20-102 and 30-11-111 based on (1) an unsigned land purchase agreement, (2) a land survey, (3) a check issued by one of the plaintiffs that was endorsed and deposited, and (4) a letter to a tax preparer referencing the check received as partial payment for the property at issue. Because the plaintiffs had an enforceable contract, the District Court properly determined that the plaintiffs suffered compensatory damages and that the personal representative's statements showed constructive fraud. The Supreme Court held that the District Court did not err in its conclusion that the limitations provided under 72-3-803 did not bar the plaintiffs' claim. Wood v. Anderson, 2017 MT 180, 388 Mont. 166, 399 P.3d 304.

Purchase of Property — Statute of Frauds — Claim Regarding Interest in Property Dismissed: Plaintiffs contended they had an oral agreement to lease and purchase real property from the defendants and demanded a portion of insurance proceeds paid to the defendants after a fire destroyed the real property at issue. The parties stipulated that there was no written contract between them to enter a lease for a period longer than 1 year or to purchase the property. Because the statute of frauds requires both leases for a period longer than 1 year and agreements to purchase the property to be in writing, the Supreme Court affirmed the District Court's grant of summary judgment in favor of the defendants. Hinebauch v. McRae, 2011 MT 270, 362 Mont. 358, 264 P.3d 1098.

No Evidence of Contract to Sell Real Property — Specific Performance Precluded: Zier and Lewis entered negotiations for Zier to buy Lewis's Montana ranch. Negotiations broke down after Zier's counteroffer was rejected. Nevertheless, Zier contended that Lewis had agreed to sell the property through Lewis's business manager, and that Zier was entitled to specific performance. The District Court concluded that no contract existed and granted summary judgment for Lewis. On appeal, the Supreme Court affirmed. A valid contract requires mutual consent of both parties, and the parties must agree on the same thing. Acceptance of an offer on terms varying from those offered is a rejection of the offer and puts an end to negotiations unless there is assent to the new terms. In this case there was no contract because there was no consent to the terms of a contract. Without a valid and binding contract, a party may not obtain specific performance. Therefore, the District Court did not err in granting summary judgment for Lewis. Zier v. Lewis, 2009 MT 266, 352 M 76, 218 P3d 465 (2009). See also Austin v. Cash, 274 M 54, 906 P2d 669 (1995).

Potential Access Rights Merged With Deeds and Extinguished — Applicability of Contract Law Doctrine of Merger: Prior to Gehring's consent to sell 360 acres to APS Corporation (APS) in 1970, they entered an agreement that included a provision on access rights, whereby

Gehring purported to grant future purchasers access to other land owned by Gehring for certain recreational purposes. After being told by the Gehring Ranch Corporation that they would not be allowed access to Gehring's land for recreation, the successors in interest to APS sought to enforce the agreement, alleging that they had been improperly excluded from the land and that the agreement created an easement over Gehring's land. The District Court granted summary judgment for the Gehring Ranch Corporation, noting that the agreement did not identify Gehring's other lands upon which an easement was purportedly created. The court also held that any agreement prior to execution of the deeds was merged with the deeds and that because the deeds transferring title did not provide for access, any access rights promised in the agreement were lost. The decision was appealed, and the Supreme Court affirmed. The clause in the agreement was part of a larger agreement to transfer property in the future, and Gehring did not intend to create an easement, but at most intended to provide for potential access privileges if certain conditions, such as creation of a property owners' association and adoption of rules governing the use of the recreational privileges, were met. The Supreme Court cited Urquhart v. Teller, 1998 MT 119, 288 M 497, 958 P2d 714 (1998), in applying the contract law doctrine of merger, holding that the deeds contained all the rights of the parties and that because no access privileges were mentioned in the deeds, any potential access rights referred to in the agreement merged with the deeds and were lost. Richman v. Gehring Ranch Corp., 2001 MT 293, 307 M 443, 37 P3d 732 (2001).

Contract Provisions Merged Into Deed — Covenants Not Intended to Be Collateral Extinguished by Unrestricted Deed: A contract for the sale of property can contain a valid covenant running with the land, but generally, all provisions in a sale contract are merged into the warranty deed, founding the purchaser's rights in the deed covenants rather than in the executed contract, unless the parties intend for an agreement in a contract for sale to be collateral. Covenants relating to title, quantity, and possession of land are generally not collateral and thus merge into the deed. In the present case, the parties intended for the contract for deed and attendant restrictions to merge into the warranty deed, so the general rule of merger applied. The District Court did not err in refusing to enforce the covenants contained in the contract for deed. Urquhart v. Teller, 1998 MT 119, 288 M 497, 958 P2d 714, 55 St. Rep. 461 (1998), followed in Richman v. Gehring Ranch Corp., 2001 MT 293, 307 M 443, 37 P3d 732 (2001), and Tungsten Holdings, Inc. v. Olson, 2002 MT 158, 310 M 374, 50 P3d 1086 (2002).

Possession of Real Property Insufficient to Grant Title Against Good Faith Purchasers — No Adverse Possession Shown: In 1989, the Luloffs bought part of a ranch from the Manweilers by a deed that excluded "Tract B". The Luloffs mistakenly assumed that Tract B was the part of the ranch that had been occupied by the Blackburns for approximately 4 years. When the Luloffs later discovered that Tract B was another part of the ranch, they brought an action to have the Blackburns evicted, and the District Court granted summary judgment. The Supreme Court held that summary judgment was correctly granted because there was no contract between the Manweilers and the Blackburns satisfying the statute of frauds for the sale of the property to the Blackburns. The Supreme Court held that the Blackburns' mere possession was insufficient against the Luloffs, who had purchased the ranch as bona fide purchasers in good faith, because they were without notice of any claim of title by the Blackburns. The Supreme Court noted that the Blackburns could not make a claim of title because they had mere possession, which did not satisfy the requirements for adverse possession because the Blackburns had not paid taxes upon the property. Luloff v. Blackburn, 274 M 64, 906 P2d 189, 52 St. Rep. 1124 (1995).

Failure of Counteroffer Under Statute of Frauds — Handwritten Additions by Sellers' Agent Not Subscribed by Sellers — Part Performance and Equitable Estoppel Inapplicable: After Austin rejected a counteroffer on property that he was interested in buying, the agent, Everett, went to the office of the listing agent, Young, who contacted one of the two owners of the property by telephone. That owner, Cash, said that she would consider sale of the property for an additional $5,000 but that she would first have to discuss it with her brother, the other owner. Everett then added a handwritten paragraph to the rejected counteroffer, noting the sale of all of the property for $115,000 and faxed it back to Austin. When Austin received the revised counteroffer, he believed that it had been signed by Cash and, believing that a binding contract had been made, lowered the sale price of other property that he owned in California. Cash and her brother subsequently received and accepted an offer for their property from a different buyer, whereupon the Austins filed a lis pendens against Cash's property, preventing its sale to the other buyer. The Supreme Court held that because neither the sellers nor their agents signed or initialed the handwritten addition to the counteroffer, the contract was not properly subscribed by the sellers or their agents and therefore did not satisfy the statute of frauds. The Supreme Court also held that the action of the Austins in reducing the sale price of their California properties was an act in contemplation of eventual performance of the contract and not an act of part performance itself. For this reason, part performance did not excuse the application of the statute of frauds. The Supreme Court also held that in order for a court to order specific performance of a contract, there had to be a binding contract in the first place and held that because the additional language to the sale contract had not been subscribed, no contract existed. Finally, the Supreme Court held that promissory estoppel is inapplicable when a contract is clearly within the statute of frauds. Austin v. Cash, 274 M 54, 906 P2d 669, 52 St. Rep. 1119 (1995).

Discussions Regarding Land Trade Insufficient to Create Contractual Obligation: Parties discussed a land exchange and worked together with a surveyor in placing stakes and laying out lines for the exchange. Weinberg contended that these actions constituted partial performance sufficient to trigger specific enforcement of the agreement. However, the discussions regarding the land trade were insufficient to create a contractual obligation. Absent a showing of consideration or evidence or indicia of what the parties agreed to and the terms of their agreement, an enforceable agreement did not exist. Quirin v. Weinberg, 252 M 386, 830 P2d 537, 49 St. Rep. 331 (1992), followed in Luloff v. Blackburn, 274 M 64, 906 P2d 189, 52 St. Rep. 1124 (1995).

Negative Easement Based on Oral Agreement — Statute of Frauds Inapplicable: Appellants claimed an oral agreement made in 1967 subjected land known as the Base Area Chalet to a negative easement that restricted the property to noncommercial activities. The Supreme Court found that a written 1971 agreement only contracted to convey property described as "sellers' land" which had been "subject to ski easement"; however, the chalet property was conveyed away by appellants in 1967 and had never been subject to the ski easement. Since the Base Area Chalet did not belong to "sellers" and was not subject to the easement in 1971, the 1971 agreement had no effect on the chalet property. For the same reason, the 1971 agreement could not satisfy the Statute of Frauds for any alleged oral agreement that would create a negative easement on the chalet property. Haggerty v. Gallatin County, 221 M 109, 717 P2d 550, 43 St. Rep. 674 (1986).

Contract to Make Will Denied — No Part Performance Exception: An oral agreement whereby respondents agreed to move to decedent's ranch and lease it from decedent for remainder of his lifetime and decedent agreed to give an undivided one-half interest in the ranch to them at his death and provide them with the right to buy the other one-half interest at the appraised value as of the date of his death was an oral agreement for disposition of decedent's property at death. The District Court committed error and contradicted its own findings of fact when it concluded that the oral agreement was for the leasing, sale, and purchase of real property. The agreement does not conform to a single particular of the requirements provided by statute for the enforcement of such an agreement. The language of 72-2-105 (renumbered 72-2-534) is unambiguous and does not provide for a part performance exception to the Statute of Frauds. Orlando v. Prewett, 218 M 5, 705 P2d 593, 42 St. Rep. 1328 (1985), followed, with regard to the holding that oral contracts to make a devise are barred, in In re Estate of Braaten, 2004 MT 213, 322 M 364, 96 P3d 1125 (2004). A mechanics' lien filed against real property that was the subject of the 1985 quiet title action against the same parties who filed the lien was held void under the doctrine of res judicata in Orlando v. Prewett, 236 M 478, 771 P2d 111, 46 St. Rep. 520 (1989).

Realtor Buying Property — Not Usual Course of Business: As part of a real estate transaction in which the buyers needed to sell a piece of property in order to purchase other property, the realtor acting on behalf of the buyers executed a memorandum stating that if the property was not sold by a set time, she would purchase the property at a stated price. The memorandum was not signed by the realtor's alleged partner. On appeal, he contended he could not be bound by the memorandum under the Statute of Frauds. The Supreme Court held that the realtor could not bind her ostensible partner since there was no written authority of agency and because the purchase of real estate was not the realtor's usual way of doing business. The alleged partner could not be bound to the contract evidenced by the memo absent his authorization thereunto in writing. McNabb v. Norine, 204 M 330, 664 P2d 927, 40 St. Rep. 878 (1983).

Equitable Principles — Estopped From Invalidating Agreement Under Statute of Frauds: Agreement between plaintiff and defendant to sell property was valid under the Statute of Frauds even though the written instrument was signed only by the plaintiff and defendant's wife when plaintiff had made an irretrievable change in position and defendant had secured an unconscionable advantage or inflicted an unjust or unconscionable loss upon the plaintiff. Bolz v. Myers, 200 M 286, 651 P2d 606, 39 St. Rep. 1747 (1982).

Performance of Oral Agreement by Party as Precluding Statute of Frauds Defense: The parties were married in 1973. They entered a prenuptial agreement providing that the real and personal property of each would remain separate. In 1974, defendant brought a quiet title action against his sisters. He executed a handwritten agreement with plaintiff that if she would finance the legal expenses of the action he would give her 10% of the land or the value thereof. He was successful, and the parties entered into an oral agreement containing the same provisions for appellate costs. The trial court found that defendant owed plaintiff 20% of the value of the land and that value be determined at the time he elected to pay and be based on 20% of the value of all the land. The defendant contended there was insufficient evidence to support the finding of the oral agreement for the additional 10% of the land. The weight of evidence and credibility of witnesses were for the District Court to determine. There is no preponderance of evidence contrary to the District Court's finding. Defendant contends the oral agreement is barred by the Statute of Frauds because it is an agreement for the sale of real property and could not be performed in a year. The District Court held and the Supreme Court affirmed that the Statute of Frauds does not bar the oral agreement because plaintiff fully performed her part of the bargain. Kartes v. Kartes, 195 M 383, 636 P2d 272, 38 St. Rep. 1941 (1981).

Specific Performance of Agreement to Sell Land — Part Performance: The Statute of Frauds does not abridge the power of any court to compel the specific performance of any agreement for the sale of real property in case of part performance thereof. Dyksterhouse v. Doornbos, 172 M 461, 564 P2d 1293 (1977).

Option Agreement: Evidence of payment of money pursuant to the purchase of real estate for the purpose of persuading seller to hold the deal open for a certain period of time and the subsequent actions of the seller in holding the property off the market were sufficient to establish a valid option agreement, as well as to show that the agreement had been fully performed. Lynch v. Shields, 165 M 396, 529 P2d 348 (1974).

Realtor Agency: Prospective buyer was entitled to return of earnest money where realtor was unable to produce any written documentation of his alleged agency to sell realty. Pack River Co. v. Young, 162 M 271, 511 P2d 12 (1973).

Memorandum Consisting of Several Writings: The note or memorandum necessary to meet the requirements of this section may consist of several writings, and it is sufficient if it contains all the essentials of the contract, although they are stated in general terms. Hughes v. Melby, 135 M 415, 340 P2d 511 (1959).

Rights-of-Way of Necessity: There can be implied grants or reservations of rights-of-way of necessity in Montana. Thisted v. Country Club Tower Corp., 146 M 87, 405 P2d 432 (1965), overruling Simonson v. McDonald, 131 M 494, 311 P2d 982 (1957).

Memorandum — Necessary Contents:

An endorsed bank check with additional words "payment land" written on it is insufficient to constitute the written "note or memorandum" required by the statutes for it does not contain all the essentials of the agreement. Lewis v. Peterson, 127 M 474, 267 P2d 127 (1954).

The memorandum must contain all the essentials of the contract, but if the material elements are stated in general terms all the details or particulars need not be stated. Johnson v. Elliot, 123 M 597, 218 P2d 703 (1950). See also McNabb v. Norine, 204 M 330, 664 P2d 927, 40 St. Rep. 878 (1983).

Oral Agreement Being Performed: Where two persons had entered into a joint adventure for the purchase of ranch lands, in suit by one party for dissolution of the partnership and an accounting, contention of defendant that purchase of certain additional land, if part of agreement to purchase for benefit of partnership, was void because not in writing was not a defense, because both parties had performed and were performing their part of oral agreement to buy ranch properties. Ivins v. Hardy, 123 M 513, 217 P2d 204 (1950).

Complaint — Allegation of Writing: Although a contract to be valid must be in writing, that fact is a matter of proof and need not be alleged in the pleading. Johnson v. Elliot, 123 M 597, 218 P2d 703 (1950).

"Party to Be Charged": The "party to be charged" means the party to be charged in the particular suit. Johnson v. Elliot, 123 M 597, 218 P2d 703 (1950).

Presumption of Written Contract: The law will presume that a contract was in writing in the absence of any statement to the contrary. Johnson v. Elliot, 123 M 597, 218 P2d 703 (1950).

Complaint — Essentials of Agreement: Where complaint showed on its face that memorandum of agreement did not contain all essentials of agreement and such essentials could not be ascertained without resort to oral evidence, demurrer to complaint was properly sustained. Dineen v. Sullivan, 123 M 195, 213 P2d 241 (1949).

Conveyance Rights in Public Lands Orally: A settler upon public lands of the United States may convey his right therein, with water rights appurtenant thereto, orally, with or without consideration, to one who thereupon takes immediate possession thereof. Geary v. Harper, 92 M 242, 12 P2d 276 (1932).

Operation of Statute in General:

A life estate in real property (or a joint tenancy with the right of survivorship) can only be created by deed or will, under the Statute of Frauds. Therefore, the contention of the grantee in a deed which reserved no such estate in the grantor that it was orally understood between the parties that the instrument should have that effect is not maintainable. Hayes v. Moffatt, 83 M 214, 271 P 433 (1928).

Where it appears, in an action of ejectment, that monuments on the boundary between adjoining properties are in place and have been identified by the witnesses for the plaintiff, thus making certain that which can be made certain, in conformity with 1-3-229, and showing that there was no dispute as to the true dividing line, no valid agreement between the parties establishing the dividing line could have been made without a complete observance of the Statute of Frauds, as expressed in this section. Myrick v. Peet, 56 M 13, 180 P 574 (1919).

Where plaintiff sought to recover money on a demand loan, defendant was properly allowed to introduce testimony tending to show that the money paid him by the former was not a loan, but a partial payment upon the purchase price of real property sold under an oral contract, even though such contract of purchase was invalid and therefore unenforceable under the Statute of Frauds. Perkins v. Allnut, 47 M 13, 130 P 1 (1913).

A contract between tenants in common for the erection of a house on the common property by one at his own expense and requiring him to make an equal division of the rents between them when the rents received equaled one-half the cost did not come within this section. Ayotte v. Nadeau, 32 M 498, 81 P 145 (1905).

An oral agreement by a purchaser at a judicial sale of a lode mining claim to take the deed in his own name and convey to another was void under this section. Largey v. Leggat, 30 M 148, 75 P 950 (1904).

Part Performance:

A parol agreement for the sale or exchange of real property may be specifically enforced in case of part performance, and where the vendee takes possession and makes valuable improvements, there is sufficient part performance to take the case out of the Statute of Frauds. Hogan v. Thrasher, 72 M 318, 233 P 607 (1925).

For possession by the vendee to constitute part performance of a parol agreement to sell or exchange land, such possession must be in pursuance of the agreement and not merely a continuance of a former possession; but where possession is followed by the making of valuable and permanent improvements it is referable to the new relation created by the contract rather than the old one. Hogan v. Thrasher, 72 M 318, 233 P 607 (1925).

Specific performance of an oral contract to sell real property could be granted where plaintiff had fully performed all the terms of the agreement to be performed by him, and defendant had put him in actual possession of the premises, upon which he had erected substantial improvements. Stevens v. Trafton, 36 M 520, 93 P 810 (1908).

Claim in Opposition to Written Title — Burden of Proof:

Where a party asserts a claim to realty in opposition to the written title, he has the burden of proof, and the evidence in support of it must be clear, full and satisfactory, nothing being left to conjecture or speculation. MacGinniss Realty Co. v. Hinderager, 63 M 172, 206 P 436 (1922).

Where it is sought to found a claim, as for a right-of-way, to a part of a ranch based upon oral negotiations, and the owner is dead, this section furnishes to the heirs their only defense. If there was, in fact, an agreement to convey the right-of-way, the owner's death would not necessarily defeat a right to specific performance, but to authorize this the terms of the contract must be definite and full and be made out by clear and unambiguous proof. Lewis v. Patton, 42 M 528, 113 P 745 (1911).

Statute of Frauds Must Be Pleaded: Where a defendant, in a suit for specific performance, admitted the making of the contract and relied on other defenses than the Statute of Frauds to defeat the action, he could not avail himself of this section without specially pleading it. Mitchell v. Henderson, 37 M 515, 97 P 942 (1908); Christiansen v. Aldrich, 30 M 446, 76 P 1007 (1904).

30-11-113. Sale equivalent to exchange.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-11-114. Warranty of money.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Part 2
Seller's Responsibilities

Part Case Notes

Modular Home — Governing Warranty Law: Sale of modular home manufactured at defendant's plant and delivered to plaintiffs' building site was governed by the U.C.C. warranty provisions and not the warranty provisions of this part, which are made inapplicable by 30-11-224. The fact that defendant had charge of the home until after it was affixed to plaintiffs' foundation and no longer had mobility did not affect the applicability of the U.C.C. warranty provisions, for the home was manufactured to plaintiffs' specifications, was thus identified to the contract under the U.C.C. at the time of the first step of its production, was movable at that time, and thus was "goods" the sale of which the U.C.C. applied. Little v. Grizzly Mfg., 195 M 419, 636 P2d 839, 38 St. Rep. 1994 (1981).

30-11-201. When seller must act as depositary.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-11-202. When seller may resell.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Operation and Effect: This section applies only where the possession of the property is retained throughout by the vendor. It had no application where possession was immediately delivered to the vendee. First Nat'l Bank v. Marlowe, 71 M 461, 230 P 374 (1924).

30-11-203. Delivery on demand.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Action to Compel Delivery: As a general rule, a proceeding to compel a corporation to deliver a certificate of stock or an action for damages for failure to make delivery cannot be maintained unless the corporation has refused delivery. Gallatin County Farmers' Alliance v. Flannery, 59 M 534, 197 P 996 (1921).

30-11-204. Delivery — where made.

Case Notes

Operation and Effect: Where an automobile dealer has no ostensible place of business other than the garage in which his machines are kept and he sells and transfers the possession of a machine at such garage, that place, in the absence of any agreement to the contrary, becomes the place of business in contemplation of law, and a redelivery at the garage by the buyer, with notice to the seller that the machine is there, constitutes a restoration. Stanhope v. Shambow, 54 M 360, 170 P 752 (1918).

30-11-205. Expense of transportation.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-11-206. Notice of election as to delivery.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-11-207. Transportation.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-11-209. Warranty defined.

Case Notes

Final Written Agreement as Precluding Oral Warranty: Plaintiffs and defendant entered an agreement whereby defendant would lease condominiums from the plaintiffs and would sell plaintiffs her home. The lease of one of the condominiums contained an option for defendant to purchase the unit by forgiving plaintiffs their obligation under the promissory note on the home. Plaintiffs discovered that the floors in the home sloped north at a rate of 5 ½ inches over 30 feet. Plaintiffs sought to rescind the contract, and defendant sought specific performance. Plaintiffs contended that defendant stated that there were no problems whatsoever with the house and that this statement created an express warranty. Defendant denied making the statement. The contract between the parties contained a clause which stated that the written agreement constituted the entire agreement and superseded all prior written or oral representations or agreements. The written contract superseded and waived all oral representations so that no express warranty existed. Woodahl v. Matthews, 196 M 445, 639 P2d 1165, 39 St. Rep. 238 (1982).

Privity of Contract: Remote vendee, having no contractual relationship with defendant rubber boot manufacturer, did not state a claim for breach of warranty where there was no showing of privity of contract between the defendant and the remote vendee. Larson v. U.S. Rubber Co., 163 F. Supp. 327 (D.C. Mont. 1958).

Character of Contract: Where the character of a contract is at issue, to wit, whether it was one of sale, sale with warranty, or agency, the primary test is the intention of the parties gathered from the whole scope and effect of the language employed. Butte Floral Co. v. Reed, 65 M 138, 211 P 325 (1922).

Election of Remedies: On breach of warranty the buyer may either retain the article and sue for damages or rescind the contract and sue for a return of the purchase price paid. Butte Floral Co. v. Reed, 65 M 138, 211 P 325 (1922).

Secondhand Article: The fact that an article sold is secondhand and known to be such does not of itself prevent an affirmation as to its condition constituting an express warranty. Butte Floral Co. v. Reed, 65 M 138, 211 P 325 (1922).

30-11-210. No implied warranty in mere contract of sale.

Case Notes

Proof of Credit Purchase — Requisite Proof of Warranty Breach: In an action to collect the purchase price of tires purchased on credit, the defendant (buyer) filed a counterclaim for breach of warranty against the plaintiff. The defendant's counterclaim properly was denied because the defendant had failed to prove a prima facie case. Defendant appealed that there was no proof of some of the purchases. The Supreme Court said that an open account between the seller and buyer can be proved by evidence that the seller's records show that the goods were sold, that invoices had been sent to the buyer who failed to object to them, and that the seller's records are accurate. Here the buyer's rebuttal testimony was indefinite, and credibility was a trial court question. No breach of warranty was proven; only the testimony of the buyer was given and no solid evidence, such as any tires, records of the amount of use of the tires, or maintenance records, was produced. This, with findings of possible alternative causes of the problems with the tires, was a sufficient record to support the finding that breach of warranty was not proved by sufficient evidence. Defendant therefore was liable for the price of the tires. D&K Distrib. v. Ford, 189 M 505, 616 P2d 1097, 37 St. Rep. 1693 (1980).

Implied Warranty of Fitness for Use: While the general rule in most jurisdictions is that the seller of merchandise makes an implied warranty of its fitness for the use for which it is purchased, the rule in Montana is that there is no such warranty under this section, except where the seller is the manufacturer of something to be consumed as food and in cases where the buyer is not accorded an opportunity to examine the article bought (30-11-216 and 30-11-217). Under this rule seller of defective douche, not having manufactured the article and plaintiff and seller having had equal opportunity to discover alleged defects, there was no implied warranty. Harrington v. Montgomery Drug Co., 111 M 564, 111 P2d 808 (1941).

Burden of Proof: Where breach of warranty of a piece of machinery for a certain purpose is relied upon in an action to recover its purchase price, the burden of showing unfitness resting upon defendant is not sustained by evidence that upon a test it did poor work, unless it is also shown that the adjustment and operation were correct at the time of the test. Jones v. Armstrong, 50 M 168, 145 P 949 (1915).

Secondhand Article: One knowingly buying a secondhand article from a person not a dealer or manufacturer, relying upon his own judgment, takes it unaccompanied by an implied warranty as to its fitness for a special purpose. Jones v. Armstrong, 50 M 168, 145 P 949 (1915).

30-11-211. Warranty of title to personal property.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Possession of Property by Buyer: In this country it is the general rule that so long as the buyer of personal property is in the undisturbed possession of it he cannot recover damages for a breach of warranty of title or set up want of title in the seller as defense to an action to recover the purchase price. Courtney v. Gordon, 74 M 408, 241 P 233 (1925).

Guaranty To Deliver:

An endorsement on a bill of sale by the buyer of personal property on a resale thereof that he would "guarantee delivery of same" did not constitute a warranty of title. Pincus v. Muntzer, 34 M 498, 87 P 612 (1906).

Where the transfer of personal property was evidenced by a bill of sale to which the purchaser upon reselling the goods added an endorsement guaranteeing delivery, but not expressly warranting title, the language of this section may not be read into the endorsement and thereby a written warranty created so as to make the statutory limitation of 8 years mentioned in 27-2-202 applicable to a suit for a breach of a warranty of title to the property sold. Pincus v. Muntzer, 34 M 498, 87 P 612 (1906).

30-11-213. Warranty when seller knows that buyer relies on seller's statements.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Final Written Agreement as Precluding Oral Warranty: Plaintiffs and defendant entered an agreement whereby defendant would lease condominiums from the plaintiffs and would sell plaintiffs her home. The lease of one of the condominiums contained an option for defendant to purchase the unit by forgiving plaintiffs their obligation under the promissory note on the home. Plaintiffs discovered that the floors in the home sloped north at a rate of 5½ inches over 30 feet. Plaintiffs sought to rescind the contract, and defendant sought specific performance. Plaintiffs contended that defendant stated that there were no problems whatsoever with the house and that this statement created an express warranty. Defendant denied making the statement. The contract between the parties contained a clause which stated that the written agreement constituted the entire agreement and superseded all prior written or oral representations or agreements. The written contract superseded and waived all oral representations so that no express warranty existed. Woodahl v. Matthews, 196 M 445, 639 P2d 1165, 39 St. Rep. 238 (1982).

30-11-214. Warranty when merchandise not in existence.

Case Notes

Modular Home — Governing Warranty Law: Sale of modular home manufactured at defendant's plant and delivered to plaintiffs' building site was governed by the U.C.C. warranty provisions and not the warranty provisions of this part, which are made inapplicable by 30-11-224. The fact that defendant had charge of the home until after it was affixed to plaintiffs' foundation and no longer had mobility did not affect the applicability of the U.C.C. warranty provisions, for the home was manufactured to plaintiffs' specifications, was thus identified to the contract under the U.C.C. at the time of the first step of its production, was movable at that time, and thus was "goods" the sale of which the U.C.C. applied. Little v. Grizzly Mfg., 195 M 419, 636 P2d 839, 38 St. Rep. 1994 (1981).

30-11-215. Manufacturer's warranty against latent defects.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

No Causal Link Between Lack of Warning and Accidental Injury — Directed Verdict Proper: As set out in Brown v. N. Am. Mfg. Co., 176 M 98, 576 P2d 711 (1978), a showing of proximate cause is a necessary predicate to plaintiff's recovery in strict liability. In arguing the causation element, Riley contended that: (1) his testimony relating to his respect for machinery and concern for safety was sufficient evidence from which to infer that he would have ridden a motorcycle differently had a warning of the propensity to wobble been given; and (2) alternatively, he was entitled to a rebuttable presumption that he would have followed a warning had one been given. However, Riley's testimony on respect and concern was general rather than direct, unequivocal testimony that he would have altered his conduct had a warning been given, which is necessary to support a causal relationship. Although the Supreme Court has cited Comment j of Restatement (Second) of Torts 402A (1965) in recognizing the failure to warn claim itself, the specific language of the Comment that gives rise to the rebuttable presumption has not been adopted. Rather than adopt the Comment wholesale, the court, consistent with Brown and its successors, required a showing of a causal link between the lack of a warning and the accident and injuries in a failure to warn claim. Absent that showing, a directed verdict on the claim was proper. Riley v. Am. Honda Motor Co., Inc., 259 M 128, 856 P2d 196, 50 St. Rep. 714 (1993). In Patch v. Hillerich & Bradsby Co., 2011 MT 175, 361 Mont. 241, 257 P.3d 383, the Supreme Court concluded that Riley was not intended to limit the flexible standard of proof in product liability cases and that Riley is only one method for proving causation.

Factors to Be Considered in Alternative Design Products Liability Case: Recognizing that all factors may not be appropriate in every case and that additional factors should be considered where appropriate, the court found that the following factors should be considered in an alternative design product liability case:

"(1) A manufacturer who sells a product in a defective condition unreasonably dangerous because of a design defect is subject to liability for harm thereby caused to the ultimate user.

(2) A product may be in a defective condition unreasonably dangerous if the manufacturer should have used an alternative design.

(3) In determining whether an alternative design should have been used, the jury should balance so many of the following factors as it finds to be pertinent at the time of manufacture:

(a) The reasonable probability that the product as originally designed would cause serious harm to the claimant.

(b) Consideration of the reasonable probability of harm from the use of the original product as compared to the reasonable probability of harm from the use of the product with the alternative design.

(c) The technological feasibility of an alternative design that would have prevented claimant's harm.

(d) The relative costs both to the manufacturer and the consumer of producing, distributing and selling the original product as compared to the product with the alternative design.

(e) The time reasonably required to implement the alternative design." Rix v. Gen. Motors Corp., 222 M 318, 723 P2d 195, 43 St. Rep. 1296 (1986), followed in Krueger v. Gen. Motors Corp., 240 M 266, 783 P2d 1340, 46 St. Rep. 2114 (1989).

Manufacturing Defects Defined: In finding jury instructions to be adequate, the court held that the essential question was whether the product was flawed or defective because it was not constructed correctly by the manufacturer. The court quoted from Caprara v. Chrysler Corp., 436 N.Y.S.2d 251 (1981), saying: "Manufacturing defects, by definition, are "imperfections that inevitably occur in a typically small percentage of products of a given design as a result of the fallibility of the manufacturing process. A defectively manufactured product does not conform in some significant aspect to the intended design, nor does it conform to the great majority of products manufactured in accordance with that design." Stated differently, a defectively manufactured product is flawed because it is misconstructed without regard to whether the intended design of the manufacturer was safe or not. Such defects result from some mishap in the manufacturing process itself, improper workmanship, or because defective materials were used in construction." Rix v. Gen. Motors Corp., 222 M 318, 723 P2d 195, 43 St. Rep. 1296 (1986), followed in Krueger v. Gen. Motors Corp., 240 M 266, 783 P2d 1340, 46 St. Rep. 2114 (1989).

Design Defect Strict Liability — Change Subsequent to Manufacture: As set forth in Brown v. N. Am. Mfg. Co., 176 M 98, 576 P2d 711 (1978), the elements to prove a prima facie case in strict liability are: (1) the product was in a defective condition "unreasonably" dangerous to the user or consumer; (2) the defect caused the accident and injuries complained of; and (3) the defect is traceable to defendant. When the case involves a design defect, changes in the product through wear, tear, and abuse do not affect whether the original design was defective and unreasonably dangerous. If the product was not defective and unreasonably dangerous when it left the manufacturer's control and subsequent changes in the product that could not have been reasonably anticipated made the product dangerous, there is no liability. Kuiper v. Goodyear Tire & Rubber Co., 207 M 37, 673 P2d 1208, 40 St. Rep. 1861 (1983), followed in Rix v. Gen. Motors Corp., 222 M 318, 723 P2d 195, 43 St. Rep. 1296 (1986), and Baldauf v. Arrow Tank & Eng'r Co., Inc., 1999 MT 81, 294 M 107, 979 P2d 166, 56 St. Rep. 337 (1999). The Brown criteria were applied in Riley v. Am. Honda Motor Co., Inc., 259 M 128, 856 P2d 196, 50 St. Rep. 714 (1993), and Meyer v. Creative Nail Design, Inc., 1999 MT 74, 294 M 46, 975 P2d 1264, 56 St. Rep. 306 (1999).

Strict Liability — No "Open and Obvious Danger" Rule — Consideration as to Assumption of Risk: The Supreme Court reaffirmed its holding in Brown v. N. Am. Mfg. Co., 176 M 98, 576 P2d 711 (1978), that it was not error for the trial court to reject a proposed jury instruction on the "open and obvious danger" rule in strict liability. The court further held that the obvious character of the defect or danger is but a factor to be considered as to the assumption of risk in strict liability cases and must be judged by applying a subjective standard to plaintiff's conduct rather than the objective standard of a reasonable man. Kuiper v. Goodyear Tire & Rubber Co., 207 M 37, 673 P2d 1208, 40 St. Rep. 1861 (1983).

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Circumstantial Evidence of Manufacturing Defect: Plaintiff met the burden of proof for a strict liability action in proving, by circumstantial evidence, a defect rendering a product unreasonably dangerous. The Court rejected defendant's assertion of the "open and obvious danger" rule and the "patent-latent" distinction. Brown v. N. Am. Mfg. Co., 176 M 98, 576 P2d 711 (1978).

Privity of Contract: In action for breach of warranty no recovery may be had in the absence of privity of contract between the manufacturer and the person seeking to enforce the warranty. Larson v. U.S. Rubber Co., 163 F. Supp. 327 (D.C. Mont. 1958).

30-11-216. Warranty of fitness for particular purpose.

Case Notes

Negligence and Strict Liability Action for Damages by Pesticide Not Preempted by FIFRA — McAlpine Overruled: Plaintiffs brought an action for damages allegedly suffered when a pesticide was applied at the building where they worked. The District Court granted summary judgment for the pesticide manufacturer on the basis that the claims were preempted by the Federal

Insecticide, Fungicide, and Rodenticide Act (FIFRA) and McAlpine v. Rhone-Poulenc Ag Co., 285 M 224, 947 P2d 474 (1997), because all of the theories of liability were based on inclusions in or omissions from the pesticide labels. In particular, 7 U.S.C. 136v(b) provides that a state may not impose or continue in effect any requirement for labeling or packaging in addition to or different from those required under the federal law. On appeal, the Supreme Court overruled McAlpine and instead applied Medtronic, Inc. v. Lohr, 518 US 470 (1996), concluding that Congress, through FIFRA, intended only to preempt states from imposing positive law requirements in the form of regulations and laws and did not intend to extinguish damage remedies under state common law. The word "requirements" in section 136v(b) means enactments of positive law by legislative or administrative bodies, not state law damage actions. The case was reversed and remanded for further proceedings. Sleath v. West Mont Home Health Serv., Inc., 2000 MT 381, 304 M 1, 16 P3d 1042, 57 St. Rep. 1629 (2000).

Damage to Crops by Herbicide — Extent of Preemption by FIFRA — Claims for Breach of Express and Implied Warranty Not Preempted — Negligence and Strict Liability Preempted — Remedy for Prevention of Discovery by Summary Judgment: McAlpine applied Weedone LV6, a herbicide manufactured by Rhone-Poulenc and distributed by Ben Taylor, to crops of barley and spring wheat. After several weeks of cool morning temperatures, McAlpine noticed damage to his crops, which experts from Montana State University (now Montana State University-Bozeman) and the Montana Department of Agriculture said was caused by cool temperatures after application of the herbicide. The McAlpines brought a civil action against Rhone-Poulenc, claiming damages from negligence, breach of express and implied warranty, and strict liability. The District Court granted summary judgment for the defendants on the basis that the plaintiffs' claims were based on deficiencies in the label on Weedone LV6 and that those claims were preempted by the Federal Insecticide, Fungicide, and Rodenticide Act (FIFRA). Citing Wis. Pub. Intervenor v. Mortier, 501 US 597 (1991), and Cipollone v. Liggett Group, Inc., 505 US 504 (1992), the Supreme Court interpreted the FIFRA preemption statement, 7 U.S.C. 136v(b), to preempt only claims based upon negligence in labeling and not to preempt the appellants' claims based upon either express or implied warranty or strict liability. Therefore, the Supreme Court held that the appellants must be given the opportunity to prove that Rhone-Poulenc and Ben Taylor breached their warranty by designing, manufacturing, and marketing a product that was inherently defective and that the same defendants are strictly liable for designing, manufacturing, and marketing an unreasonably dangerous product. In response to Rhone-Poulenc's argument that the McAlpines failed to offer any evidence to defeat summary judgment, the Supreme Court pointed out that because the District Court granted summary judgment, the McAlpines were prevented from conducting complete discovery and that until discovery was completed, it was premature for the Supreme Court to conclude that the McAlpines' evidence was insufficient. McAlpine v. Rhone-Poulenc Ag Co., 285 M 224, 947 P2d 474, 54 St. Rep. 1123 (1997), overruled in Sleath v. West Mont Home Health Serv., Inc., 2000 MT 381, 304 M 1, 16 P3d 1042, 57 St. Rep. 1629 (2000), holding that state common-law negligence and strict liability claims based on or implicating pesticide labels are not preempted by FIFRA. Following the 1997 remand of McAlpine, the McAlpines settled with Ben Taylor, Inc., and proceeded to trial against Rhone-Poulenc on a theory of strict products liability, claiming that Weedone LV6 was a defective product because its propensity to damage or destroy crops in conjunction with cold weather was a danger outside the expectations of the ordinary consumer. Rhone-Poulenc acknowledged that the crop damage was caused by the phenoxy herbicide, but argued that the damage was not unreasonably dangerous and that liability exists only when a product is sufficiently dangerous. The trial court instructed the jury that it must find that the herbicide was in a "defective condition unreasonably dangerous", rather than merely in a defective condition, and the jury returned a verdict for Rhone-Poulenc. The McAlpines appealed. The Supreme Court previously held in McJunkin v. Kaufman, 229 M 432, 748 P2d 910 (1987), that a product is defective if it is unreasonably dangerous, but a plaintiff is not required to show that a product is defective and also that it is unreasonably dangerous, because establishing that a product is unreasonably dangerous is merely a means of proving that it is defective. Thus, the "defective condition unreasonably dangerous" language creates a vague and imprecise dual test and should not have been submitted to the jury because it was not plain, clear, and concise. The jury should have been required to find merely that the product was in a defective condition, so the case was again remanded. Further, the decision in Sleath, id., also applied on remand, so evidence of the product label was admissible in further proceedings. McAlpine v. Rhone-Poulenc Ag Co., 2000 MT 383, 304 M 31, 16 P3d 1054, 57 St. Rep. 1644 (2000).

Failure to Prove Unreasonably Dangerous Defective Condition — Proper Test of Defective Product: The Supreme Court adopted a modified approach to the test of strict liability as defined by sec. 402A, Restatement (Second) of Torts, in holding that while a product is defective if it is unreasonably dangerous, the lack of a dangerous aspect does not automatically preclude a finding that the product is defective. The proper test of a defective product is whether the product is unreasonably unsuitable for its intended or foreseeable purpose. McJunkin v. Kaufman, 229 M 432, 748 P2d 910, 44 St. Rep. 2111 (1987).

Modular Home — Governing Warranty Law: Sale of modular home manufactured at defendant's plant and delivered to plaintiffs' building site was governed by the U.C.C. warranty provisions and not the warranty provisions of this part, which are made inapplicable by 30-11-224. The fact that defendant had charge of the home until after it was affixed to plaintiffs' foundation and no longer had mobility did not affect the applicability of the U.C.C. warranty provisions, for the home was manufactured to plaintiffs' specifications, was thus identified to the contract under the U.C.C. at the time of the first step of its production, was movable at that time, and thus was "goods" the sale of which the U.C.C. applied. Little v. Grizzly Mfg., 195 M 419, 636 P2d 839, 38 St. Rep. 1994 (1981).

Application of Section: Where defendant did not have enough linseed pellets to fill plaintiff's order for sheep feed and suggested that plaintiff try another type of pellet which was a part of defendant's stock on hand, it was improper to instruct under this section since there was no evidence that such pellets were manufactured under the order for a specific purpose. Seaton Ranch Co. v. Mont. Vegetable Oil & Feed Co., 123 M 396, 217 P2d 549 (1950).

Rescission Unnecessary to Claim Breach of Implied Warranty: One who purchases articles for a particular purpose need not rescind the contract and restore them to the seller upon discovering a breach of the implied warranty, but may set up his claim for damages by way of counterclaim in an action by the plaintiff for the purchase price. Busbee v. Gagnon Co., 50 M 203, 146 P 275 (1915).

30-11-217. Warranty when thing cannot be examined by buyer.

Case Notes

Buyer Entitled to Damages for Shipment of Damaged Plants: Reed owned a greenhouse and ordered a shipment of poinsettias from McCalif for Christmas. When the plants arrived, many were damaged. Reed refused to pay $3,027.09 for the marketable plants that he kept and resold, contending that he had lost $8,683.95 on the damaged plants for which he had already received purchase orders from other buyers. The Supreme Court held that the record proved that there was no other source for replacement of the damaged plants and that McCalif was aware of that fact and the fact that Reed had entered into contracts for the resale of the plants. The Supreme Court ruled that Reed had the right to accept part of the plants received and reject the rest and that Reed was entitled to incidental and consequential damages because of McCalif's breach. The measure of damages was the difference between what Reed owed for the plants that he kept and what he lost on the orders that he could not fill. McCalif Grower Supplies, Inc. v. Reed, 272 M 254, 900 P2d 880, 52 St. Rep. 659 (1995).

Equal Opportunity to Discover Defect:

Retail seller of tubeless "recap" tire was not liable under this section for injuries sustained by automobile passenger in accident caused by "blow-out" since automobile owner had equal opportunity to inspect tire and discover any defects and did in fact inspect tire. Brock v. Rothwell, 154 M 144, 461 P2d 6 (1969).

In an action for personal injuries alleged to have been sustained by the use of a defective douche it was held, that the seller not having been the manufacturer of the article under 30-11-216, and the plaintiff having had an equal opportunity with the seller to discover its alleged defects, there was no implied warranty under this section. Harrington v. Montgomery Drug Co., 111 M 564, 111 P2d 808 (1941).

30-11-220. Warranty on sale of written instrument.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-11-221. Warranty on sale of goodwill.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Breach by Seller: When buyer of business broke contract by failing to make agreed payments for exclusive business rights in a territory and seller entered the territory after buyer's breach but in violation of the agreement, buyer was entitled to a setoff of the amount of profit which seller took from the restricted territory against seller's action for the full amount of the contract. Leiman-Scott, Inc. v. Holmes, 142 M 58, 381 P2d 489 (1963).

30-11-223. Effect of general warranty.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-11-224. Uniform Commercial Code overrides.

Case Notes

Modular Home — Governing Warranty Law: Sale of modular home manufactured at defendant's plant and delivered to plaintiffs' building site was governed by the U.C.C. warranty provisions and not the warranty provisions of this part, which are made inapplicable by this section. The fact that defendant had charge of the home until after it was affixed to plaintiffs' foundation and no longer had mobility did not affect the applicability of the U.C.C. warranty provisions, for the home was manufactured to plaintiffs' specifications, was thus identified to the contract under the U.C.C. at the time of the first step of its production, was movable at that time, and thus was "goods" the sale of which the U.C.C. applied. Little v. Grizzly Mfg., 195 M 419, 636 P2d 839, 38 St. Rep. 1994 (1981).

Part 3
Merchant's Rights

30-11-302. Obligation to keep merchandise in full view.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Part 5
Auction Sales and Auctioneers

30-11-502. Sale by auction.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-11-503. Sale under written conditions.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

30-11-504. Auctioneer's memorandum of sale.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-11-508. Auctioneer — authority and bond.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-11-510. Bond and sureties — approval — filing.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-11-511. Auctioneers ex officio.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-11-512. Assistant — who may act and when.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-11-513. Auctioneers to designate one place of business — partners.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-11-514. Penalty.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-11-515. Enforcement.

Compiler's Comments

2009 Amendment: Chapter 109 after "enforced by" deleted "the department of labor and industry and". Amendment effective October 1, 2009.

Saving Clause: Section 53, Ch. 109, L. 2009, was a saving clause.

Severability: Section 54, Ch. 109, L. 2009, was a severability clause.

2001 Amendment: Chapter 483 after "department of" substituted "labor and industry" for "commerce"; and made minor changes in style. Amendment effective July 1, 2001.

1981 Amendment: Substituted "department of commerce" for "department of business regulation".

Part 6
Factors

30-11-601. Factor defined.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Livestock Company: A livestock commission company employed by one to sell livestock for him is a factor within the meaning of this section and as such entitled to be reimbursed by its principal for advances and disbursements made in good faith in the course of its employment. Bowles Livestock Comm'n Co. v. Midland Nat'l Bank, 94 M 467, 23 P2d 967 (1933).

30-11-602. Obedience required from factor.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-11-603. Sales on credit.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-11-604. Liability of factor under guaranty commission.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-11-605. Principal's consent needed to relieve factor from liability.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-11-606. Authority of factor.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-11-607. Ostensible authority.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

Part 7
Canceled Dealership Contracts, Repurchase Requirements, and Dealer Data

Part Compiler's Comments

Saving Clause: Section 7, Ch. 297, L. 1985, was a saving clause.

Source: This part is based on Minnesota Statutes 1982, 325 E.06.

Severability: Section 8, Ch. 338, L. 1983, is a severability section.

30-11-701. Definitions.

Compiler's Comments

2019 Amendment: Chapter 283 inserted definition of cancellation or canceled; and made minor changes in style. Amendment effective May 3, 2019.

Preamble: The preamble attached to Ch. 283, L. 2019, provided: "WHEREAS, the Legislature finds that the distribution and sale of motor vehicles within this state vitally affect the general economy of the state, the public interest, and the public welfare; and

WHEREAS, in order to promote the public interest and the public welfare and in the exercise of the state's police power, it is necessary to regulate motor vehicle manufacturers, distributors, and factory or distributor representatives and to regulate dealers of motor vehicles doing business in this state in order to prevent frauds, impositions, and other abuses upon its citizens and to protect and preserve the investments and properties of the citizens of this state."

Severability: Section 19, Ch. 283, L. 2019, was a severability clause.

2009 Amendment: Chapter 168 in definition of inventory in (c) at beginning substituted "new motor vehicles, trucks, trailers, semitrailers, pole trailers, travel trailers" for "automobiles, trucks" and before "dealer" deleted "an automobile or truck"; and made minor changes in style. Amendment effective April 6, 2009.

Applicability: Section 3, Ch. 168, L. 2009, provided: "[This act] applies to dealership contracts entered into or renewed on or after [the effective date of this act]." Effective April 6, 2009.

2005 Amendment: Chapter 542 in definition of inventory in (c) at end substituted reference to 61-1-101 for reference to 61-1-314 and in (d) substituted reference to 61-1-101 for reference to Title 61, chapter 1, part 1. Amendment effective January 1, 2006.

1989 Amendment: In (4) added motorcycles, motor-driven cycles, recreational vehicles, quadricycles, snowmobiles, off-highway vehicles, vessels, detachable vessel motors or engines, and repair parts to definition of inventory; and made minor changes in form. Amendment effective March 7, 1989.

Saving Clause: Section 2, Ch. 51, L. 1989, was a saving clause.

1985 Amendment: At beginning of (1)(a) inserted "with respect to a dealership contract"; inserted definitions of current net price with respect to a distribution contract and a dealership contract; at beginning of (5)(a) inserted "with respect to a dealership contract"; and inserted definition of net cost with respect to a distribution contract and definition of wholesaler.

30-11-702. Repurchase of inventory items upon cancellation of dealership or distribution contract.

Compiler's Comments

2019 Amendment: Chapter 283 in (1) at beginning substituted "Upon cancellation of a written dealership contract between a retailer and a wholesaler, manufacturer, or distributor, the wholesaler, manufacturer, or distributor shall" for "If a retailer enters into a written dealership contract and either the wholesaler, manufacturer, distributor, or retailer cancels the contract, such wholesaler, manufacturer, or distributor shall"; in (1)(a) near beginning after "cost of all new" deleted "unused" and near middle inserted "including vehicles with less than 1,000 miles on the odometer"; in (2) at beginning substituted "Upon cancellation of a written distribution contract entered into between a wholesaler and a manufacturer or distributor" for "If a wholesaler enters into a written distribution contract and either the wholesaler, manufacturer, or distributor cancels the contract"; in (2)(a) near beginning after "cost of all new" deleted "unused" and at end inserted "including vehicles with less than 1,000 miles on the odometer"; in (3) at end of first sentence substituted "retailer's or wholesaler's repurchase request" for "return of the inventory items to the wholesaler, manufacturer, or distributor"; and inserted (4) regarding 30 days to complete an inventory, evaluation, and analysis. Amendment effective May 3, 2019.

Preamble: The preamble attached to Ch. 283, L. 2019, provided: "WHEREAS, the Legislature finds that the distribution and sale of motor vehicles within this state vitally affect the general economy of the state, the public interest, and the public welfare; and

WHEREAS, in order to promote the public interest and the public welfare and in the exercise of the state's police power, it is necessary to regulate motor vehicle manufacturers, distributors, and factory or distributor representatives and to regulate dealers of motor vehicles doing business in this state in order to prevent frauds, impositions, and other abuses upon its citizens and to protect and preserve the investments and properties of the citizens of this state."

Severability: Section 19, Ch. 283, L. 2019, was a severability clause.

1991 Amendment: In (1)(a), after "items", deleted "except repair parts" and after "cancellation" inserted "plus cost of freight to return the inventory"; in (1)(b) and (2)(b) increased percentage from 85% to 100% and after "catalog" inserted "or the last catalog or price list in which the repair part was listed as"; in (1)(b), after "cancellation", inserted "plus cost of freight to return the repair parts"; and in (3), before "return", substituted "within 60 days of the" for "upon". Amendment effective April 22, 1991.

Severability: Section 9, Ch. 522, L. 1991, was a severability clause.

1985 Amendment: Near beginning of (1) after "dealership contract", deleted "evidenced by franchise agreement, sales agreement, security agreement, or other similar agreement or arrangement"; inserted (2) stating manufacturer's and distributor's duties relating to inventory repurchase upon cancellation of distribution contract; and in first sentence of (3) substituted "retailer's or wholesaler's account" for "retailer's account" and substituted "subsection (1) or (2)" for "subsection (1)".

30-11-703. Excepted inventory.

Compiler's Comments

2019 Amendment: Chapter 283 in (7) after "essentially new" deleted "unused"; in (11) inserted second sentence regarding inventory acquired by trade between or among dealers in the ordinary course of business; and made minor changes in style. Amendment effective May 3, 2019.

Preamble: The preamble attached to Ch. 283, L. 2019, provided: "WHEREAS, the Legislature finds that the distribution and sale of motor vehicles within this state vitally affect the general economy of the state, the public interest, and the public welfare; and

WHEREAS, in order to promote the public interest and the public welfare and in the exercise of the state's police power, it is necessary to regulate motor vehicle manufacturers, distributors, and factory or distributor representatives and to regulate dealers of motor vehicles doing business in this state in order to prevent frauds, impositions, and other abuses upon its citizens and to protect and preserve the investments and properties of the citizens of this state."

Severability: Section 19, Ch. 283, L. 2019, was a severability clause.

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

30-11-704. Repurchase of inventory of deceased retailer or wholesaler.

Compiler's Comments

1985 Amendment: Near beginning of sentence substituted "retailer, wholesaler, or majority stockholder" for "retailer or majority stockholder" and after "operating as a retailer" inserted "or wholesaler".

30-11-705. Reimbursement for or repurchase of signs, special equipment, and special tools.

Compiler's Comments

2019 Amendment: Chapter 283 substituted current introductory clause for former introductory clause that read: "Upon the termination, cancellation, nonrenewal, or refusal to continue a dealership contract by a wholesaler, manufacturer, or distributor, the wholesaler, manufacturer, or distributor shall pay the retailer"; in (1) near middle substituted "acquired from any source, because the sign" for "if the acquisition of the sign"; in (2)(b) at beginning substituted "if a sign, item of special equipment, or special tool has" for "if the special equipment has", near middle substituted "if the sign, item of special equipment, or special tool is leased" for "the special tools are leased", and after "amounts" substituted "required to be paid upon termination of" for "that are required to terminate"; in (3) near beginning inserted "removing, repairing damage caused by removal"; and made minor changes in style. Amendment effective May 3, 2019.

Preamble: The preamble attached to Ch. 283, L. 2019, provided: "WHEREAS, the Legislature finds that the distribution and sale of motor vehicles within this state vitally affect the general economy of the state, the public interest, and the public welfare; and

WHEREAS, in order to promote the public interest and the public welfare and in the exercise of the state's police power, it is necessary to regulate motor vehicle manufacturers, distributors, and factory or distributor representatives and to regulate dealers of motor vehicles doing business in this state in order to prevent frauds, impositions, and other abuses upon its citizens and to protect and preserve the investments and properties of the citizens of this state."

Severability: Section 19, Ch. 283, L. 2019, was a severability clause.

Saving Clause: Section 4, Ch. 177, L. 2001, was a saving clause.

Effective Date: Section 5, Ch. 177, L. 2001, provided that this section is effective on passage and approval. Approved March 30, 2001.

30-11-711. Rights not affected.

Compiler's Comments

1985 Amendment: In (1) near middle of subsection, substituted "retailer's or wholesaler's account" for "retailer's account" and near end of subsection, substituted "retailer's or wholesaler's purchase" for "retailer's purchase"; and at end of (2) after "retailer", inserted "or wholesaler".

30-11-712. Civil liability.

Compiler's Comments

2019 Amendment: Chapter 283 in introductory clause in first sentence near middle inserted "or reimburse a wholesaler for" and "or a retailer for any inventory, signs, special equipment, or special tools" and at end deleted "100% of the current net price of the inventory, plus any freight charges paid by the retailer or wholesaler, the retailer's or wholesaler's attorney fees, and court costs"; inserted (1) regarding sums required under this part; inserted (2) regarding storage charges for warehouse storage plus inventory financing charges; inserted (3) regarding interest on sums due from the date of the request until paid; inserted (4) regarding attorney fees, court costs, and litigation expenses; and made minor changes in style. Amendment effective May 3, 2019.

Preamble: The preamble attached to Ch. 283, L. 2019, provided: "WHEREAS, the Legislature finds that the distribution and sale of motor vehicles within this state vitally affect the general economy of the state, the public interest, and the public welfare; and

WHEREAS, in order to promote the public interest and the public welfare and in the exercise of the state's police power, it is necessary to regulate motor vehicle manufacturers, distributors, and factory or distributor representatives and to regulate dealers of motor vehicles doing business in this state in order to prevent frauds, impositions, and other abuses upon its citizens and to protect and preserve the investments and properties of the citizens of this state."

Severability: Section 19, Ch. 283, L. 2019, was a severability clause.

1985 Amendment: After "freight charges paid by the retailer", inserted "or wholesaler" and substituted "retailer's or wholesaler's attorney fees" for "retailer's attorney fees".

30-11-713. Remedy as supplemental.

Compiler's Comments

2019 Amendment: Chapter 283 in (1)(a) at end inserted "signs, special equipment, or special tools"; and in (2) at end of first sentence and near middle of second sentence substituted "this part" for "30-11-702" and near middle of second sentence after "any inventory" substituted current text regarding parts, signs, special equipment, or special tools not included in contract remedies and one time limit on claim of loss or damage for "not covered by contract". Amendment effective May 3, 2019.

Preamble: The preamble attached to Ch. 283, L. 2019, provided: "WHEREAS, the Legislature finds that the distribution and sale of motor vehicles within this state vitally affect the general economy of the state, the public interest, and the public welfare; and

WHEREAS, in order to promote the public interest and the public welfare and in the exercise of the state's police power, it is necessary to regulate motor vehicle manufacturers, distributors, and factory or distributor representatives and to regulate dealers of motor vehicles doing business in this state in order to prevent frauds, impositions, and other abuses upon its citizens and to protect and preserve the investments and properties of the citizens of this state."

Severability: Section 19, Ch. 283, L. 2019, was a severability clause.

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

1985 Amendment: Inserted (1)(b) providing remedy supplemental to any agreement between the wholesaler and manufacturer or distributor; and in (2) in first sentence, substituted "retailer or wholesaler may elect" for "retailer may elect" and in second sentence, substituted "retailer's or wholesaler's right" for "retailer's right".

30-11-717. Definitions.

Compiler's Comments

2023 Amendment: See 2023 Session Law for amendment made by sec. 1, Ch. 362, L. 2023. Amendment effective May 2, 2023.

Applicability: Section 11, Ch. 362, L. 2023, provided: "(1) [This act] applies to all presently existing or hereafter established systems of distribution of motor vehicles in this state, including all existing agreements between a manufacturer, a factory branch, a distributor or a distributor branch, and a motor vehicle dealer, except to the extent that such application would impair valid contractual agreements in violation of the state or federal constitution.

(2) [This act] does not:

(a) govern, restrict, or apply to data that exists outside of a dealer data system, including data that is generated by a motor vehicle or devices that a consumer connects to a motor vehicle; or

(b) authorize a dealer or third party to use data that is obtained from a person in a manner that is inconsistent with either:

(i) an agreement with the person; or

(ii) the purposes for which the person provided the data to the dealer or third party."

Preamble: The preamble attached to Ch. 362, L. 2023, provided: "WHEREAS, the Legislature finds that the distribution and sale of motor vehicles within this state vitally affect the general economy of the state, the public interest, and the public welfare; and

WHEREAS, to promote the public interest and the public welfare and in the exercise of the state's police power, it is necessary to regulate motor vehicle manufacturers, distributors, and factory or distributor representatives and to regulate dealers of motor vehicles doing business in this state to prevent frauds, impositions, and other abuses upon its citizens and to protect and preserve the investments and properties of the citizens of this state."

Severability: Section 10, Ch. 362, L. 2023, was a severability clause.

Effective Date: Section 20, Ch. 283, L. 2019, provided: "[This act] is effective on passage and approval." Approved May 3, 2019.

Preamble: The preamble attached to Ch. 283, L. 2019, provided: "WHEREAS, the Legislature finds that the distribution and sale of motor vehicles within this state vitally affect the general economy of the state, the public interest, and the public welfare; and

WHEREAS, in order to promote the public interest and the public welfare and in the exercise of the state's police power, it is necessary to regulate motor vehicle manufacturers, distributors, and factory or distributor representatives and to regulate dealers of motor vehicles doing business in this state in order to prevent frauds, impositions, and other abuses upon its citizens and to protect and preserve the investments and properties of the citizens of this state."

Severability: Section 19, Ch. 283, L. 2019, was a severability clause.

30-11-718. Prohibited actions.

Compiler's Comments

2023 Amendment: See 2023 Session Law for amendment made by sec. 2, Ch. 362, L. 2023. Amendment effective May 2, 2023.

Applicability: Section 11, Ch. 362, L. 2023, provided: "(1) [This act] applies to all presently existing or hereafter established systems of distribution of motor vehicles in this state, including all existing agreements between a manufacturer, a factory branch, a distributor or a distributor branch, and a motor vehicle dealer, except to the extent that such application would impair valid contractual agreements in violation of the state or federal constitution.

(2) [This act] does not:

(a) govern, restrict, or apply to data that exists outside of a dealer data system, including data that is generated by a motor vehicle or devices that a consumer connects to a motor vehicle; or

(b) authorize a dealer or third party to use data that is obtained from a person in a manner that is inconsistent with either:

(i) an agreement with the person; or

(ii) the purposes for which the person provided the data to the dealer or third party."

Preamble: The preamble attached to Ch. 362, L. 2023, provided: "WHEREAS, the Legislature finds that the distribution and sale of motor vehicles within this state vitally affect the general economy of the state, the public interest, and the public welfare; and

WHEREAS, to promote the public interest and the public welfare and in the exercise of the state's police power, it is necessary to regulate motor vehicle manufacturers, distributors, and factory or distributor representatives and to regulate dealers of motor vehicles doing business in this state to prevent frauds, impositions, and other abuses upon its citizens and to protect and preserve the investments and properties of the citizens of this state."

Severability: Section 10, Ch. 362, L. 2023, was a severability clause.

Effective Date: Section 20, Ch. 283, L. 2019, provided: "[This act] is effective on passage and approval." Approved May 3, 2019.

Preamble: The preamble attached to Ch. 283, L. 2019, provided: "WHEREAS, the Legislature finds that the distribution and sale of motor vehicles within this state vitally affect the general economy of the state, the public interest, and the public welfare; and

WHEREAS, in order to promote the public interest and the public welfare and in the exercise of the state's police power, it is necessary to regulate motor vehicle manufacturers, distributors, and factory or distributor representatives and to regulate dealers of motor vehicles doing business in this state in order to prevent frauds, impositions, and other abuses upon its citizens and to protect and preserve the investments and properties of the citizens of this state."

Severability: Section 19, Ch. 283, L. 2019, was a severability clause.

30-11-719. Other responsibilities and restrictions.

Compiler's Comments

2023 Amendment: See 2023 Session Law for amendment made by sec. 3, Ch. 362, L. 2023. Amendment effective May 2, 2023.

Applicability: Section 11, Ch. 362, L. 2023, provided: "(1) [This act] applies to all presently existing or hereafter established systems of distribution of motor vehicles in this state, including all existing agreements between a manufacturer, a factory branch, a distributor or a distributor branch, and a motor vehicle dealer, except to the extent that such application would impair valid contractual agreements in violation of the state or federal constitution.

(2) [This act] does not:

(a) govern, restrict, or apply to data that exists outside of a dealer data system, including data that is generated by a motor vehicle or devices that a consumer connects to a motor vehicle; or

(b) authorize a dealer or third party to use data that is obtained from a person in a manner that is inconsistent with either:

(i) an agreement with the person; or

(ii) the purposes for which the person provided the data to the dealer or third party."

Preamble: The preamble attached to Ch. 362, L. 2023, provided: "WHEREAS, the Legislature finds that the distribution and sale of motor vehicles within this state vitally affect the general economy of the state, the public interest, and the public welfare; and

WHEREAS, to promote the public interest and the public welfare and in the exercise of the state's police power, it is necessary to regulate motor vehicle manufacturers, distributors, and factory or distributor representatives and to regulate dealers of motor vehicles doing business in this state to prevent frauds, impositions, and other abuses upon its citizens and to protect and preserve the investments and properties of the citizens of this state."

Severability: Section 10, Ch. 362, L. 2023, was a severability clause.

Effective Date: Section 20, Ch. 283, L. 2019, provided: "[This act] is effective on passage and approval." Approved May 3, 2019.

Preamble: The preamble attached to Ch. 283, L. 2019, provided: "WHEREAS, the Legislature finds that the distribution and sale of motor vehicles within this state vitally affect the general economy of the state, the public interest, and the public welfare; and

WHEREAS, in order to promote the public interest and the public welfare and in the exercise of the state's police power, it is necessary to regulate motor vehicle manufacturers, distributors, and factory or distributor representatives and to regulate dealers of motor vehicles doing business in this state in order to prevent frauds, impositions, and other abuses upon its citizens and to protect and preserve the investments and properties of the citizens of this state."

Severability: Section 19, Ch. 283, L. 2019, was a severability clause.

30-11-720. Dealer data vendors — authorized integrators — requirements.

Compiler's Comments

Effective Date: Section 9, Ch. 362, L. 2023, provided: "[This act] is effective on passage and approval." Approved May 2, 2023.

Applicability: Section 11, Ch. 362, L. 2023, provided: "(1) [This act] applies to all presently existing or hereafter established systems of distribution of motor vehicles in this state, including all existing agreements between a manufacturer, a factory branch, a distributor or a distributor branch, and a motor vehicle dealer, except to the extent that such application would impair valid contractual agreements in violation of the state or federal constitution.

(2) [This act] does not:

(a) govern, restrict, or apply to data that exists outside of a dealer data system, including data that is generated by a motor vehicle or devices that a consumer connects to a motor vehicle; or

(b) authorize a dealer or third party to use data that is obtained from a person in a manner that is inconsistent with either:

(i) an agreement with the person; or

(ii) the purposes for which the person provided the data to the dealer or third party."

Preamble: The preamble attached to Ch. 362, L. 2023, provided: "WHEREAS, the Legislature finds that the distribution and sale of motor vehicles within this state vitally affect the general economy of the state, the public interest, and the public welfare; and

WHEREAS, to promote the public interest and the public welfare and in the exercise of the state's police power, it is necessary to regulate motor vehicle manufacturers, distributors, and factory or distributor representatives and to regulate dealers of motor vehicles doing business in this state to prevent frauds, impositions, and other abuses upon its citizens and to protect and preserve the investments and properties of the citizens of this state."

Severability: Section 10, Ch. 362, L. 2023, was a severability clause.

Part 8

Termination, Cancellation, Nonrenewal, or Substantial Alteration of Farm Implements Dealership Agreements

Part Case Notes

Consignment and Sales Agreement Subject to MFIDA — Damage Award Proper: The parties entered a consignment and sales agreement for the sale of farm equipment, under which plaintiff would consign and sell certain equipment to defendant for sale to defendant's customers. Plaintiff subsequently filed an action to declare the agreement void. The District Court denied plaintiff's motion and entered judgment for defendant, holding that plaintiff changed the competitive circumstances of the agreement, and awarded damages to defendant. Defendant appealed on grounds that damages were underestimated. Plaintiff cross-appealed on grounds that the court erred in finding that the agreement was subject to the Montana Farm Implements Dealership Act (MFIDA), that the damage award was improper, and that the court erred by concluding that defendant did not waive the MFIDA by agreeing to a termination provision in the agreement that allowed plaintiff to cancel the agreement within 30 days of notice to defendant. The Supreme Court affirmed on all issues. The MFIDA was enacted for a public purpose and defendant did not waive the protective provisions of the MFIDA by entering the agreement, so the agreement was subject to the MFIDA. Additionally, there was substantial evidence in the record, including testimony from numerous experts, to support the damage award. Although several methods were proposed to calculate damages, the District Court was in the best position to judge the credibility of the witnesses and to resolve the conflicting methods, and the Supreme Court declined to disturb the District Court's findings based on the record. Tractor & Equip. Co. v. Zerbe Bros., 2008 MT 449, 348 M 30, 199 P3d 222 (2008).

30-11-801. Definitions.

Compiler's Comments

2001 Amendment: Chapter 483 in definition of department substituted reference to department of labor and industry for reference to department of commerce and substituted "2-15-1701" for "2-15-1801"; and made minor changes in style. Amendment effective July 1, 2001.

1991 Amendment: Inserted definitions of Department, designated family member, and designated successor; and in definition of good cause inserted "when used in 30-11-801 through 30-11-803 and 30-11-811" and inserted (b) defining good cause when used in 30-11-804 through 30-11-809. Amendment effective April 22, 1991.

Severability: Section 9, Ch. 522, L. 1991, was a severability clause.

30-11-802. Cancellation and alteration of dealerships.

Case Notes

Significant Alteration of Dealership Contract Allowing Retroactive Application of Dealership Termination Law — Damage Award Proper: The District Court awarded Van Ripers damages, costs, and attorney fees for the unlawful violation of the farm equipment dealership by Ford New Holland (Ford). Ford contended that the court incorrectly applied the provisions of 30-11-803 and this section retroactively to a dealership contract in effect prior to the effective date of this section. However, the sale of assets by the original dealer significantly altered the dealership relationship and contract, allowing the retroactive application of this section. By terminating Van Ripers' franchise without notice, failing to notify Van Ripers of a dealership attrition plan, and leaving Van Ripers on "stop ship" status after a disputed parts account was paid, Ford violated this section and Van Ripers were entitled to damages for breach of contract and lost profits, even though the amount of damage was uncertain. Van Riper v. Ford New Holland, Inc., 261 M 206, 862 P2d 47, 50 St. Rep. 1289 (1993).

30-11-803. Notice of termination or change in dealership.

Case Notes

Significant Alteration of Dealership Contract Allowing Retroactive Application of Dealership Termination Law — Damage Award Proper: The District Court awarded Van Ripers damages, costs, and attorney fees for the unlawful violation of the farm equipment dealership by Ford New Holland (Ford). Ford contended that the court incorrectly applied the provisions of 30-11-802 and this section retroactively to a dealership contract in effect prior to the effective date of this section. However, the sale of assets by the original dealer significantly altered the dealership relationship and contract, allowing the retroactive application of this section. By terminating Van Ripers' franchise without notice, failing to notify Van Ripers of a dealership attrition plan, and leaving Van Ripers on "stop ship" status after a disputed parts account was paid, Ford violated this section and Van Ripers were entitled to damages for breach of contract and lost profits, even though the amount of damage was uncertain. Van Riper v. Ford New Holland, Inc., 261 M 206, 862 P2d 47, 50 St. Rep. 1289 (1993).

30-11-804. Transfer.

Compiler's Comments

Severability: Section 9, Ch. 522, L. 1991, was a severability clause.

Effective Date: Section 11, Ch. 522, L. 1991, provided that this section is effective April 22, 1991.

30-11-805. Refusal to honor succession to ownership — notice required.

Compiler's Comments

Severability: Section 9, Ch. 522, L. 1991, was a severability clause.

Effective Date: Section 11, Ch. 522, L. 1991, provided that this section is effective April 22, 1991.

30-11-806. Procedure to determine right to succeed.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

Severability: Section 9, Ch. 522, L. 1991, was a severability clause.

Effective Date: Section 11, Ch. 522, L. 1991, provided that this section is effective April 22, 1991.

30-11-807. Written designation of succession unaffected.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral. Amendment effective October 1, 2009.

Severability: Section 9, Ch. 522, L. 1991, was a severability clause.

Effective Date: Section 11, Ch. 522, L. 1991, provided that this section is effective April 22, 1991.

30-11-808. Illegal cancellation of dealership based on natural disaster.

Compiler's Comments

Source: This section is based on section 325E.063, Minnesota Statutes Annotated.

Severability: Section 9, Ch. 522, L. 1991, was a severability clause.

Effective Date: Section 11, Ch. 522, L. 1991, provided that this section is effective April 22, 1991.

30-11-809. Civil damages.

Compiler's Comments

2017 Amendment: Chapter 181 inserted reference to 30-11-814; and made minor changes in style. Amendment effective October 1, 2017.

Applicability: Section 6, Ch. 181, L. 2017, provided: "[This act] applies to all dealer agreements that are executed or renewed on or after [the effective date of this act]." Effective October 1, 2017.

Severability: Section 9, Ch. 522, L. 1991, was a severability clause.

Effective Date: Section 11, Ch. 522, L. 1991, provided that this section is effective April 22, 1991.

Case Notes

Consignment and Sales Agreement Subject to MFIDA — Damage Award Proper: The parties entered a consignment and sales agreement for the sale of farm equipment, under which plaintiff would consign and sell certain equipment to defendant for sale to defendant's customers. Plaintiff subsequently filed an action to declare the agreement void. The District Court denied plaintiff's motion and entered judgment for defendant, holding that plaintiff changed the competitive circumstances of the agreement, and awarded damages to defendant. Defendant appealed on grounds that damages were underestimated. Plaintiff cross-appealed on grounds that the court erred in finding that the agreement was subject to the Montana Farm Implements Dealership Act (MFIDA), that the damage award was improper, and that the court erred by concluding that defendant did not waive the MFIDA by agreeing to a termination provision in the agreement that allowed plaintiff to cancel the agreement within 30 days of notice to defendant. The Supreme Court affirmed on all issues. The MFIDA was enacted for a public purpose and defendant did not waive the protective provisions of the MFIDA by entering the agreement, so the agreement was subject to the MFIDA. Additionally, there was substantial evidence in the record, including testimony from numerous experts, to support the damage award. Although several methods were proposed to calculate damages, the District Court was in the best position to judge the credibility of the witnesses and to resolve the conflicting methods, and the Supreme Court declined to disturb the District Court's findings based on the record. Tractor & Equip. Co. v. Zerbe Bros., 2008 MT 449, 348 M 30, 199 P3d 222 (2008).

30-11-814. Grantor's right of first refusal — farm implements.

Compiler's Comments

Effective Date: This section is effective October 1, 2017.

Applicability: Section 6, Ch. 181, L. 2017, provided: "[This act] applies to all dealer agreements that are executed or renewed on or after [the effective date of this act]." Effective October 1, 2017.

Part 9

Termination, Cancellation, Nonrenewal, Substantial Alteration, or Transfer of Construction Equipment Dealership Agreements

Part Compiler's Comments

Effective Date: This part is effective October 1, 2001.

30-11-901. Definitions.

Compiler's Comments

Code Commissioner Instruction: Pursuant to sec. 221(1), Ch. 483, L. 2001, in definition of department the code commissioner changed "department of commerce" to "department of labor and industry" and "2-15-1801" to "2-15-1701".

30-11-908. Civil damages.

Compiler's Comments

2017 Amendment: Chapter 181 inserted reference to 30-11-914; and made minor changes in style. Amendment effective October 1, 2017.

Applicability: Section 6, Ch. 181, L. 2017, provided: "[This act] applies to all dealer agreements that are executed or renewed on or after [the effective date of this act]." Effective October 1, 2017.

30-11-914. Grantor's right of first refusal — construction equipment.

Compiler's Comments

Effective Date: This section is effective October 1, 2017.

Applicability: Section 6, Ch. 181, L. 2017, provided: "[This act] applies to all dealer agreements that are executed or renewed on or after [the effective date of this act]." Effective October 1, 2017.

CHAPTER 12
WEIGHTS, MEASURES, STANDARDS, AND LABELING

Part 1
General Provisions

30-12-101. Definitions.

Compiler's Comments

2005 Amendment: Chapter 34 inserted definition of on-farm scale; and made minor changes in style. Amendment effective March 18, 2005.

Effective Date — Applicability: Section 4, Ch. 34, L. 2005, provided: "[This act] is effective on passage and approval [approved March 18, 2005] and applies to weighing devices licensed or renewed on or after [the effective date of this act]."

2001 Amendment: Chapter 483 in definition of commodity in package form in second sentence near beginning after "not in" substituted "a consumer package form or nonconsumer package form" for "package form as defined in this section"; in definition of department substituted reference to department of labor and industry for reference to department of commerce and substituted "part 17" for "part 18"; and made minor changes in style. Amendment effective July 1, 2001.

1989 Amendment: Inserted definition of commerce, trade, or commercial; at end of definition of weight, measure, and weights and measures inserted last sentence excluding time measuring devices.

1981 Amendment: Substituted "department of commerce" for "department of business regulation" in (5).

30-12-102. Systems of weights and measures.

Compiler's Comments

1989 Amendment: Near end of first sentence, after "one or both of these systems", substituted "may" for "shall"; and near end substituted "institute of standards and technology" for "bureau of standards".

30-12-103. State standards of weight and measure.

Compiler's Comments

1989 Amendment: Near middle of first sentence substituted "institute of standards and technology" for "bureau of standards"; at end deleted "and they shall be submitted at least once in 10 years to the national bureau of standards for certification"; and made minor changes in phraseology.

30-12-105. Use of metric sizes in sale of commodities — department to make rules.

Compiler's Comments

2001 Amendment: Chapter 483 after "department of" substituted "labor and industry" for "commerce"; and made minor changes in style. Amendment effective July 1, 2001.

1981 Amendments: Chapter 575 inserted "of business regulation" after "department".

Chapter 274 substituted "department of commerce" for "department of business regulation".

Statement of Intent: The statement of intent attached to Senate Bill 82 (Ch. 75, L. 1979) provided: "A statement of intent is required for this bill in that it delegates authority to adopt rules in Section 1.

Senate Bill 82 is enacted into law in order to provide for the voluntary use of metric sizes in packaging. It is particularly directed at Title 30, chapter 12, part 4, and the following or similar commodities: bread, butter, oleomargarine, and margarine, fluid dairy products, flour, corn meal, and hominy grits, as well as furnace and stove oil, and berries and small fruits. The purpose of providing rulemaking authority for the department in allowing for metric sizes is to provide for voluntary use of metric sizes; that is, the rulemaking process will provide the greatest opportunity for industry and consumer input. If metric sizes were defined by statute as under the current law for other sizes, it is possible that either the industry or the consumer may be forced into a position of accepting sizes which are not compatible with their needs. Furthermore, Congress, while attempting to effect the conversion of the United States to the metric system, may, either by statute or rule, define those packaging requirements for the commodities which this bill deals with. In such an instance, rather than returning to the legislature and requesting amendment to the statute, a more efficient and expeditious method of change is provided for. Thus, bread, fluid dairy products, or the other commodities mentioned may be packaged and sold either in the sizes currently provided for in the statutes or in the sizes which will be defined by department rule with the assistance of the industries and consumers involved."

Incorporation Into Existing Law: This section was enacted without any codification instructions and without any definition of "department". The apparent intent of the Legislature was that it become part of Title 30, chapter 12, parts 1 through 5, and that the provisions in parts 1 through 5 apply to it. The Code Commissioner has codified it accordingly. See 1-11-103(4).

30-12-107. Split weighing of commodities allowed — disclosure — rules.

Compiler's Comments

Effective Date: Section 5, Ch. 296, L. 2013, provided: "[This act] is effective July 1, 2013."

Part 2
Authority of Department of Labor and Industry

Part Collateral References

Weights and Measures, Montana Department of Labor and Industry, https://bsd.dli.mt.gov/weights-and-measures.

30-12-201. General powers and duties of department.

Compiler's Comments

1989 Amendment: In last sentence inserted "used in commerce or trade that are"; and made minor change in phraseology.

30-12-202. Specific powers and duties of department — rules.

Compiler's Comments

2023 Amendment: See 2023 Session Law for amendment made by sec. 1, Ch. 228, L. 2023. Amendment effective January 1, 2024.

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

1989 Amendment: In (3), in two places, substituted "institute of standards and technology" for "bureau of standards"; and made minor changes in phraseology.

30-12-203. Licensing of weighing devices.

Compiler's Comments

2023 Amendment: See 2023 Session Law for amendment made by sec. 2, Ch. 228, L. 2023. Amendment effective January 1, 2024.

2013 Amendment: Chapter 356 in (3) increased fees from $16 to $20, from $26 to $33, from $51 to $64, from $130 to $165, and from $225 to $280. Amendment effective July 1, 2013.

2007 Amendment: Chapter 196 in (3) increased fees for weighing devices as follows: 499 pounds or less increased from $12 to $16, 500 through 1,999 pounds increased from $20 to $26, 2,000 through 7,999 pounds increased from $40 to $51, 8,000 through 60,000 pounds increased from $100 to $130, and 60,001 pounds or more increased from $175 to $225. Amendment effective October 1, 2007.

2005 Amendment: Chapter 34 in (2) at end of first sentence substituted "department" for "division of weights and measures"; in (5)(a) near middle inserted exception clause; inserted (5)(b) concerning licenses for on-farm scales; at beginning of (6)(a)(i) inserted "for on-farm scales"; inserted (6)(a)(ii) concerning late fee for all other licenses; inserted (6)(b) concerning sealing and removing weighing device from service if fee not paid; substituted (6)(c) prohibiting use of weighing device removed from service until fees are paid for former text that read: "A person failing to pay the renewal license fee before the first day of the sixth month of the year in which the license fee is due forfeits the right to use the weighing device, and it must be taken out of service by the division of weights and measures until the renewal fee and late renewal fee are paid"; and made minor changes in style. Amendment effective March 18, 2005.

Effective Date — Applicability: Section 4, Ch. 34, L. 2005, provided: "[This act] is effective on passage and approval [approved March 18, 2005] and applies to weighing devices licensed or renewed on or after [the effective date of this act]."

1997 Amendment: Chapter 366 in (3), near beginning after "section", inserted "except that fees may be paid by credit card and may be discounted for payment processing charges paid by the department to a third party"; in (5), at end, substituted "the anniversary date established by rule by the board of review established in 30-16-302" for "December 31"; and in (6), in first and second sentences after "before", substituted reference to the first day of the sixth month of the year in which the license fee is due for "July 1".

1997 Statement of Intent: The statement of intent attached to Ch. 366, L. 1997, provided: "A statement of intent is required for this bill because [section 1] [30-16-104] grants rulemaking authority to the board of review established in 30-16-302 for the purpose of implementing a one-stop business licensing pilot project required by the 54th Legislature."

1993 Amendment: Chapter 615 in (2), in second sentence, substituted "must require" for "should include"; in (3) increased fees for 499 pounds or less from $5 to $12, for 500 pounds through 1,999 pounds from $8 to $20, for 2,000 pounds through 7,999 pounds from $15 to $40, for 8,000 pounds through 60,000 pounds from $40 to $100, and for 60,001 pounds or more from $70 to $175; inserted (7) requiring fees to be deposited in state special revenue fund for administration and enforcement; and made minor changes in style.

Applicability: Section 3, Ch. 615, L. 1993, provided: "[This act] applies to licenses and fees imposed after December 31, 1993."

1983 Amendment: In (3), increased license fees from $2.50 to $5, from $4 to $8, from $10 to $15, from $20 to $40, and from $35 to $70; increased the weight range on the last two categories of (3) from 40,000 to 60,000 pounds and from 40,001 pounds or more to 60,001 pounds or more; in (6) substituted language requiring assessment of late renewal fee and forfeiture of right to use device until fees are paid for "Any person failing to pay the renewal license fee when due as required by this section shall forfeit the right to use the weighing device, and it shall be taken out of service by the division of weights and measures."

30-12-205. General testing.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-12-207. Inspection of packages.

Compiler's Comments

1989 Amendment: In (1), in first sentence, substituted "adopt by rule and implement a schedule to" for "from time to time" and inserted second sentence relating to requirements for randomness; and made minor changes in phraseology.

1989 Statement of Intent: The statement of intent attached to Ch. 442, L. 1989, provided: "A statement of intent is required for this bill because it grants rulemaking authority to the department of commerce to implement and carry out provisions of the Montana Code Annotated relating to inspection of packages. The legislature intends that the department adopt rules or amend existing rules in a manner that will provide that packages or amounts of commodities are tested to see that they contain the amounts represented to ensure that the public may rely on representations of the amounts of commodities being sold. It is contemplated that the rules adopted provide, among other things, that the department establish procedures and schedules for random inspection of packages and amounts of commodities throughout the state and that the rules provide for the random selection of test sites throughout the state."

30-12-211. Duty of owners of incorrect apparatus.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Part 3
Method of Sale of Commodities

30-12-301. Method of sale of commodities — general.

Compiler's Comments

2021 Amendment: Chapter 320 inserted (1)(h) concerning homemade food or homemade food products; and made minor changes in style. Amendment effective April 30, 2021.

2015 Amendment: Chapter 239 in (1) in two places substituted "may be sold" for "shall be sold"; inserted (1)(g) regarding cottage food products; and made minor changes in style. Amendment effective October 1, 2015.

30-12-302. Method of sale of commodities — packages — declarations of quantity and origin — variations — exemptions.

Administrative Rules

ARM 24.351.321 NIST Handbook 133 — checking the net contents of packaged goods.

30-12-306. Sale by net weight.

Compiler's Comments

2013 Amendment: Chapter 296 in (1) at end inserted "on the basis of net weight"; inserted (2) regarding split weighing; and made minor changes in style. Amendment effective July 1, 2013.

Part 4
Sale of Specific Commodities

30-12-406. Bulk deliveries sold in terms of weight and delivered by vehicle.

Compiler's Comments

2013 Amendment: Chapter 296 inserted (1)(d) regarding net weight by split weighing; in (2) in second sentence substituted "the delivery tickets" for "these tickets"; and made minor changes in style. Amendment effective July 1, 2013.

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-12-409. Sale of gasoline and distillates on other than gross volume basis unlawful — exception.

Compiler's Comments

1983 Amendment: In (1), inserted "except" clause and after "sale" inserted "barter, or exchange"; inserted (2) requiring sale on basis of gross volume delivered or on assumption that temperature is 60 degrees Fahrenheit, allowing option only on annual basis and to certain deliveries, stating adjustment standards, and requiring provision of net and gross gallons invoice listings; and inserted (3) stating exceptions.

Part 5
Offenses and Penalties

Part Compiler's Comments

Section Not Codified: Section 90-192, R.C.M. 1947, a severability clause, was not codified in the MCA. This clause has not been repealed and is still valid law. Citation may be made to sec. 40, Ch. 99, L. 1969.

30-12-504. Offenses and penalties.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Conduct Amounting to False Pretenses — Overlapping Statutes: Misdemeanors under Packaged Commodities Offered for Sale Act (since repealed) and the False Weight and Measures Act (replaced by this chapter) were not lesser included offenses of felony of obtaining money by false pretenses since above acts required "sale" while felony statute does not. The State has discretionary power to choose under which law it will charge defendant and the fact that two statutes overlap in prohibiting the same act does not mean that the defendant can only be prosecuted under statute providing lesser penalty. St. v. Lagerquist, 152 M 21, 445 P2d 910 (1968).

Part 7
Country of Origin of Meat

Part Compiler's Comments

Contingent Voidness: Section 8, Ch. 279, L. 2005, provided: "Upon the funding and full implementation of federal mandatory country of origin labeling, adopted as part of the 2002 federal farm bill, [sections 1, 2(1), (3), (5), and (6), 3(2) through (5), 4, and 5 of this act] [30-12-701, 30-12-702(1), (3), (5), and (6), 30-12-704, 30-12-705, and 30-12-706] are void." Pursuant to the final rule that was adopted by the federal Department of Agriculture and that became effective on March 16, 2009, as found on page 2658, Volume 74, of the Federal Register, mandatory country of origin labeling was implemented.

Severability: Section 7, Ch. 279, L. 2005, was a severability clause.

30-12-702. Definitions.

Compiler's Comments

Effective Date: Section 9(1), Ch. 279, L. 2005, provided that this section is effective October 1, 2006.

30-12-703. Labeling permitted.

Compiler's Comments

Effective Date: Section 9(2), Ch. 279, L. 2005, provided: "[Section 3(1) [30-12-703] and this section] are effective on passage and approval." Approved April 19, 2005.

CHAPTER 13
ASSUMED BUSINESS NAMES, TRADEMARKS, AND RELATED RIGHTS

Chapter Compiler's Comments

Severability Clause: Section 8, Ch. 367, L. 1977, read: "If a part of this act is invalid, all valid parts that are severable from the invalid part remain in effect. If a part of this act is invalid in one or more of its applications, the part remains in effect in all valid applications that are severable from the invalid applications."

Part 1
General Provisions

30-13-121. Goodwill of business.

Case Notes

Breach of Contract — Value of Goodwill Determined: In an action for breach of a contract to sell and purchase a barber shop business, the sole issue on appeal was the proper determination of the value of goodwill attributable to the shop's location. The Court found that the District Court improperly restricted the reasonable value of goodwill associated with the shop's location to a 1-month period, in light of the facts that the purchaser had obtained a long-term lease and that there was no indication that the lessor would have been unwilling to lease to the seller on a long-term rather than a month-to-month basis. While there is no rigid rule for determining the value of goodwill, the best indicator is the purchase price agreed upon in a voluntary arm's-length transaction. The three elements comprising the purchase price in this contract were the goodwill associated with the shop's location, the seller's furniture and fixtures, and the shop's telephone connection. The seller removed the fixtures and furniture and disconnected the telephone upon learning of the purchaser's new lease arrangements. These things were valued at $3,000. The seller's recovery was therefore based on the purchase price less the $3,000. An estimate of business lost due to changing locations was then used to determine the percentage of the base price representing the shop's goodwill attached to the shop's location. Baldwin v. Stuber, 187 M 430, 610 P2d 160 (1980).

Owner Entitled to Protection in Exclusive Enjoyment: Goodwill, although intangible, is property capable of transfer, and owner is entitled to same protection in the exclusive enjoyment of it as he is in that of his tangible possessions. A competitor cannot so dress his goods or advertise them as to take away the trade reputation which another has established by a long course of honesty and fair dealing with the public in the same business. Truzzolino Food Prod. Co. v. F. W. Woolworth Co., 108 M 408, 91 P2d 415 (1939), overruled on another point in Fauver v. Wilkoske, 123 M 228, 211 P2d 420 (1949).

Goodwill Intangible: Goodwill of a business is intangible. Esselstyn v. Holmes, 42 M 507, 114 P 118 (1911).

30-13-122. Goodwill transferable.

Case Notes

Breach of Contract — Value of Goodwill Determined: In an action for breach of a contract to sell and purchase a barber shop business, the sole issue on appeal was the proper determination of the value of goodwill attributable to the shop's location. The Court found that the District Court improperly restricted the reasonable value of goodwill associated with the shop's location to a 1-month period, in light of the facts that the purchaser had obtained a long-term lease and that there was no indication that the lessor would have been unwilling to lease to the seller on a long-term rather than a month-to-month basis. While there is no rigid rule for determining the value of goodwill, the best indicator is the purchase price agreed upon in a voluntary arm's-length transaction. The three elements comprising the purchase price in this contract were the goodwill associated with the shop's location, the seller's furniture and fixtures, and the shop's telephone connection. The seller removed the fixtures and furniture and disconnected the telephone upon learning of the purchaser's new lease arrangements. These things were valued at $3,000. The seller's recovery was therefore based on the purchase price less the $3,000. An estimate of business lost due to changing locations was then used to determine the percentage of the base price representing the shop's goodwill attached to the shop's location. Baldwin v. Stuber, 187 M 430, 610 P2d 160 (1980).

Owner Entitled to Protection in Exclusive Enjoyment: Although goodwill of a business is intangible, it is property capable of transfer, and owner thereof is entitled to the same protection in its exclusive enjoyment as he is in that of his tangible possessions. Esselstyn v. Holmes, 42 M 507, 114 P 118 (1911).

Operation and Effect: Where debtor transferred his stock of goods by an itemized bill of sale, which did not include goodwill of the business, evidence as to the value of the goodwill was inadmissible on issue of fraud toward creditors in the conveyance. Yoder v. Reynolds, 28 M 183, 72 P 417 (1903) (suit for conversion of personalty and trespass on realty).

30-13-131. Product of the mind — ownership.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-13-133. Transfer.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-13-135. Subsequent inventor or author.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-13-141. Definitions.

Compiler's Comments

1993 Amendment: Chapter 120 in definition of person inserted reference to limited liability company.

30-13-142. Unauthorized manufacture of sound recordings prohibited.

Compiler's Comments

1981 Amendment: Pursuant to sec. 7, Ch. 198, L. 1981, inserted language allowing the court to fine the offender a maximum of $50,000 in lieu of imprisonment or to punish the offender by both a fine and imprisonment.

30-13-151. Definitions.

Compiler's Comments

Effective Date: Section 6, Ch. 186, L. 2015, provided that this section is effective on passage and approval. Approved April 2, 2015.

30-13-152. Bad faith assertion of patent right.

Compiler's Comments

Effective Date: Section 6, Ch. 186, L. 2015, provided that this section is effective on passage and approval. Approved April 2, 2015.

30-13-153. Remedies for bad faith assertion of patent right.

Compiler's Comments

Effective Date: Section 6, Ch. 186, L. 2015, provided that this section is effective on passage and approval. Approved April 2, 2015.

30-13-154. Damages.

Compiler's Comments

Effective Date: Section 6, Ch. 186, L. 2015, provided that this section is effective on passage and approval. Approved April 2, 2015.

Part 2

Assumed Business Names

Part Case Notes

CASES DECIDED UNDER FORMER LAW

USE OF FICTITIOUS NAME BY PARTNERSHIP

Nonallowance of Suit:

The disability imposed by section 63-602, R.C.M. 1947 (now repealed), is limited to maintaining an action on an account or contract. First Sec. Bank v. U.S., 213 F. Supp. 362 (D.C. Mont. 1963).

The disability imposed by section 63-602, R.C.M. 1947 (now repealed), (not allowing maintenance of an action on contracts or transactions) for failure to comply with section 63-601, R.C.M. 1947 (now repealed), cannot avail a defendant sued by copartners conducting business under a fictitious name, except upon affirmative allegation and proof. It is in the nature of matter in abatement. The inhibition does not destroy the right of action upon which recovery is sought but merely imposes a disability to maintain action until compliance with section 63-601, R.C.M. 1947 (now repealed). Croft v. Bain, 49 M 484, 143 P 960 (1914).

Certificate — Filing Required: If name under which business is transacted fairly discloses true name of individual (or of each partner in case of partnership), section 63-606, R.C.M. 1947 (now repealed), does not apply. Otherwise, the name used is fictitious and the requirement of filing a certificate must be met. Canonica v. St. George, 64 M 200, 208 P 607 (1922).

Failure to File Certificate:

Although plaintiff's use of name "Tony's Tin Shop" did not disclose his true name, nonsuiting plaintiff was error where he made out a prima facie case and defendant did not plead or prove failure to comply with section 63-606, R.C.M. 1947 (now repealed), which required filing of a fictitious name certificate. Canonica v. St. George, 64 M 200, 208 P 607 (1922).

Failure of one doing business under fictitious name to file certificate showing his true name does not invalidate the contract or other transaction sued on by him or destroy his right of action but operates only upon the remedy and then only until the requirements of section 63-606, R.C.M. 1947 (now repealed), have been met. Canonica v. St. George, 64 M 200, 208 P 607 (1922).

In action to recover on contract or obligation by one doing business under fictitious name, an allegation of compliance with statute is not part of statement of his cause of action, his failure in that regard being a matter of defense which must be specially pleaded, else it is waived. Canonica v. St. George, 64 M 200, 208 P 607 (1922).

Transacting Business: A person who, in a single isolated instance, signs a contract with a fictitious name, is not "transacting" or "doing" business within inhibition of section 63-606, R.C.M. 1947 (now repealed), and may invoke aid of court to enforce his claim. Keffler v. Wilds, 50 M 381, 146 P 1103 (1915).

Maintenance of Action:

It is not the right to begin an action but the right to maintain it that is withheld by section 63-602, R.C.M. 1947 (now repealed), for failure to comply with its terms requiring filing of fictitious partnership name. If, before the defense is interposed, plaintiff complies with statutory provisions, the action may be maintained. The defense is an affirmative one and is waived unless pleaded in the answer. Reilly v. Hatheway, 46 M 1, 125 P 417 (1912).

Suit involving a partnership claim may be instituted in name of persons composing the partnership. The fact that plaintiffs are copartners did not appear from face of complaint and was not raised by answer. An objection to the right to maintain the suit being deemed waived, it was not error to exclude evidence showing the fictitious name certificate had been filed. Wilson v. Yegen Bros., 38 M 504, 100 P 613 (1909).

Firm Name:

The name "McLaughlin Bros." did not come within section 63-601, R.C.M. 1947 (now repealed). It cannot be said, as a matter of law, that such name is a designation not showing the names of persons interested as partners. Vaughan v. Kujath, 44 M 484, 120 P 1121 (1912).

Where plaintiffs, A. Guiterman, S. A. Guiterman, and L. A. Guiterman, were doing business under the firm name of Guiterman Bros., the same was neither fictitious nor a designation not showing the names of partners, within purview of section 63-601, R.C.M. 1947 (now repealed). Guiterman v. Wishon, 21 M 458, 54 P 566 (1898).

30-13-201. Definitions.

Compiler's Comments

2001 Amendment: Chapter 27 in definition of assumed business name deleted former (b) that read: "(b) the full, true, and correct name of a limited liability partnership"; inserted definition of business name identifier; in definition of person after "corporation" inserted "limited partnership, limited liability company, limited liability partnership"; and made minor changes in style. Amendment effective October 1, 2001.

1995 Amendment: Chapter 449 in definition of assumed business name inserted (b) concerning name of limited liability partnership.

30-13-202. Registration of assumed business name — when prohibited — contest procedure — rulemaking authority.

Compiler's Comments

2019 Amendment: Chapter 271 in (3) at end after "procedures set forth in" substituted "35-14-401" for "35-1-310". Amendment effective June 1, 2020.

Effective Date: Section 9, Ch. 166, L. 2015, provided that subsection (4) of this section (enacted by sec. 1 of Ch. 166) is effective on passage and approval. Approved April 1, 2015.

2011 Amendment: Chapter 110 inserted (3) allowing a person doing business in the state to contest the registration of an assumed business name. Amendment effective April 1, 2011.

2001 Amendment: Chapter 27 in (2) substituted language prohibiting the use of certain business name identifiers for former language that read: "When the applicant is other than a corporation, limited partnership, limited liability company, or limited liability partnership, the secretary of state may not register the assumed business name for which application is made if the name applied for contains or there is added at the end of the name the word "corporation", "company", "incorporated", or "limited" or an abbreviation of one of the words"; and made minor changes in style. Amendment effective October 1, 2001.

1995 Amendment: Chapter 449 in (1), after "same as or", substituted "not distinguishable on the record from" for "deceptively similar to" and after "company name" inserted "limited liability partnership name"; in (2), after "company", inserted "or limited liability partnership"; and made minor changes in style.

1993 Amendment: Chapter 120 in (1), near middle, and in (2), near beginning, inserted reference to limited liability company; and made minor changes in style.

1983 Amendment: Inserted (2) prohibiting registration of name of other than a corporation or limited partnership if certain designations are in name.

1981 Amendment: (In (1)) inserted "name" after "limited partnership"; inserted "or reserved" after "registered".

Administrative Rules

ARM 44.5.131 Distinguishable on/in the record(s).

Case Notes

Interpretation of Preliminary Injunction — Not Appealable: The District Court's application of an existing preliminary injunction, prohibiting use of a deceptively similar name, to appellant's newly acquired name was not an injunction in itself but merely an interpretation of a preliminary injunction and therefore an interlocutory order, not appealable. Am. Furniture, Inc. v. Am. Furniture Warehouse Co., 219 M 11, 709 P2d 1013, 42 St. Rep. 1804 (1985).

30-13-203. Application for registration of assumed business name.

Compiler's Comments

2015 Amendment: Chapter 166 deleted former (3) that read: "(3) the date of first use, in commerce, of the proposed assumed business name"; and made minor changes in style. Amendment effective April 1, 2015.

2011 Amendment: Chapter 26 in introductory clause after "secretary of state" deleted "or by electronic means established by the board of review established in 30-16-302"; in (1) substituted "business mailing address" for "address, including the street name and number"; in (2) after "complete" deleted "name of the"; and made minor changes in style. Amendment effective October 1, 2011.

1999 Amendment: Chapter 229 deleted former (5) that read: "(5) the name of county or counties in which business is being transacted"; and made minor changes in style. Amendment effective April 2, 1999.

1997 Amendment: Chapter 366 near middle of introductory clause, after "shall", substituted "register" for "execute and file" and after "secretary of state" inserted "or by electronic means established by the board of review established in 30-16-302"; in (3), before "assumed", inserted "the proposed"; in (4), after "under", substituted "the proposed assumed" for "such"; and made minor changes in style.

1997 Statement of Intent: The statement of intent attached to Ch. 366, L. 1997, provided: "A statement of intent is required for this bill because [section 1] [30-16-104] grants rulemaking authority to the board of review established in 30-16-302 for the purpose of implementing a one-stop business licensing pilot project required by the 54th Legislature."

1983 Amendment: In lead-in, after "execute" deleted ", verify,".

30-13-204. Filing application for registration — issuance of certificate.

Compiler's Comments

2017 Amendment: Chapter 23 in (2) at end substituted "in effect for 5 years unless canceled earlier" for "in effect until canceled". Amendment effective October 1, 2017.

2005 Amendment: Chapter 71 in (1) at beginning of first sentence substituted "The applicant shall complete and submit an application" for "One original and one copy of application" and near middle after "business name" substituted "along with all applicable fees" for "shall be executed and delivered" and at end of second sentence after "shall" deleted "when all fees have been paid as provided in this part"; in (1)(a) substituted "application" for "original and one copy"; in (1)(b) substituted "application" for "original"; in (1)(c) after "registration" deleted "to which he shall affix the copy" and before "to the applicant" deleted part of former (2) that read: "(2) The certificate of registration, together with the copy of the application for registration of an assumed business name affixed thereto by the secretary of state, shall be returned"; and made minor changes in style. Amendment effective October 1, 2005.

1983 Amendment: At beginning of (1), substituted "One original and one copy" for "Duplicate originals"; inserted "executed and" before "delivered"; in (1)(a), substituted "the original and the copy" for "each of the duplicate originals"; in (1)(b), substituted "the original" for "one of the duplicate originals"; in (1)(c), substituted "copy" for "other original"; in (2), substituted "copy" for "duplicate original"; and made minor phraseology changes.

30-13-205. When registration of assumed business name by foreign corporation or foreign limited partnership prohibited.

Compiler's Comments

1983 Amendment: Inserted "or foreign limited partnership" and "or certificate of registration".

30-13-206. Term and renewal of assumed business name registration.

Compiler's Comments

2011 Amendment: Chapter 26 in (1) after "secretary of state" deleted "or by electronic means established by rule by the board of review established in 30-16-302"; in (3) at beginning deleted "Subject to subsection (3)(b)"; deleted former (3)(b) that read: "(b) If a limited liability partnership fails to file an application for renewal with the secretary of state within a 90-day period prior to the expiration date of the registration, the secretary of state shall cancel the registration and the partnership is no longer a limited liability partnership"; and made minor changes in style. Amendment effective October 1, 2011.

2003 Amendment: Chapter 75 in (3)(b) after "expiration date of the registration" deleted "the secretary of state shall again notify the limited liability partnership of the pending expiration and give the limited liability partnership an additional 90 days within which to renew its registration. If the limited liability partnership fails to renew its registration within the second 90-day period"; and made minor changes in style. Amendment effective October 1, 2003.

1997 Amendment: Chapter 366 in (1), in second sentence after "secretary of state", inserted "or by electronic means established by rule by the board of review established in 30-16-302".

1997 Statement of Intent: The statement of intent attached to Ch. 366, L. 1997, provided: "A statement of intent is required for this bill because [section 1] [30-16-104] grants rulemaking authority to the board of review established in 30-16-302 for the purpose of implementing a one-stop business licensing pilot project required by the 54th Legislature."

1995 Amendment: Chapter 449 at beginning of (3)(a) inserted "Subject to subsection (3)(b)"; inserted (3)(b) concerning failure of limited liability partnership to file application for renewal; and made minor changes in style.

30-13-207. Application for renewal of assumed business name.

Compiler's Comments

2011 Amendment: Chapter 26 in (2) substituted "business mailing address" for "address, including street name and number, if any"; and made minor changes in style. Amendment effective October 1, 2011.

2003 Amendment: Chapter 75 at beginning of introductory clause deleted "One original and one copy of". Amendment effective October 1, 2003.

1999 Amendment: Chapter 229 deleted former (4) that read: "(4) the name of the county or counties in which business is being transacted"; and made minor changes in style. Amendment effective April 2, 1999.

1983 Amendments: Chapter 131, at beginning of section, substituted "One original and one copy" for "Duplicate originals"; and made minor phraseology changes.

Chapter 174, in lead-in, after "executed" deleted ", verified,".

30-13-208. Filing of application for renewal of registration of assumed business name — issuance of certificate.

Compiler's Comments

2005 Amendment: Chapter 71 in introductory clause after "paid" deleted "as provided in this part"; in (1) substituted "application" for "original and the copy"; in (2) substituted "application" for "original"; in (3) after "renewal" deleted "to which he shall affix the copy" and before "to the applicant" deleted part of former (2) that read: "(2) The certificate of renewal, together with the copy of the application for renewal of registration of an assumed business name affixed thereto by the secretary of state, shall be returned"; and made minor changes in style. Amendment effective October 1, 2005.

1983 Amendment: In (1)(a), substituted "the original and the copy" for "each of the duplicate originals"; in (1)(b), substituted "the original" for "one of the duplicate originals"; in (1)(c), substituted "copy" for "other duplicate original"; in (2), substituted "copy" for "duplicate original"; and made minor phraseology changes.

30-13-209. Amendment.

Compiler's Comments

1999 Amendment: Chapter 229 in (2) substituted "description of the business transacted" for "identity of the county or counties in which the name is or is intended to be used". Amendment effective April 2, 1999.

1995 Amendment: Chapter 449 in introductory clause extended time from 60 days to 1 year; and made minor changes in style.

30-13-210. Filing amendment to registration of assumed business name — issuance of certificate.

Compiler's Comments

2005 Amendment: Chapter 71 in (1) deleted former first sentence that read: "One original and one copy of an amendment to the registration of an assumed business name must be delivered to the secretary of state" and in first sentence inserted requirement to file with secretary of state and after "include" deleted "but is not limited to the following information"; inserted (1)(g) concerning other information determined by the secretary of state to be necessary; in (2) after "paid" deleted "as provided in this part"; in (2)(a) substituted "application for amendment" for "original and the copy"; in (2)(b) after "original" inserted "application for amendment"; in (2)(c) after "amendment" deleted "to which the secretary of state shall affix the copy" and before "to the registrant" deleted part of former (3) that read: "(3) The certificate of amendment, together with the copy of the amendment required in subsection (1), must be returned"; and made minor changes in style. Amendment effective October 1, 2005.

1999 Amendment: Chapter 229 deleted former (1)(e) and (1)(f) that read: "(e) the name of the county or counties in which the name is being used;

(f) if there is a change in the identity of the county or counties or addition of a county or counties in which the assumed business name is being used or is to be used, the name of the new county or counties"; and made minor changes in style. Amendment effective April 2, 1999.

1997 Amendment: Chapter 366 in (1), in first sentence after "business name", deleted "executed and verified on forms furnished by the secretary of state"; in (3), after "amendment", substituted "required in subsection (1), must" for "affixed thereto by the secretary of state, shall"; and made minor changes in style.

1997 Statement of Intent: The statement of intent attached to Ch. 366, L. 1997, provided: "A statement of intent is required for this bill because [section 1] [30-16-104] grants rulemaking authority to the board of review established in 30-16-302 for the purpose of implementing a one-stop business licensing pilot project required by the 54th Legislature."

1983 Amendment: In (1), substituted "One original and one copy" for "Duplicate originals"; in (2)(a), substituted "the original and the copy" for "each of the duplicate originals"; in (2)(b), substituted "the original" for "one of the duplicate originals"; in (2)(c), substituted "copy" for "other duplicate original"; in (3), substituted "copy" for "duplicate original"; and made minor phraseology changes.

30-13-211. Reservation of proposed assumed business name.

Compiler's Comments

1999 Amendment: Chapter 229 deleted former (5) that read: "(5) the county or counties in which applicant intends to conduct business"; and made minor changes in style. Amendment effective April 2, 1999.

30-13-212. Filing application for reservation of assumed business name — issuance of certificate.

Compiler's Comments

2005 Amendment: Chapter 71 in introductory clause at beginning of first sentence substituted "The applicant shall complete and submit" for "One original and one copy of" and after "name" substituted "and all applicable fees" for "duly executed by the applicant, shall be delivered" and at end of second sentence deleted "when all fees have been paid as provided in this part"; in (1) substituted "application" for "original and the copy"; in (2) substituted "application" for "original"; in (3) after "reservation" deleted "to which he shall affix the copy" and before "to the applicant" deleted part of former (2) that read: "(2) The certificate of reservation, together with the copy of the application for reservation of an assumed business name affixed thereto by the secretary of state, shall be returned"; and made minor changes in style. Amendment effective October 1, 2005.

1983 Amendments: Chapter 131, in (1), substituted "One original and one copy" for "Duplicate originals"; in (1)(a), substituted "the original and the copy" for "each of the duplicate originals"; in (1)(b), substituted "the original" for "one of the duplicate originals"; in (1)(c), substituted "copy" for "other duplicate original"; in (2), substituted "copy" for "duplicate original"; and made minor phraseology changes.

Chapter 174, in (1), after "executed" deleted "and verified".

30-13-213. Voluntary cancellation of registration of assumed business name.

Compiler's Comments

2017 Amendment: Chapter 23 in (1) near middle after "the secretary of state" deleted "an executed and verified original affidavit of" and after "an assumed business name" inserted "form"; in (2) substituted "form" for "affidavit" and after "file it and" substituted "deliver" for "mail"; and made minor changes in style. Amendment effective October 1, 2017.

2011 Amendment: Chapter 26 in (1)(a) after "complete" deleted "name of the"; in (1)(b) substituted "business mailing address" for "address, including the street name and number, if any"; and made minor changes in style. Amendment effective October 1, 2011.

1995 Amendment: Chapter 449 in (2) substituted "letter acknowledging cancellation" for "letter of acknowledgment"; and made minor changes in style.

30-13-215. Effect of transacting business without certificate.

Case Notes

Standing to File Construction Lien Despite Construction Corporation's Involuntary Dissolution: Plaintiff asserted that defendant had no standing to file a construction lien because defendant's corporation had been involuntarily dissolved for failure to file the first annual corporate report. The District Court disagreed, and the Supreme Court affirmed. Defendant filed the lien as an individual claimant and had standing to pursue the lien as a person who furnished services pursuant to a real estate improvement contract. It would have been inequitable for plaintiff to avoid an obligation because the corporation had been involuntarily dissolved after acting in good faith through its principals, and plaintiff was properly estopped from denying the status of the corporation. Weimar v. Lyons, 2007 MT 182, 338 M 242, 164 P3d 922 (2007), following Kosena v. Eck, 195 M 12, 635 P2d 1287 (1981).

Individual Not Accountable for Default Judgment Against Unregistered Business: This section prevents an unregistered business from filing suit under its unregistered name. Nothing in the statute indicates that an individual should be held accountable for a default judgment entered against an unregistered business. Jerry Martin & Associates, Inc. v. Don's Westland Bulk, 267 M 464, 884 P2d 795, 51 St. Rep. 1119 (1994).

30-13-216. Evidentiary effect of certificates and documents of secretary of state.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Corporation Acting Under Assumed Name Without Registration — No Right of Access to Courts: In an action by a foreign corporation against Montana parties, under 35-1-1004 (repealed and replaced by 35-1-1027, now also repealed), the out-of-state corporation is without authority to bring suit in Montana because it is a foreign corporation transacting business in the state without a certificate of authority. The corporation received a certificate more than 10 years ago, but it has since been suspended. Another company incorporated by the same principals presently holds a valid certificate of authority in this state, but the record contains no evidence that the businesses have been merged, although apparently the second foreign corporation used the first corporation's name as a trade name. Under this section, a corporation acting under an assumed name without registration has no right of access to state courts. The plaintiff's complaint is dismissed unless the corporation amends its complaint to name the proper party within a reasonable time as prescribed by former Rule 17(a), M.R.Civ.P. (now superseded). Mktg. Specialists, Inc. v. Serv. Mktg. of Mont., Inc., 214 M 377, 693 P2d 540, 42 St. Rep. 32 (1985).

30-13-217. Fees and charges to be established and collected by secretary of state.

Compiler's Comments

2011 Amendment: Chapter 26 deleted former (1)(c) that read: "(c) a license fee from each limited liability partnership at the time of registration under 30-13-203 and at the time of each renewal of registration under 30-13-206 through 30-13-208"; and made minor changes in style. Amendment effective October 1, 2011.

2001 Amendment: Chapter 396 substituted (1) concerning setting certain fees in accordance with 2-15-405 for former (1) through (3) that read: "(1) The secretary of state shall by administrative rule establish, charge, and collect in accordance with the provisions of this part and commensurate with costs:

(a) fees for filing documents and issuing certificates; and

(b) miscellaneous charges.

(2) The secretary of state shall maintain records sufficient to support the fees and miscellaneous charges established under this section.

(3) In addition to the fees and charges in subsection (1), the secretary of state shall charge and collect from each limited liability partnership a license fee of:

(a) $50 at the time of registration under 30-13-203; and

(b) $50 at the time of each renewal of registration under 30-13-206 through 30-13-208"; and in (2) after "charges" deleted "established under this section". Amendment effective July 1, 2001.

1997 Amendment: Chapter 366 inserted (4) allowing payment of fees and charges by credit card and discount for payment processing charges.

1997 Statement of Intent: The statement of intent attached to Ch. 366, L. 1997, provided: "A statement of intent is required for this bill because [section 1] [30-16-104] grants rulemaking authority to the board of review established in 30-16-302 for the purpose of implementing a one-stop business licensing pilot project required by the 54th Legislature."

1995 Amendment: Chapter 449 inserted (3) concerning fees for limited liability partnerships.

1985 Amendment: Substituted language requiring Secretary of State by rule to establish, charge, and collect fees and charges, and maintain records relating to such fees and charges for "The secretary of state shall collect for:

(1) filing application for registration of assumed business name and issuing certificate thereon, $15;

(2) filing application for renewal of registration of assumed business name and issuing certificate thereon, $10;

(3) filing amendment to registration of assumed business name and issuing certificate thereon, $10;

(4) filing application for reservation of assumed business name and issuing certificate thereon, $15; and

(5) filing any other instrument not provided for in this section, $5."

Administrative Rules

ARM 44.5.119 Assumed business name fees.

30-13-218. Execution constituting affirmation — penalty — warning.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-13-219. Political party central committee assumed business name.

Compiler's Comments

Effective Date: Section 9(2), Ch. 198, L. 2019, provided that this section is effective on passage and approval. Approved April 25, 2019.

Retroactive Applicability: Section 10, Ch. 198, L. 2019, provided: "[Sections 2 through 6] [13-38-106, 13-38-107, 13-38-202, 30-13-219, and 30-13-342] apply retroactively, within the meaning of 1-2-109, to August 1, 2018."

Preamble: The preamble attached to Ch. 198, L. 2019, provided: "WHEREAS, the office of committee representative is a position created by the Montana Legislature pursuant to section 13-38-201, MCA; and

WHEREAS, the committee representatives in each precinct constitute the city or county central committee of their respective political parties; and

WHEREAS, the Legislature has delegated the power of the State of Montana to party central committees to participate in the process of filling vacancies for legislative and county commission positions; and

WHEREAS, the State of Montana has the power to regulate political parties to ensure elections are orderly, fair, and honest; and

WHEREAS, other courts have recognized that when a state delegates power to a political party committee to fill vacancies, the state may require compliance with state law; and

WHEREAS, the State of Montana has an interest in limiting opportunities for fraud and corruption by party leadership; and

WHEREAS, the Montana Supreme Court has recognized the power to intervene in the affairs of a political party when the rights of individuals are involved; and

WHEREAS, the enactment of secret rules governing committee representatives, the use of fraudulent proxies of committee representatives, the arbitrary removal of committee representatives, and the filing of false trade and service marks with the Montana Secretary of State are fraudulent and corrupt practices; and

WHEREAS, the enactment of secret rules governing committee representatives, the use of fraudulent proxies of committee representatives, and the removal of committee representatives before the conclusion of a term may result in a disorderly, unfair, and dishonest election to fill a vacancy in a legislative or county commission position; and

WHEREAS, it is in the interest of the State of Montana to prevent fraud and corruption and to ensure fair, honest, and orderly elections conducted by committee representatives and to protect the rights of individuals by setting clear expectations and guidelines for the office of committee representative."

Severability: Section 8, Ch. 198, L. 2019, was a severability clause.

30-13-221. Filing of facsimile copy.

Compiler's Comments

1997 Amendment: Chapter 290 at end of first sentence in (1) deleted "provided that he receives the original document within 5 working days of the receipt of the facsimile copy"; deleted introductory phrase and (1)(a), (1)(b), (2), and (3) that read: "A facsimile copy may be filed under this section if it:

(a) is produced by a method of transmission of images in which the image is scanned at the transmitter, reconstructed at the receiving station, and duplicated on paper at the receiving station; and

(b) is legible and the same size as the original.

(2) During the 5-day period referred to in subsection (1), the recorded facsimile copy constitutes constructive notice for all purposes of the original document.

(3) If the original document is not received within 5 working days of receipt of the facsimile copy as provided in subsection (1), the filing of the facsimile copy is void"; and made minor changes in style. Amendment effective April 18, 1997.

Part 3
Trademarks

Part Compiler's Comments

Savings: Section 20, Ch. 429, L. 1979, provided: "This act does not affect any right which matured or proceeding which was commenced prior to July 1, 1980."

Severability: Section 21, Ch. 429, L. 1979, was a severability clause.

Effective Date: Section 23, Ch. 429, L. 1979, provided: "This act is effective on July 1, 1980."

Part Case Notes

CASES DECIDED UNDER FORMER TRADEMARK LAW

Exclusive Use: A person may be protected in the exclusive use of his own name or that of a place, building, or other designation selected by him and by use of which, in connection with his business, he has acquired for it a valuable good will. Esselstyn v. Holmes, 42 M 507, 114 P 118 (1911).

Generic or Descriptive Names:

Names of an article of trade which are generic or which are merely descriptive of its qualities or characteristics cannot be employed as trademarks or trade names. Esselstyn v. Holmes, 42 M 507, 114 P 118 (1911).

Plaintiff was not entitled to the exclusive use of the words "Owl Creek Coal" as a trade name for coal mined in a district known as the "Owl Creek Coalfield" in which there is competitive mining. Esselstyn v. Holmes, 42 M 507, 114 P 118 (1911).

30-13-301. Definitions.

Compiler's Comments

2009 Amendment: Chapter 177 inserted definitions of counterfeit mark, counterfeiter, and retail value; and made minor changes in style. Amendment effective July 1, 2009.

2003 Amendment: Chapter 257 inserted definitions of abandoned, dilution, and use; in definition of applicant near middle after "registration of a" substituted "mark" for "trademark"; in definition of person at end after "organization" inserted "capable of suing and being sued in a court of law"; in definition of registrant near middle after "registration of a" substituted "mark" for "trademark"; in definition of service mark in first sentence near beginning after "means" substituted "any word, name, symbol, or device or any combination of words, names, symbols, or devices used by a person" for "a mark used in the sale or advertising of services", near middle after "identify" inserted "and distinguish", after "one person" deleted "and distinguish them" and inserted "including a unique service", and at end after "others" inserted "and to indicate the source of the services, even if that source is unknown" and inserted second sentence providing for the registration of certain titles, character names, and other distinctive features of radio or television programs; in definition of trade names near beginning after "means" substituted "any name" for "a word, name, symbol, device, or any combination thereof" and near end after "vocation" deleted "or occupation and distinguish it from the business, vocation, or occupation of others"; in definition of trademark near middle before "used" deleted "adopted and", after "identify" substituted "and distinguish the goods of that person, including a unique product, from those manufactured or sold" for "goods made or sold by the person and to distinguish them from goods made or sold", and at end after "others" inserted "and to indicate the source of the goods, even if that source is unknown"; and made minor changes in style. Amendment effective July 1, 2003.

1993 Amendment: Chapter 120 in definition of person inserted reference to limited liability company; and made minor changes in style.

30-13-303. Registrability.

Compiler's Comments

2003 Amendment: Chapter 257 in subsections (1)(a), (1)(b), (1)(c), (1)(d), and (1)(f) at beginning inserted "consists of or"; in (1)(e) at beginning substituted "consists of" for "comprises"; in (1)(e)(i) and (1)(e)(ii) near beginning after "when" substituted "used on or in connection with" for "applied to"; in (2) in second sentence near middle after "distinctive" substituted "as used on or in connection with" for "as applied to" and at end after "date" substituted "on which the claim of distinctiveness is made" for "of the filing of the application for registration"; and made minor changes in style. Amendment effective July 1, 2003.

Case Notes

"Yellowstone Outfitters" — Primarily Geographically Descriptive: "Yellowstone" is the name of a river, a county, and a national park. "Outfitters" is a name descriptive of services being offered in the region around Yellowstone National Park. Together the two denote outfitting services in the Yellowstone area. Therefore, the name "Yellowstone Outfitters" is primarily geographically descriptive within the meaning of 30-13-303(1) and under the ruling of Esselstyn v. Holmes, 42 M 507, 117 P 118 (1911). Further, "Yellowstone Outfitters" does not fall within the 30-13-303(2) exception to the rule against appropriation of geographically descriptive names because there has been no showing that appellant's name has become distinctive of his services. Warwood v. Hubbard, 218 M 438, 709 P2d 637, 42 St. Rep. 1719 (1985).

30-13-310. Filing of applications.

Compiler's Comments

Effective Date: Section 18, Ch. 257, L. 2003, provided that this section is effective July 1, 2003.

Administrative Rules

ARM 44.5.131 Distinguishable on/in the record(s).

30-13-311. Application for registration.

Compiler's Comments

2003 Amendment: Chapter 257 in (1) in introductory clause near beginning after "who" deleted "adopts and" and after "mark" deleted "in this state"; inserted (1)(a)(iii) requiring partnerships to furnish the state of organization and the names of general partners; deleted former (1)(b) that read: "(b) the essential feature of the mark to be registered"; in (1)(b) in two places before "in connection with" inserted "on or"; deleted former (1)(e) that read: "(e) a statement that the mark is presently in use in this state by the applicant"; in (1)(d) near beginning after "owner of the mark" substituted "that the mark is in use, and that, to the knowledge of the person verifying the application, no other person has registered the mark, either federally or in this state, or has" for "and that no other person has", after "use the mark" deleted "in this state", and at end after "resembles" substituted "the mark as to be likely, when applied to the goods or services of the other person, to cause confusion, to cause mistake, or to deceive" for "it that it might be calculated to deceive or might be mistaken for it"; inserted (2) authorizing the secretary of state to obtain certain information from an applicant if an application has been filed by the applicant with the United States patent and trademark office; inserted (3) concerning drawing of mark to accompany application; in (4) near beginning after "signed" inserted "and verified"; in (5) near middle after "accompanied by" substituted "three specimens showing" for "two copies of a specimen or facsimile of" and at end inserted "as actually used"; and made minor changes in style. Amendment effective July 1, 2003.

1993 Amendment: Chapter 120 in (1)(a), after "incorporation", inserted "or, if a limited liability company, the state of organization"; in (2), after "firm", inserted "or limited liability company"; and made minor changes in style.

1985 Amendment: In (4) substituted "as provided for in 30-13-320" for "of $20, payable to the secretary of state".

1983 Amendments: Chapter 131, in (3), substituted "two copies of a specimen or facsimile" for "in duplicate".

Chapter 174, in (2), substituted "signed by the applicant" for "signed and verified by affidavit of the applicant".

Administrative Rules

ARM 44.5.120 Trademark fees.

ARM 44.5.141 Requirements for filing trademark applications, renewals, and assignments.

30-13-312. Certificate of registration.

Compiler's Comments

2003 Amendment: Chapter 257 substituted language in (1) providing for the issuance of a certificate of registration by the secretary of state and designating what information must be shown on the certificate for former subsections (1) and (2) that read: "(1) One original and one copy of an application for registration of a mark must be delivered to the secretary of state. If the secretary of state finds that the application complies with the requirements of this part, he shall, when all fees have been paid as prescribed in this part:

(a) endorse on the original and the copy the word "filed" and the month, day, and year of the filing thereof;

(b) file the original in his office; and

(c) issue a certificate of registration to which he shall affix the copy.

(2) The certificate of registration, together with the copy of the application for registration of mark affixed thereto, shall be returned to the applicant"; and made minor changes in style. Amendment effective July 1, 2003.

1983 Amendment: In (1), substituted "One original and one copy" for "Duplicate originals"; in (1)(a), substituted "the original and the copy" for "each such duplicate original"; substituted "word" for "words"; deleted "for record" after "filed"; in (1)(b), substituted "the original" for "one such duplicate original"; in (1)(c), substituted "copy" for "other duplicate original"; and in (2), substituted "copy" for "duplicate original".

30-13-313. Duration and renewal.

Compiler's Comments

2011 Amendment: Chapter 26 in (5) in introductory clause inserted "and the following information" and inserted (5)(a) through (5)(e) relating to information required for renewal applications; and made minor changes in style. Amendment effective October 1, 2011.

2003 Amendment: Chapter 257 in (1) near beginning after "term of" decreased duration of registration period from 10 years to 5 years, near middle after "that term" inserted "in a manner complying with the requirements of the secretary of state", and at end decreased registration renewal periods from 10 years to 5 years; deleted former (2) and (3) that read: "(2) An application for renewal of mark registration must be delivered to the secretary of state and shall set forth information including but not limited to the following:

(a) the name and business address of the applicant;

(b) a description of the mark; and

(c) a statement that the mark is still in use by the applicant in this state.

(3) The application for renewal of mark registration must be signed by the applicant"; inserted (3) providing that registrations may be renewed for successive 5-year periods; inserted (4) providing for the continued existence and renewal of registrations in force on July 1, 2003; inserted (5) requiring applications for renewal to include a verified statement; and made minor changes in style. Amendment effective July 1, 2003.

1985 Amendment: In (4) substituted "as provided for in 30-13-320" for "of $20, payable to the secretary of state".

1983 Amendment: In (3), substituted "signed by the applicant" for "signed and verified by affidavit of the applicant".

Administrative Rules

ARM 44.5.120 Trademark fees.

30-13-315. Assignment — change of name — other instruments.

Compiler's Comments

2003 Amendment: Chapter 257 in (1) inserted second sentence requiring assignments to be executed instruments and at beginning of third sentence inserted "Upon recording the assignment, the secretary of state shall issue a new certificate in the name of the assignee"; deleted former (2), (3), and (4) that read: "(2) One original and one copy of an assignment of a mark must be delivered to the secretary of state and shall set forth information including but not limited to the following:

(a) the name and address of the assignor;
(b) the name and address of the assignee;
(c) the registration number of the mark; and
(d) the date of registration.

(3) The assignment of a mark must be signed and verified by the assignor.

(4) The assignment of a mark must be accompanied by a filing fee as provided for in 30-13-320"; inserted (2) providing a procedure for effecting a change of the name of the person to whom a mark was issued or for whom an application was filed and authorizing the secretary of state to issue a new registration certificate; inserted (3) providing for the recording of other instruments relating to a registered mark or application; inserted (4) providing that an acknowledgment is prima facie evidence of the execution of an assignment; inserted (5) requiring that a certified copy of an instrument be accepted for recording; and made minor changes in style. Amendment effective July 1, 2003.

1985 Amendment: In (4) substituted "as provided for in 30-13-320" for "of $20, payable to the secretary of state".

1983 Amendment: In (2), substituted "One original and one copy" for "Duplicate originals".

Administrative Rules

ARM 44.5.120 Trademark fees.

30-13-317. Records.

Compiler's Comments

2003 Amendment: Chapter 257 at end after "part" inserted "as well as a record of all documents recorded pursuant to 30-13-315". Amendment effective July 1, 2003.

30-13-318. Cancellation.

Compiler's Comments

2003 Amendment: Chapter 257 at end of introductory clause after "register" inserted "in whole or in part"; deleted former (1) that read: "(1) after July 1, 1981, each registration made prior to July 1, 1980, that is more than 10 years old and not renewed in accordance with this part"; in (1) near middle before "request" substituted "voluntary" for "written", after "cancellation" deleted "signed and verified by", and at end after "record" deleted "and accompanied by fees as prescribed in this part"; inserted (3)(e) providing for the cancellation of a mark that has become the generic name for goods or services; and made minor changes in style. Amendment effective July 1, 2003.

1983 Amendment: In (2), before "request" changed "voluntary" to "written", before "the registrant" inserted "signed and verified by", and at end inserted "and accompanied by fees as prescribed in this part"; and made minor changes in phraseology.

30-13-320. Secretary of state to establish and collect fees.

Compiler's Comments

2001 Amendment: Chapter 396 substituted text concerning collection of fees and charges set and deposited in accordance with 2-15-405 for former text that read: "The secretary of state shall by administrative rule establish and provide for collection of fees and miscellaneous charges for filing documents and issuing certificates as required by this part. The fees must be commensurate with the costs of processing the documents and certificates. The secretary of state shall maintain records sufficient to support the fees and miscellaneous charges established under this part." Amendment effective July 1, 2001.

Administrative Rules

ARM 44.5.120 Trademark fees.
ARM 44.5.121 Miscellaneous fees.

30-13-331. Classification.

Compiler's Comments

2003 Amendment: Chapter 257 at beginning of first sentence substituted "The secretary of state shall adopt rules establishing a classification of goods and services" for "The following classes of goods and services are established", in third sentence near middle after "services" deleted "comprised in a single class with regard to" and at end after "used" inserted "indicating the appropriate class or classes of goods or services", in fourth sentence at beginning substituted "When" for "However, in no event may", near middle before "classes" substituted "multiple" for "different", and after "classes" at end inserted "the secretary of state may require payment of a fee for each class", and inserted fifth sentence requiring the classification of goods and services to conform to classification of the United States patent and trademark office, if possible; deleted former (2) and (3) that read: "(2) The classes of goods are as follows:

(a) raw or partly prepared materials;
(b) receptacles;
(c) baggage, animal equipments, portfolios, and pocketbooks;
(d) abrasive and polishing materials;
(e) adhesives;
(f) chemicals and chemical compositions;
(g) cordage;
(h) smokers' articles, not including tobacco products;
(i) explosives, firearms, equipment, and projectiles;
(j) fertilizers;
(k) inks and inking materials;
(l) construction materials;
(m) hardware and plumbing and steamfitting supplies;
(n) metals and metal casting and forgings;
(o) oils and greases;
(p) paints and painters' materials;
(q) tobacco products;
(r) medicines and pharmaceutical preparations;
(s) vehicles;
(t) linoleum and oil cloth;
(u) electrical apparatus, machines, and supplies;
(v) games, toys, and sporting goods;
(w) cutlery, machinery, and tools, and parts thereof;
(x) laundry appliances and machines;
(y) locks and safes;
(z) measuring and scientific appliances;
(aa) horological instruments;
(bb) jewelry and precious metal ware;
(cc) brooms, brushes, and dusters;
(dd) crockery, earthenware, and porcelain;
(ee) filters and refrigerators;
(ff) furniture and upholstery;
(gg) glassware;
(hh) heating, lighting, and ventilating apparatus;
(ii) belting, hose, machinery packing, and nonmetallic tires;
(jj) musical instruments and supplies;
(kk) paper and stationery;
(ll) prints and publications;
(mm) clothing;
(nn) fancy goods, furnishings, and notions;
(oo) canes, parasols, and umbrellas;
(pp) knitted, netted, and textile fabrics, and substitutes therefor;
(qq) thread and yarn;
(rr) dental, medical, and surgical appliances;
(ss) soft drinks and carbonated waters;
(tt) foods and ingredients of foods;
(uu) wines;
(vv) malt beverages and liquors;

(ww) distilled alcoholic liquors;
(xx) merchandise not otherwise classified;
(yy) cosmetics and toilet preparations;
(zz) detergents and soaps.
(3) The classes of services are as follows:
(a) miscellaneous;
(b) advertising and business;
(c) insurance and financial;
(d) construction and repair;
(e) communications;
(f) transportation and storage;
(g) material treatment;
(h) education and entertainment"; and made minor changes in style. Amendment effective July 1, 2003.

Administrative Rules

ARM 44.5.141 Requirements for filing trademark applications, renewals, and assignments.

30-13-332. Fraudulent registration.

Compiler's Comments

2003 Amendment: Chapter 257 in first sentence near middle after "fraudulent representation" inserted "or declaration"; and made minor changes in style. Amendment effective July 1, 2003.

30-13-333. Infringement.

Compiler's Comments

2009 Amendment: Chapter 177 in (1) at beginning of introductory clause inserted "In addition to the penalties and remedies provided for in 30-13-338 and"; and made minor changes in style. Amendment effective July 1, 2009.

2003 Amendment: Chapter 257 in (1) near beginning after "30-13-336" inserted "and subsection (2) of this section" and near middle after "brought by the" substituted "registrant" for "lawful owner of a registered mark"; and made minor changes in style. Amendment effective July 1, 2003.

30-13-334. Injury to business reputation — dilution.

Compiler's Comments

2003 Amendment: Chapter 257 in (1) substituted language providing that the owner of a mark or trade name that is famous in this state is entitled to an injunction against another person's use of a mark or trade name as well as other relief provided in this section for former language that read: "Likelihood of injury to business reputation or of dilution of the distinctive quality of a mark registered under this part or a mark valid at common law or a trade name valid at common law is grounds for injunctive relief notwithstanding the absence of competition between the parties or the absence of confusion as to the source of goods or services"; inserted (2) establishing factors for a court to consider in determining whether a mark is distinctive and famous; inserted (3) providing that the owner of a famous mark is only entitled to injunctive relief unless the other person willfully intended to trade on the owner's reputation or to cause dilution of the mark; inserted (4) listing certain activities that are not actionable under this section; and made minor changes in style. Amendment effective July 1, 2003.

30-13-335. Remedies.

Compiler's Comments

2003 Amendment: Chapter 257 in (1) inserted fifth sentence allowing a court to enter a judgment not to exceed three times profits and damages and attorney fees under certain circumstances; and made minor changes in style. Amendment effective July 1, 2003.

Case Notes

Venue When No Mandatory Penalty Exists — Trademark Infringement: Plaintiff corporation brought a trademark infringement action in Gallatin County. Defendant corporation sought a change of venue to Cascade County because defendant resided there and because any alleged tort occurred there. The District Court applied 25-2-124 and determined that because this section imposed a statutory penalty for trademark infringement, venue was proper in Gallatin County as the place where the cause or some part of the cause arose. Defendant appealed on grounds that the court should have applied 25-2-122 because the claims were based in tort and because any alleged tort would have been committed in defendant's business offices in Cascade County where the decision to use the trademark originated. The Supreme Court found that the penalty in this section was optional and at the discretion of the trial court, rather than mandatory. Because the statute failed to exact punishment, it was error for the District Court to apply 25-2-124 to determine venue because a statutory penalty was not imposed. The Supreme Court then addressed defendant's argument that any alleged tort was committed in Cascade County. Pursuant to the holding in BHC Holding Co. v. Hurley, 242 M 4, 788 P2d 322 (1990), tort is committed, for purposes of determining venue, where there is a concurrence of breach of obligation and the occasion of damages. Defendant may have made the decision to use the trademark at its offices in Cascade County, making Cascade County a proper venue for the case, but that action simply started in motion defendant's duty not to interfere with plaintiff's business. The alleged breach reached fruition when defendant widely distributed its products containing the allegedly illegal trademark to the marketplace, including Gallatin County, the location of plaintiff's principal place of business and the place where plaintiff allegedly suffered lost profits and other related damages. Thus, the concurrence of breach of obligation and the occasion of damages occurred in Gallatin County, rendering Gallatin County a proper venue. Therefore, even though the District Court improperly applied 25-2-124, its determination that Gallatin County was a proper venue was legally correct under 25-2-122, so the District Court was affirmed. Circle S Seeds of Mont., Inc. v. Mont. Merchandising, Inc., 2006 MT 311, 335 M 16, 157 P3d 671 (2006).

30-13-337. Forum for actions regarding registration — service on out-of-state registrants.

Compiler's Comments

Code Commissioner Correction: In (2) substituted "Rule 4(c)(2)(C), (c)(2)(D), and (d) through (s)" for "Rule 4D" to reflect revisions adopted by Supreme Court Order No. AF 07-0157 dated April 26, 2011.

Effective Date: Section 18, Ch. 257, L. 2003, provided that this section is effective July 1, 2003.

30-13-338. Trademark counterfeiting — presumption — penalties — restitution — forfeiture.

Compiler's Comments

2011 Amendment: Chapter 19 in (1)(b) after "25" deleted brackets around "items of". Amendment effective October 1, 2011.

Effective Date: Section 5, Ch. 177, L. 2009, provided that this section is effective July 1, 2009.

Code Commissioner Correction: The Code Commissioner inserted the bracketed language in (1)(b) to improve grammar.

30-13-342. Political party central committee marks.

Compiler's Comments

Effective Date: Section 9(2), Ch. 198, L. 2019, provided that this section is effective on passage and approval. Approved April 25, 2019.

Retroactive Applicability: Section 10, Ch. 198, L. 2019, provided: "[Sections 2 through 6] [13-38-106, 13-38-107, 13-38-202, 30-13-219, and 30-13-342] apply retroactively, within the meaning of 1-2-109, to August 1, 2018."

Preamble: The preamble attached to Ch. 198, L. 2019, provided: "WHEREAS, the office of committee representative is a position created by the Montana Legislature pursuant to section 13-38-201, MCA; and

WHEREAS, the committee representatives in each precinct constitute the city or county central committee of their respective political parties; and

WHEREAS, the Legislature has delegated the power of the State of Montana to party central committees to participate in the process of filling vacancies for legislative and county commission positions; and

WHEREAS, the State of Montana has the power to regulate political parties to ensure elections are orderly, fair, and honest; and

WHEREAS, other courts have recognized that when a state delegates power to a political party committee to fill vacancies, the state may require compliance with state law; and

WHEREAS, the State of Montana has an interest in limiting opportunities for fraud and corruption by party leadership; and

WHEREAS, the Montana Supreme Court has recognized the power to intervene in the affairs of a political party when the rights of individuals are involved; and

WHEREAS, the enactment of secret rules governing committee representatives, the use of fraudulent proxies of committee representatives, the arbitrary removal of committee representatives, and the filing of false trade and service marks with the Montana Secretary of State are fraudulent and corrupt practices; and

WHEREAS, the enactment of secret rules governing committee representatives, the use of fraudulent proxies of committee representatives, and the removal of committee representatives before the conclusion of a term may result in a disorderly, unfair, and dishonest election to fill a vacancy in a legislative or county commission position; and

WHEREAS, it is in the interest of the State of Montana to prevent fraud and corruption and to ensure fair, honest, and orderly elections conducted by committee representatives and to protect the rights of individuals by setting clear expectations and guidelines for the office of committee representative."

Severability: Section 8, Ch. 198, L. 2019, was a severability clause.

CHAPTER 14
UNFAIR TRADE PRACTICES AND CONSUMER PROTECTION

Chapter Compiler's Comments

Similarity to Uniform Law: This chapter is substantially similar to the Uniform Unfair Trade Practices and Consumer Protection Law, which may be found in 29 Suggested State Legislation 141 (1972).

Chapter Administrative Rules

Title 23, chapter 19, ARM Consumer Protection Office.

Chapter Case Notes

Claims Under Unfair Trade Practices Act Subject to Statute of Limitations on Actions for Constructive Fraud: As a liability created by statute that is neither a penalty nor a statutory debt, claims brought under the Montana Unfair Trade Practices and Consumer Protection Act of 1973 are subject to the 2-year statute of limitations in 27-2-211. Osterman v. Sears, Roebuck & Co., 2003 MT 327, 318 M 342, 80 P3d 435 (2003), following Royal Ins. Co. v. Roadarmel, 2000 MT 259, 301 M 508, 11 P3d 105 (2000).

Exercise of Ordinary Diligence Required in Discovery of Unfair Trade Practices Constituting Fraud for Tolling Statute of Limitations: For purposes of tolling the statute of limitations in an action for fraud or unfair trade practices, ordinary diligence must be exercised by the aggrieved party in discovery of the facts constituting the fraud or deceptive practice. Pursuant to Johnson v. Barrett, 1999 MT 176, 295 M 254, 983 P2d 925 (1999), the test is whether the plaintiff has information of circumstances sufficient to put a reasonable person on inquiry or has the opportunity to obtain knowledge from sources open to the plaintiff's investigation. Mere ignorance of the facts will not suffice to toll the statute of limitations. In this case, plaintiff filed an unfair trade practices complaint about 2 years and 9 months after entering an agreement with defendant siding installer, believing at the time that the contract was with the defendant company that manufactured the siding. However, plaintiff showed no affirmative conduct by either defendant that was calculated to obscure the existence of a cause of action, nor were the facts giving rise to the alleged fraud concealed. Thus, plaintiff discovered or should have discovered the facts constituting the alleged fraud when the contract was entered more than 2 years prior to filing suit, so the claim was barred by the 2-year statute of limitations in 27-2-211. Osterman v. Sears, Roebuck & Co., 2003 MT 327, 318 M 342, 80 P3d 435 (2003).

Provisions of Act Not Applicable — Attorney Fees Proper: The District Court found that the provisions of the Montana Unfair Trade Practices and Consumer Protection Act of 1973 were inapplicable to the subject of this case but that pursuant to the Act the defendant, as prevailing party, was entitled to reasonable attorney fees under 30-14-133. Appellant contended that since the Act did not apply, award of attorney fees was not appropriate. The Supreme Court affirmed the award, noting that defendant prevailed on the main issue in controversy and that since the action was brought under the Act, reasonable attorney fees were proper. Dillree v. Devoe, 223 M 47, 724 P2d 171, 43 St. Rep. 1521 (1986).

Applicability of Chapter Where No Fraud, Duress, or Undue Influence Present: Attorney, minutes before he was to defend client on criminal charges, threatened to withdraw as counsel unless client executed security agreement and quitclaim deed as security for attorney's fee. Attorney had given the instruments to client weeks before trial, but client had failed to execute them. No fraud, duress, or undue influence was found. Under these facts, this chapter has no application. Matthews v. Berryman, 196 M 49, 637 P2d 822, 38 St. Rep. 2112 (1981).

Part 1
Consumer Protection Act

Part Compiler's Comments

Severability Clause: Section 18, Ch. 275, L. 1973, read: "If any provision of this act is declared unconstitutional, or the application to any person or circumstances is held invalid, the constitutionality of the remainder of the act and its applicability to other persons and circumstances is not affected."

Part Case Notes

Summary Judgment Appropriate When Issues Raised for First Time on Appeal — No Evidence Presented Showing That Operation of Day-Care Service Without License Caused Financial Harm. Kostelecky v. Peas in a Pod, LLC, 2022 MT 195, 410 Mont. 239, 518 P.3d 840.

Failure to Disclose City Zoning Ordinance, Water and Mold Damage Alleged — Negligence, Constructive Fraud, and Consumer Protection Act Violations Alleged — Duty of Care for Real Estate Professionals. Young v. ERA Advantage Realty, 2022 MT 138, 409 Mont. 234, 513 P.3d 505.

Federal Supremacy Clause Not Violated — No Express or Conflict Preemption for Lawsuit Against Student Loan Servicer — State Claims Allowable: The plaintiff borrower filed suit against the defendant student loan servicer raising claims that the defendant violated the Montana Consumer Protection Act, was negligent in its accounting of his student loan payments, engaged in deceit, negligent misrepresentation, or constructive fraud, and breached the implied covenant of good faith and fair dealing. The District Court dismissed the plaintiff's complaint against the defendant under the supremacy clause of the United States Constitution and determined the claim was expressly preempted by the federal Higher Education Act of 1965, 20 U.S.C. 1098g. On appeal, the Supreme Court reversed, holding that the defendant's claims were not expressly preempted by 20 U.S.C. 1098g and that the defendant's claims were not preempted under a theory of conflict preemption. Reavis v. Pennsylvania Higher Educ. Assistance Agency, 2020 MT 181, 400 Mont. 424, 467 P.3d 588.

Denial of Motion to Amend Filed Within Motions Deadline — Abuse of Discretion — Judgment Vacated: The plaintiff, a financial services company, financed the defendant's purchase of a fifth-wheel trailer from a dealership. Although the dealership had told the defendant that the trailer was brand new, it required thousands of dollars in repairs shortly after she purchased it. After the defendant stopped making payments on the trailer, the plaintiff subsequently filed a lawsuit seeking possession of the trailer based on the loan's default. The dealership later joined in the lawsuit as a third-party defendant. After the plaintiff filed a motion for summary judgment, the plaintiff moved to amend her pleading within the motions deadline. However, the District Court denied the motion, finding that it would unduly prejudice the dealership, and issued a judgment in favor of the dealership. On appeal, the Supreme Court reversed and vacated the judgment, noting that the dealership could not claim undue prejudice because it had not filed a motion for summary judgment and holding that the District Court had abused its discretion in not allowing the defendant to amend her pleading. Ally Financial, Inc. v. Stevenson, 2018 MT 278, 393 Mont. 332, 430 P.3d 522, followed in Diana's Great Idea, LLC v. Jarrett, 2020 MT 199, 401 Mont. 1, 471 P.3d 38.

Alleged Misrepresentations Not False at Time They Were Made — Montana Consumer Protection Act — Negligent Misrepresentation: The plaintiff purchased a home from the defendant based on representations that the Yellowstone Club would build ski-out access. After the plaintiff purchased the home, the Yellowstone Club declared bankruptcy and the ski-out access was not constructed as planned. The plaintiff sued the defendant, alleging breach of contract, negligent misrepresentation, and violation of the Montana Consumer Protection Act. The District Court granted summary judgment to the defendant on the contract claims; however, after a bench trial, it found for the plaintiff on the remaining claims. On appeal, the defendant argued that at the time the statements were made, they were not false because the Yellowstone Club had intended to construct the access and the bankruptcy was unanticipated. The Supreme Court agreed with the defendant, holding that both the negligent misrepresentations and the Consumer Protection Act claims required that the defendant's statements must be false at the time they were made. WLW Realty Partners, LLC v. Continental Partners VIII, LLC, 2015 MT 312, 381 Mont. 333, 360 P.3d 1112.

Montana Consumer Protection Act Claims for Billing on Uncompleted Construction — Expert Evidence Unnecessary: The defendant started construction on an addition to the plaintiff's home in 2011. Before the addition was completed, the defendant left the job and then allegedly overbilled the plaintiff for the work. Ultimately, the plaintiff sued the defendant under the Montana Consumer Protection Act (MCPA). The District Court granted the defendant summary judgment because the plaintiff did not offer expert testimony. On appeal, the plaintiff argued that expert testimony regarding the defendant's billing for the project was not required. The Supreme Court agreed and remanded the case to the District Court to allow that portion of the MCPA to proceed. Hein v. Sott, 2015 MT 196, 380 Mont. 85, 353 P.3d 494.

Motion to Amend Judgment Improperly Denied — Judgment Against Estate Reduced to Policy Limits of Decedent: The plaintiff filed a lawsuit against the decedent's estate for injuries sustained from a vehicle driven by the estate's decedent. The complaint was filed 15 months after the estate had filed a notice to creditors pursuant to 72-3-801. After a jury awarded the plaintiff $400,000, the estate filed a motion to reduce the amount of damages to $100,000, which was the limit of the decedent's insurance policy. The District Court denied the motion. On appeal, the Supreme Court affirmed in part, finding that the plaintiff could not recover more than $100,000 from the estate itself but could instead try to collect the remainder from the decedent's insurance company under the Montana Unfair Trade Practices Act. The Supreme Court vacated the judgment and remanded the matter to the District Court to issue an order barring the plaintiff from recovering more than $100,000 from the estate. Locke v. Estate of Davis, 2015 MT 141, 379 Mont. 256, 350 P.3d 33.

Montana Consumer Protection Act — No Federal Fair Credit Reporting Act Preemption: After the defendant bank acknowledged that the charges on the plaintiff's credit card were unauthorized and that the plaintiff was not personally liable for the charges, the defendant bank, nonetheless, referred the plaintiff's account to a collection agency. The plaintiff filed suit under the Montana Consumer Protection Act (MCPA). The District Court found that the defendant bank was entitled to judgment on the pleadings on the basis that the plaintiff's MCPA claim was preempted by the federal Fair Credit Reporting Act, 15 U.S.C. 1681-1681x (FCRA). The Supreme Court reversed. Although the FCRA authorizes federal preemption when a financial institution, in the ordinary course of business, furnishes information to a "consumer reporting agency", 15 U.S.C. 1681s-2, the preemption provision did not apply to the plaintiff's MCPA claim because the defendant bank was not furnishing information to a "consumer reporting agency" but, rather, was furnishing information to a collection agency. Curtis v. Citibank (S. Dak.), N.A., 2011 MT 247, 362 Mont. 211, 261 P.3d 1059.

Negligence Compared With Violation of Consumer Protection Act: The jury found the defendant violated the Consumer Protection Act and was negligent. The trial court applied the comparative negligence statute to reduce the plaintiffs' recovery under the Act. On appeal, the Supreme Court affirmed the reduction of damages, stating that the law as stated in the jury instructions does not allow the separation of the defendant's actions in violation of the Consumer Protection Act from its actions that were negligent. Evans v. Teakettle Realty, 226 M 363, 736 P2d 472, 44 St. Rep. 723 (1987).

Public Service Commission Exempt From Consumer Protection Act: The plain meaning of 30-14-105 is that actions and transactions of the Public Service Commission, acting under its statutory authority, are exempt from the Consumer Protection Act. Rozel Corp. v. Dept. of Public Service Regulation, 226 M 237, 735 P2d 282, 44 St. Rep. 618 (1987).

No Individual Cause of Action Concerning Goods Purchased for Business Rather Than for Personal, Family, or Household Purposes: When uncontradicted testimony established that a machine had been purchased for use in respondents' business, respondents did not fall within the class of persons who may bring a private action under 30-14-133. Doll v. Major Muffler Centers, Inc., 208 M 401, 687 P2d 48, 41 St. Rep. 429 (1984).

Part Law Review Articles

Pay Attention! Marginalized Communities, the Consumer Financial Protection Bureau, and Regulatory Advocacy, Thompson, 82 Mont. L. Rev. 343 (2021).

Morrow v. Bank of America, Further Developments in Consumer Law in Montana and Their Impact on Consumers in the Age of COVID-19, Wilson & McCulloch, 82 Mont. L. Rev. 193 (2021).

The Erosion of Equity and the Attack on the FTC's Redress Authority, Vladeck, 82 Mont. L. Rev. 159 (2021).

Is the CFPB Still on the Beat? The CFPB's (Non)Response to the COVID-19 Pandemic, Cowie, 82 Mont. L. Rev. 41 (2021).

One Short of a Load: Why an Illinois Brick Repealer Will Increase Private Antitrust Enforcement in Montana, Price, 74 Mont. L. Rev. 399 (2013).

Big Interest Rates Under the Big Sky: The Case for Payday and Title Lending Reform in Montana, Lundberg, 68 Mont. L. Rev. 181 (2007).

Part Collateral References

Office of Consumer Protection, Montana Department of Justice, https://dojmt.gov/consumer.

30-14-102. Definitions.

Compiler's Comments

2021 Amendment — Code Commissioner Correction: Chapter 262 in definition of trade and commerce inserted (b) concerning direct patient care agreements established pursuant to 50-4-107; and made minor changes in style. Amendment effective October 1, 2021.

Chapter 262 in (8)(b) referred to "[section 1]". However, the apparent intent of the original bill was to refer to sec. 2, Ch. 262, and the Code Commissioner has changed the final statutory reference in (8)(b) accordingly.

2007 Amendment: Chapter 331 in definition of gift certificate in (a) near beginning after "gift card" inserted "or stored value card"; and made minor changes in style. Amendment effective April 27, 2007.

Effective Date — Retroactive Applicability: Section 4, Ch. 331, L. 2007, provided: "[This act] is effective on passage and approval and applies retroactively, within the meaning of 1-2-109, to gift certificates issued or sold after September 30, 2005." Approved April 27, 2007.

2005 Amendments — Composite Section: Chapter 280 in definition of department substituted "department of justice" for "department of administration" and substituted "2-15-2001" for "2-15-1001". Amendment effective July 1, 2005.

Chapter 291 inserted definitions of gift certificate and possessor; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 4, Ch. 291, L. 2005, was a saving clause.

2003 Amendment: Chapter 322 inserted definition of consumer; deleted definition of national advertising that read: ""National advertising" means any advertising run simultaneously in five or more states and over which a local advertiser has no control"; and made minor changes in style. Amendment effective April 15, 2003.

2001 Amendment: Chapter 483 in definition of department substituted reference to department of administration for reference to department of commerce and substituted "2-15-1001" for "2-15-1801"; and made minor changes in style. Amendment effective July 1, 2001.

1981 Amendment: Substituted "department of commerce" for "department of business regulation" in (1).

Case Notes

Consumer Protection Act Not Applicable to Negligence or Malpractice Claims Against Hospital: The plaintiff sued a hospital under the Consumer Protection Act for negligence in credentialing the doctor who delivered her baby. The Supreme Court affirmed the District Court's dismissal of the claim on the basis that the Act applies only to entrepreneurial, commercial, or business aspects of running a hospital. Brookins v. Mote, 2012 MT 283, 367 Mont. 193, 292 P.3d 347. See also Hastie v. Alpine Orthopedics & Sports Medicine, 2015 MT 346, 382 Mont. 21, 363 P.3d 435.

Publicly Filed Floodplain Study Not Considered Trade Secret — Denial of Injunction to Prohibit Copying of Study Proper: Plaintiff conducted a floodplain study that was filed with the city of Kalispell as part of a property development permit request. Owners of nearby property sought to review and copy the study. The city allowed review of the study, but the request for a copy was denied without permission of plaintiff. Plaintiff denied the copy request and sought an injunction to prohibit the city from providing copies of the study, but the request for an injunction was denied, so plaintiff appealed, citing trade secrets and copyright protection. The Supreme Court noted that a trade secret must be the subject of reasonable efforts to maintain its secrecy. However, the study document was readily ascertainable by anyone who wished to view it, so plaintiff could not argue that the study was a confidential trade secret. Further, plaintiff failed to show that the contemplated use of the data would violate copyright law. Last, plaintiff argued that the District Court failed to engage in the constitutional balancing analysis required in 2-6-102 (now repealed), but the Supreme Court held that plaintiff did not establish any individual privacy or property interest that could be balanced against the merits of public disclosure. Thus, denial of the injunction request was affirmed. Billmayer v. Kalispell, 2007 MT 116, 337 M 242, 160 P3d 869 (2007).

Jury Instruction Regarding Contractor's Involvement in Trade or Commerce — Waiver of Defense by Failure to Include in Final Pretrial Order: Defendant objected to a jury instruction stating defendant's involvement in trade or commerce, contending that that determination and the applicability of the Consumer Protection Act to his business were questions of fact for the jury. However, the final pretrial order did not contain any factual issue, legal theory, or defense that defendant was contesting the applicability of the Montana Unfair Trade practices and Consumer Protection Act of 1973 to his business, so that theory or defense was waived as an issue to be determined by the trier of fact at trial. The Supreme Court found that the agreed facts in the pretrial order supported a determination that defendant was in fact engaged in trade or commerce, as defined in this section, so giving of a jury instruction to that effect was not in error. Plath v. Schonrock, 2003 MT 21, 314 M 101, 64 P3d 984 (2003).

Consumer Loan by Bank Covered by Act: Because the Montana Unfair Trade Practices and Consumer Protection Act of 1973 is in derogation of the common law, it should be liberally construed with a view to effect its object and to promote justice. The approach to defining what is meant by the word "services" should be broad in scope. The Act applies to a consumer loan by a bank. Baird v. Norwest Bank, 255 M 317, 843 P2d 327, 49 St. Rep. 1026 (1992).

30-14-103. Unlawful practices.

Administrative Rules

ARM 23.19.507 State do-not-call database.

Case Notes

No Ascertainable Loss — Claim for Unfair or Deceptive Practices Fails: A health care provider issued refunds for overpayment to a patient on two occasions by mailing prepaid debit cards issued through a bank in the amount of the refund due. The patient activated the first card but did not use either card to pay for goods, withdraw money at an ATM, or exchange the cards for cash at a bank. The patient sued the health care provider for, among other claims, violations of the Montana Consumer Protection Act. The District Court found that the patient had not suffered an ascertainable loss because the health care provider first issued the debit cards and later issued checks for the full refund due. Because the prerequisite of having suffered an ascertainable loss was not met, the District Court granted summary judgment to the health care provider on the Montana Consumer Protection Act claims. The Supreme Court affirmed. Bratton v. Sisters of Charity of Leavenworth Health Sys., 2020 MT 86, 399 Mont. 490, 461 P.3d 127.

Relationship Between Bank and Customer Generally Does Not Give Rise to Fiduciary Duty: The District Court entered summary judgment for a bank in a convoluted contracts and tax case. The plaintiff appealed on the basis that the bank violated the Consumer Protection Act by breaching a duty and negligently servicing the loan. The Supreme Court affirmed entry of summary judgment, noting that a bank generally does not owe a fiduciary relationship to its customer unless it actively advises customers in the conduct of their affairs. Graham-Rogers v. Wells Fargo Bank, N.A., 2019 MT 226, 397 Mont. 262, 449 P.3d 798.

Tort, Fraud, Negligence, and Montana Unfair Trade Practices Act Claims Related to Faulty Water System — Statute of Limitations Runs From Notice of Problems, Not Upon Attempted Sale of Home — Claims Time-Barred: The plaintiffs were homeowners who had numerous water-related issues with their home, including having no water, intermittent flooding, and insufficient water pressure. When they went to sell the home, they learned it did not qualify for conventional financing because of water violations issued by the Department of Environmental Quality (DEQ). The plaintiffs then filed tort and unfair trade practices claims against the county, the DEQ, and an engineering firm. The District Court granted the defendants summary judgment, concluding that the plaintiffs had been on notice of the problems since the home was built and that the statute of limitations had run on their claims. On appeal, the Supreme Court agreed that the statute of limitations began to run when the plaintiffs first learned their home had issues with its water system and not when they learned that the house did not qualify for conventional financing. Norbeck v. Flathead County, 2019 MT 84, 395 Mont. 294, 438 P.3d 811.

Violation Under MCPA — Sufficiency of Pleading: A mortgagee obtained a loan for a residential property and fell behind on payments. The mortgagee contacted the bank for assistance to modify her monthly payments, and alleged that the bank instructed her to stop making monthly mortgage payments in order to qualify for a loan assistance program. The mortgagee stopped making payments but never qualified for the assistance program. The mortgagee defaulted on the loan but continued to reside on the property. The mortgagee received at least nine notices of sale over an 8-year period, each of which, the mortgagee alleged, accelerated all amounts due. The deed of trust contained a provision stating the procedure that the lender was required to follow to provide notice to the mortgagee prior to accelerating the loan. As a result, the mortgagee sued, alleging six causes of action, one of which was violations under the Montana Consumer Protection Act (MCPA). The District Court dismissed the mortgagee's claim of violations of the MCPA. Relying on similarities to Jacobson v. Bayview Loan Servicing, LLC, 2016 MT 101, 383 Mont. 257, 371 P.3d 397, the Supreme Court reversed, finding that an MCPA violation had been sufficiently pleaded so as to survive a Rule 12(b)(6), M.R.Civ.P. (Title 25, ch. 20), motion by the mortgagee's allegation of a violation of provisions of the trust indenture. Puryer v. HSBC Bank USA, 2018 MT 124, 391 Mont. 361, 419 P.3d 105.

Choice of Law — Deceptive Acts or Practices — Inapplicable to Counterclaims Governed by New York Law: This section was inapplicable because the defendant's counterclaims were subject to New York law, and although New York has a similar prohibition on deceptive acts or practices, the defendant did not allege a violation of New York law. HSBC Bank USA, N.A. v. Anderson, 2017 MT 257, 389 Mont. 106, 406 P.3d 416.

District Court's Findings Under Fair Debt Collection Practices Act — Establishment of State Law Grounds for Violations of Montana Consumer Protection Act: The defendant's false assignments and surrounding misrepresentations and conduct were unfair and deceptive practices under the Montana Consumer Protection Act (MCPA). The District Court's findings were supported by substantial evidence demonstrating liability under the MCPA. Jacobson v. Bayview Loan Servicing, LLC, 2016 MT 101, 383 Mont. 257, 371 P.3d 397.

Podiatrist Properly Excluded From Providing Testimony Regarding Doctor's Standard of Care — Consumer Protection Act Claims Properly Dismissed: The plaintiff sued the defendants, a doctor and his related medical business. The plaintiff alleged medical malpractice and violations of the Montana Consumer Protection Act (MCPA) violations stemming from the defendants' purported refusal to conduct further postoperative visits after his foot surgery. The plaintiff intended to call a podiatrist to testify to the standard of care. However, the District Court excluded the podiatrist because he was not a doctor of medicine or doctor of osteopathy as required in 26-2-601 and 37-3-102. The District Court then granted partial summary judgment on the MCPA claim because the legal theories were premised upon allegations of professional negligence. A jury found in favor of the defendant. On appeal, the Supreme Court affirmed, holding that the podiatrist did not meet statutory criteria to provide standard of care testimony and that the MCPA claims failed because the claim stemmed from the alleged acts of professional negligence. Hastie v. Alpine Orthopedics & Sports Medicine, 2015 MT 346, 382 Mont. 21, 363 P.3d 435.

Alleged Misrepresentations Not False at Time They Were Made — Montana Consumer Protection Act — Negligent Misrepresentation: The plaintiff purchased a home from the defendant based on representations that the Yellowstone Club would build ski-out access. After the plaintiff purchased the home, the Yellowstone Club declared bankruptcy and the ski-out access was not constructed as planned. The plaintiff sued the defendant, alleging breach of contract, negligent misrepresentation, and violation of the Montana Consumer Protection Act (MCPA). The District Court granted summary judgment to the defendant on the contract claims; however, after a bench trial, it found for the plaintiff on the remaining claims. On appeal, the defendant argued that at the time the statements were made, they were not false because the Yellowstone Club had intended to construct the access and the bankruptcy was unanticipated. The Supreme Court agreed with the defendant, holding that both the negligent misrepresentations and the MCPA claims required that the defendant's statements must be false at the time they were made. WLW Realty Partners, LLC v. Continental Partners VIII, LLC, 2015 MT 312, 381 Mont. 333, 360 P.3d 1112.

Dismissal Based on Expired Statute of Limitations Improper — Date Claims Accrued Unclear: Plaintiffs were radiologists who had contracted with the defendant hospital for a number of years to provide radiology services to its patients. After the hospital closed its radiology department to all nonemployee physicians in 2011, the plaintiffs filed a complaint alleging unfair trade practices and intentional interference with prospective advantage. The District Court granted the defendant's motion to dismiss the complaint as untimely, concluding that the statute of limitations started running from the time the parties' exclusive contract for services had expired, in 2009. On appeal, the Supreme Court reversed and remanded the case for further proceedings, holding that dismissal was improper because the Supreme Court could not determine from the pleadings when the plaintiffs' claims had accrued. Mont. Interventional & Diagnostic Radiology Specialists v. St. Peter's Hospital, 2015 MT 258, 381 Mont. 25, 355 P.3d 777.

Claims Under Montana Consumer Protection Act — Barred by Statute of Limitations: The defendant constructed a home for the plaintiff in 2001. Each winter after the home's construction, the plaintiff noticed water damage. Each time, the defendant would inspect the damage and report that he had repaired the problem. In 2012, the plaintiff hired a roofing contractor to inspect the roof and learned that the water damage was caused by improper ventilation of the roof, an issue never identified by the defendant. The plaintiff sued the defendant, alleging violations of the Montana Consumer Protection Act (MCPA), and argued that the statute of limitation should be tolled because the defendant's inspections had prevented him from discovering the cause of injury. The District Court dismissed the claim. On appeal, the Supreme Court reversed, finding that the District Court had erred in dismissing claims involving the MCPA that were alleged to have occurred within the 2 years prior to the lawsuit's filing date, and remanded to the District Court for further proceedings on the remaining claims. Hein v. Sott, 2015 MT 196, 380 Mont. 85, 353 P.3d 494.

Misleading Statements by Bank Concerning Loan Modification — Summary Judgment Reversed: After requesting a loan modification, plaintiffs alleged that the defendant bank instructed them to default on their existing real estate loan and make partial payments while keeping them in a servicing status that required full payments on the loan. The Supreme Court reversed the District Court's summary judgment for the bank and found that, if proven, these practices were sufficient to state a deceptive practice claim and show substantial injury to consumers. Morrow v. Bank of America, N.A., 2014 MT 117, 375 Mont. 38, 324 P.3d 1167, distinguished in House v. U.S. Bank Nat'l Ass'n, 2021 MT 45, 403 Mont. 287, 481 P.3d 820.

Conditional Right to Refinance — Mortgagee Failed to Comply With Terms — No Contract of Adhesion: The plaintiff signed a promissory note secured by a deed of trust. The note provided for a balloon payment at the end of its term and stated that the bank did not have an obligation to refinance. The note also provided a conditional right to refinance the loan. After the plaintiff failed to satisfy one of the terms for refinancing, the bank foreclosed. The plaintiff filed an action for damages under the Montana Consumer Protection Act and for quiet title to the property. The plaintiff argued that the provision regarding conditional refinancing constituted a contract of adhesion and that the bank's enforcement of it was unconscionable. The District Court granted summary judgment to the bank, and the plaintiff appealed. The Supreme Court affirmed, agreeing that the provisions regarding conditional refinancing of the note were clear and not misleading, especially given that the plaintiff was a realtor. Doherty v. Fed. Nat'l Mtg. Ass'n, 2014 MT 56, 374 Mont. 151, 319 P.3d 1279.

Definition of Unfair Act or Practice Under Consumer Protection Act: As a matter of law, as the term is used in the Montana Consumer Protection Act, an unfair act or practice is one that offends established public policy and that is immoral, unethical, oppressive, unscrupulous, or substantially injurious to consumers. Rohrer v. Knudson, 2009 MT 35, 349 M 197, 203 P3d 759 (2009), followed in Anderson v. ReconTrust Co., 2017 MT 313, 390 Mont. 12, 407 P.3d 692.

Question Whether Seller of Subdivision Lot Violated Consumer Protection Law — Remand: Plaintiffs sued the seller of a subdivision lot for violating the Montana Consumer Protection Act (MCPA) by failing to disclose that the lot contained uncontrolled fill material to a depth of about 31 feet below grade, which resulted in shifting of the foundation of plaintiffs' home, causing damages. The jury apportioned negligence of 10% to defendant, 45% to the city, and 45% to plaintiffs, and plaintiffs appealed. In determining whether the MCPA was violated, the Supreme Court held that the record contained conflicting evidence as to whether soil compaction and density studies were completed and that the studies were necessary to determine whether the seller offended established public policy and whether any unfair act or practice caused plaintiffs' damages warranting recovery under the MCPA. Therefore, the case was remanded for retrial. Rohrer v. Knudson, 2009 MT 35, 349 M 197, 203 P3d 759 (2009).

Electric Cooperative Requirement That New Customer Pay Prior Customer's Delinquent Bill Unreasonable: Granbois applied to have an electric cooperative provide service to her lot. However, the bylaws of the cooperative required that before she could receive service, Granbois pay the delinquent bill of the person who previously received service at the location. She paid the delinquent bill, began receiving service, and then brought an action against the cooperative on grounds that the policy violated unfair trade practices. Citing Howe v. Big Horn Elec. Co-op, 206 M 297, 670 P2d 936, 40 St. Rep. 1670 (1983), the Supreme Court held that the disparity in the relative positions of the cooperative and the consumer necessarily required the cooperative to deal reasonably with its members and that the policy requiring a new customer to either pay the predecessor's bill or go without electricity was an unreasonable restriction on Granbois's access to electric services. After determining that the case could proceed as an unfair trade practices action, the court remanded with instructions to refund Granbois the amount of the delinquent bill. Granbois v. Big Horn County Elec. Co-op, Inc., 1999 MT 222, 296 M 45, 986 P2d 1097, 56 St. Rep. 874 (1999).

Expert Testimony Unnecessary on Issue of Standard of Care — District Court Not Directed as to All Expert Testimony on All Claims: Durbins purchased a home through the seller's realtors. Contrary to the representations of the realtors, Durbins discovered that the property had no legal septic system, that the household water was unsafe to use for any purpose, and that the access road was located on the neighbor's property. Durbins brought an action against the realtors, alleging negligent misrepresentation, actual and constructive fraud, and statutory violations involving the Montana real estate licensing laws and the Montana Unfair Trade Practices and Consumer Protection Act of 1973. The defendants sought and achieved dismissal of the case on the grounds that Durbins failed to prove through expert testimony the applicable standard of care of the realtors. The Supreme Court held that expert witnesses were unnecessary to prove a standard of care. Durbins also asked that the Supreme Court direct the District Court to exclude testimony of any expert witnesses on any claim asserted by the Durbins. The Supreme Court noted that the District Courts have great latitude concerning the admissibility of evidence and that the District Court would in any event have to comply with Rule 702, M.R.Ev. (Title 26, ch. 10). The Supreme Court therefore declined to direct the District Court as requested by the Durbins. Durbin v. Ross, 276 M 463, 916 P2d 758, 53 St. Rep. 471 (1996).

Retention of Building Materials by Architects Not Violative of Professional Conduct or Consumer Protection Act: Architects who retained property and building materials from a building site after defendant failed to make contractual payments did not violate standards of professional conduct or commit unfair practices under the Montana Unfair Trade Practices and Consumer Protection Act of 1973. Taylor, Thon, Thompson & Peterson v. Cannaday, 230 M 151, 749 P2d 63, 45 St. Rep. 102 (1988).

No Proof of Misrepresentation by Car Salesman: When the plaintiff, a purchaser of a used truck, brought an action against defendant car salesman alleging that the condition of a truck had been misrepresented, the District Court did not err in ruling that the plaintiff failed to offer proof establishing that the truck did not conform to the representations made by the salesman. The defects discovered by the plaintiff were discoverable by reasonable inspection and none rendered the truck inoperable or presented a safety hazard. Emick v. Koch, 227 M 365, 739 P2d 947, 44 St. Rep. 1153 (1987).

Parallel Pricing as Insufficient Circumstantial Evidence of Restraint of Trade: Where the State brought an action against the defendant retail gasoline dealer, alleging that the defendant acted to restrain trade in the setting of gasoline prices, the federal District Court found that the defendant's actions of price following and parallel pricing were consistent with the defendant's own policies and self-interest, were a rational response to market conditions, were not accompanied by any evidence of other "plus factors" tending to show restraint of trade, and that the evidence of the defendant's pricing methods was therefore insufficient circumstantial evidence to show a violation of either state or federal law. St. v. SuperAmerica, 559 F. Supp. 298, 40 St. Rep. 944 (D.C. Mont. 1983).

Consumer Protection Act Violation Alleged as Cause of Accident — Agency Rule Not in Conflict With Federal Law — Summary Judgment: The District Court properly denied summary judgment on plaintiff's Court No. II, which claimed misrepresentation as to the odometer reading on a used car sold to her by defendant corporation as the proximate cause of her accident and subsequent injuries. A state agency rule adopted pursuant to 30-14-104 was not inconsistent with the rules and decisions of the FTC and decisions of the Federal Courts, although the rule deals with sales and the main purpose of the federal law is to prevent unlawful restraint of trade. Whether the alleged violation was a cause of plaintiff's damages was a jury issue. Kopischke v. First. Cont. Corp., 187 M 471, 610 P2d 668 (1980).

30-14-104. Federal interpretation — rules determining unfair competition and deception.

Administrative Rules

ARM 23.19.101 Unlawful acts or practices.

Title 23, chapter 19, subchapter 2, ARM Motor vehicles, sales, repairs, maintenance, and service.

ARM 23.19.507 State do-not-call database.

Case Notes

Alleged Misrepresentations Not False at Time They Were Made — Montana Consumer Protection Act — Negligent Misrepresentation: The plaintiff purchased a home from the defendant based on representations that the Yellowstone Club would build ski-out access. After the plaintiff purchased the home, the Yellowstone Club declared bankruptcy and the ski-out access was not constructed as planned. The plaintiff sued the defendant, alleging breach of contract, negligent misrepresentation, and violation of the Montana Consumer Protection Act (MCPA). The District Court granted summary judgment to the defendant on the contract claims; however, after a bench trial, it found for the plaintiff on the remaining claims. On appeal, the defendant argued that at the time the statements were made, they were not false because the Yellowstone Club had intended to construct the access and the bankruptcy was unanticipated. The Supreme Court agreed with the defendant, holding that both the negligent misrepresentations and the MCPA claims required that the defendant's statements must be false at the time they were made. WLW Realty Partners, LLC v. Continental Partners VIII, LLC, 2015 MT 312, 381 Mont. 333, 360 P.3d 1112.

Definition of Unfair Act or Practice Under Consumer Protection Act: As a matter of law, as the term is used in the Montana Consumer Protection Act, an unfair act or practice is one that offends established public policy and that is immoral, unethical, oppressive, unscrupulous, or substantially injurious to consumers. Rohrer v. Knudson, 2009 MT 35, 349 M 197, 203 P3d 759 (2009).

Permitted Delegation of Legislative Authority: This section prescribes with reasonable clarity the limits of power delegated to the state administrative agency in defining unlawful or deceptive practices in trade and commerce and does not represent an unconstitutional delegation of legislative power to either the state administrative agency or to the Federal Trade Commission and the federal courts, whose determinations the state agency is empowered but not required to adopt. T & W Chevrolet v. Darvial, 196 M 287, 641 P2d 1368, 39 St. Rep. 112 (1982).

Consumer Protection Act Violation Alleged as Cause of Accident — Agency Rule Not in Conflict With Federal Law — Summary Judgment: The District Court properly denied summary judgment on plaintiff's Court No. II, which claimed misrepresentation as to the odometer reading on a used car sold to her by defendant corporation as the proximate cause of her accident and subsequent injuries. A state agency rule adopted pursuant to 30-14-104 was not inconsistent with the rules and decisions of the FTC and decisions of the Federal Courts, although the rule deals with sales and the main purpose of the federal law is to prevent unlawful restraint of trade. Whether the alleged violation was a cause of plaintiff's damages was a jury issue. Kopischke v. First. Cont. Corp., 187 M 471, 610 P2d 668 (1980).

30-14-105. Exemptions.

Compiler's Comments

2003 Amendment: Chapter 322 in (1) at end inserted reference to the state auditor and deleted "acting under statutory authority of this part or the United States"; in (2) after "when the" inserted "merchant, publisher" and at end deleted "and did not have a direct financial interest in the advertised product or service"; deleted (3) that read: "(3) national advertising"; and made minor changes in style. Amendment effective April 15, 2003.

Case Notes

Public Service Commission Exempt From Consumer Protection Act: The plain meaning of this section is that actions and transactions of the Public Service Commission, acting under its statutory authority, are exempt from the Consumer Protection Act. Rozel Corp. v. Dept. of Public Service Regulation, 226 M 237, 735 P2d 282, 44 St. Rep. 618 (1987).

30-14-108. Termination of gift certificate prohibited — fee limitation — redemption — posting required.

Compiler's Comments

Saving Clause: Section 4, Ch. 291, L. 2005, was a saving clause.

Effective Date: This section is effective October 1, 2005.

30-14-111. Department to restrain unlawful acts.

Compiler's Comments

2021 Amendment: Chapter 535 in (3) at end inserted "if the person is not a resident of this state or does not maintain a place of business in this state". Amendment effective October 1, 2021.

2003 Amendment: Chapter 322 in (3) after "principal place of business or" deleted "with consent of the parties, may be brought"; and made minor changes in style. Amendment effective April 15, 2003.

30-14-112. Assurance of compliance.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-14-113. Investigative demand.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-14-114. Department authority.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-14-121. Duties of county attorney.

Compiler's Comments

2005 Amendment: Chapter 280 at beginning of second sentence after "county attorney" deleted "or the attorney general"; near middle of third sentence substituted "county attorney alone, the county attorney shall" for "county attorney alone or the attorney general on request of the county attorney, the person prosecuting shall"; in middle of last sentence substituted "county attorney shall report on the action" for "county attorney or attorney general shall make a report thereon"; and made minor changes in style. Amendment effective July 1, 2005.

30-14-122. Employment of investigator by county attorney.

Compiler's Comments

2011 Amendment: Chapter 128 substituted "counties having a taxable valuation of $30 million or more" for "first- and second-class counties". Amendment effective July 1, 2011.

30-14-131. Restoration — court orders.

Compiler's Comments

2005 Amendment: Chapter 280 inserted (2) relating to award of attorney fees; and made minor changes in style. Amendment effective July 1, 2005.

2003 Amendment: Chapter 322 inserted (2) relating to an equitable order or judgment; and made minor changes in style. Amendment effective April 15, 2003.

30-14-132. Powers of receiver — proof of damages — jurisdiction.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-14-133. Damages — limitation on residential construction disputes — notice to public agencies — attorney fees — prior judgment as evidence.

Compiler's Comments

2021 Amendments — Composite Section: Chapter 46 in (1)(a) at beginning of first sentence inserted exception clause; inserted (1)(b) precluding consumer protection actions if construction dispute actions are brought; and made minor changes in style. Amendment effective October 1, 2021.

Chapter 521 in (1) near middle of first sentence after "may bring an individual" inserted "action", near end of first sentence substituted "money damages in the amount of any ascertainable loss of money or property" for "actual damages", and substituted current last sentence concerning the awarding of money damages for former last sentence that read: "The court may, in its discretion, award up to three times the actual damages sustained and may provide any other equitable relief that it considers necessary or proper"; in (3) at end of first sentence added exception clause and inserted second sentence limiting attorney fees to no more than $250 an hour; and made minor changes in style. Amendment effective October 1, 2021.

2003 Amendment: Chapter 322 in (1) in first sentence substituted "A consumer who" for "Any person who purchases or leases goods or services primarily for personal, family, or household purposes and thereby", after "lessor" inserted "or service provider", and increased amount of damages from $200 to $500 and inserted second sentence allowing an individual claim in justice's court; in (3) inserted second sentence relating to an action brought without an attorney; and made minor changes in style. Amendment effective April 15, 2003.

Case Notes

No Ascertainable Loss — Claim for Unfair or Deceptive Practices Fails: A health care provider issued refunds for overpayment to a patient on two occasions by mailing prepaid debit cards issued through a bank in the amount of the refund due. The patient activated the first card but did not use either card to pay for goods, withdraw money at an ATM, or exchange the cards for cash at a bank. The patient sued the health care provider for, among other claims, violations of the Montana Consumer Protection Act. The District Court found that the patient had not suffered an ascertainable loss because the health care provider first issued the debit cards and later issued checks for the full refund due. Because the prerequisite of having suffered an ascertainable loss was not met, the District Court granted summary judgment to the health care provider on the Montana Consumer Protection Act claims. The Supreme Court affirmed. Bratton v. Sisters of Charity of Leavenworth Health Sys., 2020 MT 86, 399 Mont. 490, 461 P.3d 127.

Ascertainable Loss of Money or Property — Sufficiency of Pleading: A mortgagee obtained a loan for a residential property and fell behind on payments. The mortgagee contacted the bank for assistance to modify her monthly payments, and alleged that the bank instructed her to stop making monthly mortgage payments in order to qualify for a loan assistance program. The mortgagee stopped making payments but never qualified for the assistance program. The mortgagee defaulted on the loan but continued to reside on the property. The mortgagee received at least nine notices of sale over an 8-year period, each of which, the mortgagee alleged, accelerated all amounts due. The deed of trust contained a provision stating the procedure that the lender was required to follow to provide notice to the mortgagee prior to accelerating the loan. As a result, the mortgagee sued, alleging six causes of action, one of which was violations under the Montana Consumer Protection Act (MCPA). The District Court dismissed the mortgagee's MCPA claim in part because it concluded that the mortgagee had failed to allege any ascertainable loss of money and property as a result of the bank's unfair practices. On appeal, the Supreme Court reversed, finding that by alleging damages of "cost and fees, attorney fees, and ascertainable loss of money and property by executing a legal proceeding to stop" the foreclosure of the property, the mortgagee had established an ascertainable loss of money or property for the purpose of 30-14-133. Puryer v. HSBC Bank USA, 2018 MT 124, 391 Mont. 361, 419 P.3d 105.

Purchase in Yellowstone County — Delivery of Purchased Item in Chouteau County — Venue Proper in Chouteau County: The defendant purchased a fifth-wheel trailer from an RV dealership located in Billings. The dealership's principal corporate office was located in Bozeman. The plaintiff, a financial company, financed the trailer's purchase. The RV dealership delivered the trailer to the plaintiff's home in Fort Benton, in Chouteau County. After the defendant later defaulted on her loan, the plaintiff filed a claim in Chouteau County. The defendant filed her answer, as well as a third-party complaint against the dealership for negligence and violations of the Montana Consumer Protection Act. The third-party defendant filed a motion to change venue to Yellowstone County, arguing that the delivery of the trailer to the defendant's residence was insufficient to confer venue to Chouteau County under 30-14-133. The District Court denied the motion, and the third-party defendant appealed to the Supreme Court. The Supreme Court affirmed, ruling that the delivery of the purchased good to Chouteau County was sufficient to confer venue that county. Ally Financial, Inc., v. Stevenson, 2017 MT 190, 388 Mont. 246, 399 P.3d 899.

Subject Matter Jurisdiction Challenged — Venue, Not Jurisdiction, Conferred by Cited Statute — Venue Proper: The defendant purchased a fifth-wheel trailer from an RV dealership located in Billings. The dealership's principal corporate office was located in Bozeman. The plaintiff, a financial company, financed the trailer's purchase. The RV dealership delivered the trailer to the defendant's home in Fort Benton, in Chouteau County. After the defendant later defaulted on her loan, the plaintiff filed a claim in Chouteau County. The defendant filed her answer, as well as a third-party complaint against the dealership for negligence and violations of the Montana Consumer Protection Act. The third-party defendant filed a motion for judgment on the pleadings because the District Court lacked subject matter jurisdiction over the consumer protection claim pursuant to 30-14-133. Following denial of the motion, the third-party defendant appealed to the Supreme Court, which affirmed. The court held that 30-14-133 confers not jurisdiction but venue and that venue was proper in Chouteau County. Ally Financial, Inc., v. Stevenson, 2017 MT 190, 388 Mont. 246, 399 P.3d 899.

District Court Properly Awarded Damages for Violations of Montana Consumer Protection Act: The damages awarded by the District Court were well supported by substantial evidence and within the court's discretion. Jacobson v. Bayview Loan Servicing, LLC, 2016 MT 101, 383 Mont. 257, 371 P.3d 397.

Attorney Fees in Favor of Defendant Affirmed — Inappropriate Hindsight Reasoning Not Applied: The owner of a large lodge claimed the defendant violated the Montana Consumer Protection Act by selling him allegedly defective flooring. Following a verdict in favor of the defendant flooring company, the defendant requested attorney fees, which the District Court awarded and the Supreme Court affirmed. The Supreme Court held that although rare, there are times when it is appropriate to award attorney fees to ensure that the MCPA is not abused and held further that the District Court did not engage in inappropriate hindsight reasoning by relying on evidence to resolve a question of fact. B Bar J Ranch, LLC v. Carlisle Wide Plank Floors, Inc., 2012 MT 246, 366 Mont. 506, 288 P.3d 228.

Definition of Unfair Act or Practice Under Consumer Protection Act: As a matter of law, as the term is used in the Montana Consumer Protection Act, an unfair act or practice is one that offends established public policy and that is immoral, unethical, oppressive, unscrupulous, or substantially injurious to consumers. Rohrer v. Knudson, 2009 MT 35, 349 M 197, 203 P3d 759 (2009).

Question Whether Seller of Subdivision Lot Violated Consumer Protection Law — Remand: Plaintiffs sued the seller of a subdivision lot for violating the Montana Consumer Protection Act (MCPA) by failing to disclose that the lot contained uncontrolled fill material to a depth of about 31 feet below grade, which resulted in shifting of the foundation of plaintiffs' home, causing damages. The jury apportioned negligence of 10% to defendant, 45% to the city, and 45% to plaintiffs, and plaintiffs appealed. In determining whether the MCPA was violated, the Supreme Court held that the record contained conflicting evidence as to whether soil compaction and density studies were completed and that the studies were necessary to determine whether the seller offended established public policy and whether any unfair act or practice caused plaintiffs' damages warranting recovery under the MCPA. Therefore, the case was remanded for retrial. Rohrer v. Knudson, 2009 MT 35, 349 M 197, 203 P3d 759 (2009).

Standard for Award of Attorney Fees to Prevailing Defendant in Consumer Protection Action: The District Court found that as the prevailing party in an action brought under the Montana Unfair Trade Practices and Consumer Protection Act of 1973, defendant was entitled to attorney fees. The Supreme Court held that the standard for awarding attorney fees to a defendant differs from the standard applicable to a prevailing plaintiff and that the proper standard for awarding fees to a defendant should mirror similar awards to defendants under Title 49, ch. 2, commonly known as the Montana Human Rights Act. Applying Christiansburg Garment Co. v. Equal Employment Opportunity Comm'n, 434 US 412 (1978), the court held that an award of attorney fees to a prevailing defendant under the Montana Unfair Trade Practices and Consumer Protection Act should be made only upon a finding that plaintiff's action was frivolous, unreasonable, or without foundation, even though the action was not brought in subjective bad faith. Because the District Court did not apply the Christiansburg standard, the Supreme Court reversed. Tripp v. Jeld-Wen, Inc., 2005 MT 121, 327 M 146, 112 P3d 1018 (2005), followed in Harmon v. Fiscus Realty, Inc., 2011 MT 232, 362 Mont. 135, 261 P.3d 1031. However, see Coleman Constr., Inc. v. Kudrna, 2006 MT 98, 332 M 112, 136 P3d 970 (2006), in which the Supreme Court declined to extend the Tripp standard to a successful defendant entitled to collect attorney fees under The Montana Residential Landlord and Tenant Act of 1977.

Claims Under Unfair Trade Practices Act Subject to Statute of Limitations on Actions for Constructive Fraud: As a liability created by statute that is neither a penalty nor a statutory debt, claims brought under the Montana Unfair Trade Practices and Consumer Protection Act of 1973 are subject to the 2-year statute of limitations in 27-2-211. Osterman v. Sears, Roebuck & Co., 2003 MT 327, 318 M 342, 80 P3d 435 (2003), following Royal Ins. Co. v. Roadarmel, 2000 MT 259, 301 M 508, 11 P3d 105 (2000).

Exercise of Ordinary Diligence Required in Discovery of Unfair Trade Practices Constituting Fraud for Tolling Statute of Limitations: For purposes of tolling the statute of limitations in an action for fraud or unfair trade practices, ordinary diligence must be exercised by the aggrieved party in discovery of the facts constituting the fraud or deceptive practice. Pursuant to Johnson v. Barrett, 1999 MT 176, 295 M 254, 983 P2d 925 (1999), the test is whether the plaintiff has information of circumstances sufficient to put a reasonable person on inquiry or has the opportunity to obtain knowledge from sources open to the plaintiff's investigation. Mere ignorance of the facts will not suffice to toll the statute of limitations. In this case, plaintiff filed an unfair trade practices complaint about 2 years and 9 months after entering an agreement with defendant siding installer, believing at the time that the contract was with the defendant company that manufactured the siding. However, plaintiff showed no affirmative conduct by either defendant that was calculated to obscure the existence of a cause of action, nor were the facts giving rise to the alleged fraud concealed. Thus, plaintiff discovered or should have discovered the facts constituting the alleged fraud when the contract was entered more than 2 years prior to filing suit, so the claim was barred by the 2-year statute of limitations in 27-2-211. Osterman v. Sears, Roebuck & Co., 2003 MT 327, 318 M 342, 80 P3d 435 (2003).

No Evidence of False Representation of Material Fact — Claim of Negligent Misrepresentation Properly Dismissed: Plaintiff claimed that vinyl siding was sold, furnished, and installed on her home under misleading circumstances because the installer failed to clearly identify the relationship with the siding manufacturer. However, plaintiff failed to specify any false statements made by either the installer or the manufacturer that led her to believe that this was true. Absent evidence demonstrating the primary element of the cause of action, plaintiff's negligent representation claim failed as a matter of law. Osterman v. Sears, Roebuck & Co., 2003 MT 327, 318 M 342, 80 P3d 435 (2003), following Yellowstone II Dev. Group, Inc. v. First Am. Title Ins. Co., 2001 MT 41, 304 M 223, 20 P3d 755 (2001).

Discretionary, Not Punitive, Nature of Treble Damage Award: The purpose of the trebling provision in this section is to encourage private individuals to pursue violations of the Montana Unfair Trade Practices and Consumer Protection Act of 1973 by making it more economically feasible to pursue claims when actual damages are minimal. To be eligible for treble damages, this section does not require a plaintiff to prove malice, oppression, or fraud, which under Montana law is prerequisite conduct necessary to allowing punitive damages. Nothing in the statutory language indicates that trebling of damages under the Act is punitive rather than compensatory or remedial in nature, as indicated by the Legislature's intent in drafting the Act without including specific conduct that would trigger the imposition of treble damages. Because of the compensatory or remedial nature of the treble damages provision, the District Court in this case committed reversible error when it ruled that treble damages could not be awarded because the evidence did not support a finding generally associated with punitive damages. Rather, a District Court should be guided by the overall purpose of the Act itself, and use discretion in making a treble award on a case-by-case basis. Plath v. Schonrock, 2003 MT 21, 314 M 101, 64 P3d 984 (2003), followed in Vader v. Fleetwood Enterprises, Inc., 2009 MT 6, 348 M 344, 201 P3d 139 (2009), with regard to discretion of District Court to increase damage award without any particular criteria.

Partial Award of Attorney Fees Improper When Not Supported by Competent Evidence Established at Hearing: The District Court properly used its discretion in awarding attorney fees under this section, but the award was only partial, and the court failed to hold an evidentiary hearing to determine the amount to be awarded. Without the support of competent evidence gathered at a hearing, the award was an abuse of discretion. The Supreme Court reversed and ordered an evidentiary hearing for the determination of reasonable attorney fees in accordance with the criteria established in Swenson v. Janke, 274 M 354, 908 P2d 678 (1995). Plath v. Schonrock, 2003 MT 21, 314 M 101, 64 P3d 984 (2003).

Expert Testimony Unnecessary on Issue of Standard of Care — District Court Not Directed as to All Expert Testimony on All Claims: Durbins purchased a home through the seller's realtors. Contrary to the representations of the realtors, Durbins discovered that the property had no legal septic system, that the household water was unsafe to use for any purpose, and that the access road was located on the neighbor's property. Durbins brought an action against the realtors, alleging negligent misrepresentation, actual and constructive fraud, and statutory violations involving the Montana real estate licensing laws and the Montana Unfair Trade Practices and Consumer Protection Act of 1973. The defendants sought and achieved dismissal of the case on the grounds that Durbins failed to prove through expert testimony the applicable standard of care of the realtors. The Supreme Court held that expert witnesses were unnecessary to prove a standard of care. Durbins also asked that the Supreme Court direct the District Court to exclude testimony of any expert witnesses on any claim asserted by the Durbins. The Supreme Court noted that the District Courts have great latitude concerning the admissibility of evidence and that the District Court would in any event have to comply with Rule 702, M.R.Ev. (Title 26, ch. 10). The Supreme Court therefore declined to direct the District Court as requested by the Durbins. Durbin v. Ross, 276 M 463, 916 P2d 758, 53 St. Rep. 471 (1996).

Repossession of Vehicle as Constituting Conversion — Damages: Entriken purchased a new pickup, granting the credit union a security interest in the vehicle, purchased credit disability insurance as part of the loan, and authorized payroll deduction for direct payment of the loan. Entriken was subsequently injured on the job. He notified the credit union that he was no longer working and completed the proper documents so that the disability insurance company could begin making the monthly payments. Three weeks later, Entriken received a delinquency notice but was informed by the credit union that the notice was merely a formality and that he need not worry because the disability payments would be arriving shortly. About 5 weeks later the credit union caused the vehicle to be repossessed, adding costs of repossession, storage, transportation, and legal fees to the outstanding loan balance. Without proper notice to Entriken or filing a deficiency judgment, the credit union sold the truck. Following sale of the truck, the credit union continued to receive credit disability payments as well as payroll deductions from Entriken, who was subsequently reemployed. Despite claims that Entriken had failed to properly insure the vehicle and had been delinquent in payments, the District Court correctly found that the credit union had converted the vehicle and awarded Entriken actual damages, damages for loss of use, attorney fees, and treble damages under this section. The Supreme Court affirmed the conversion question and the award of actual damages plus interest and attorney fees, reversed the award of loss of use damages as being unfounded on legal authority, and recalculated the treble damage award, under the rationale of Baird v. Norwest Bank, 255 M 317, 843 P2d 327, 49 St. Rep. 1026 (1992), to three times the actual damages rather than three times the actual damages plus the actual damages. Entriken v. Motor Coach Fed. Credit Union, 256 M 85, 845 P2d 93, 49 St. Rep. 1148 (1992).

Breach of Loan Contract for Failure to Honor Late Payment Agreement: Testimony of borrowers that bank's representative agreed to give them until September 15 to make late payment of an overdue loan payment, of borrowers' former attorney in support of borrowers' testimony, and of bank employee that one of the borrowers told her on the phone that he had promised to pay by September 15 was sufficient evidence to support jury's verdict that bank breached the loan contract when, beginning on September 12, it initiated collection procedures, accelerated payments and demanded payment of the loan in full, refused further payments on the loan, and repossessed the collateral. However, there was no fraud because bank's representative testified that the agreement was for payment by September 1, she entered that date in the bank's computer, and there was no evidence that she intended to enter the wrong date. Baird v. Norwest Bank, 255 M 317, 843 P2d 327, 49 St. Rep. 1026 (1992).

Consumer Loan by Bank Covered by Act: Because the Montana Unfair Trade Practices and Consumer Protection Act of 1973 is in derogation of the common law, it should be liberally construed with a view to effect its object and to promote justice. The approach to defining what is meant by the word "services" should be broad in scope. The Act applies to a consumer loan by a bank. Baird v. Norwest Bank, 255 M 317, 843 P2d 327, 49 St. Rep. 1026 (1992).

Attorney Fees — No Record on Appeal: Plaintiffs and defendant were each negligent in causing plaintiffs' damages. The jury also found the defendant violated the Consumer Protection Act. Under the verdict form used, it was not possible for the Supreme Court to apportion damages between the negligence count and the Consumer Protection Act count. The trial court denied attorney fees to the plaintiffs, stating that they were equally negligent in the events leading to the action. No transcript was provided on appeal. In the absence of a record on appeal, the Supreme Court cannot evaluate the trial court's basis for denying attorney fees and will not interfere with the court's discretion under these circumstances. Evans v. Teakettle Realty, 226 M 363, 736 P2d 472, 44 St. Rep. 723 (1987).

Negligence Compared With Violation of Consumer Protection Act: The jury found the defendant violated the Consumer Protection Act and was negligent. The trial court applied the comparative negligence statute to reduce the plaintiffs' recovery under the Act. On appeal, the Supreme Court affirmed the reduction of damages, stating that the law as stated in the jury instructions does not allow the separation of the defendant's actions in violation of the Consumer Protection Act from its actions that were negligent. Evans v. Teakettle Realty, 226 M 363, 736 P2d 472, 44 St. Rep. 723 (1987).

Provisions of Act Not Applicable — Attorney Fees Proper: The District Court found that the provisions of the Montana Unfair Trade Practices and Consumer Protection Act of 1973 were inapplicable to the subject of this case but that pursuant to the Act the defendant, as prevailing party, was entitled to reasonable attorney fees under this section. Appellant contended that since the Act did not apply, award of attorney fees was not appropriate. The Supreme Court affirmed the award, noting that defendant prevailed on the main issue in controversy and that since the action was brought under the Act, reasonable attorney fees were proper. Dillree v. Devoe, 223 M 47, 724 P2d 171, 43 St. Rep. 1521 (1986).

Section Inapplicable to Purchaser of Goods for Business Purposes: When uncontradicted testimony established that a machine had been purchased for use in respondents' business, respondents did not fall within the class of persons who may bring a private action under this part. Doll v. Major Muffler Centers, Inc., 208 M 401, 687 P2d 48, 41 St. Rep. 429 (1984).

Exemplary Damages: In an action to rescind a contract to purchase an automobile, there was no requirement that plaintiff show malice, oppression, or fraud on the part of the seller in order to recover exemplary damages under 30-14-133. T & W Chevrolet v. Darvial, 196 M 287, 641 P2d 1368, 39 St. Rep. 112 (1982).

Consumer Protection Act Violation Alleged as Cause of Accident — Agency Rule Not in Conflict With Federal Law — Summary Judgment: The District Court properly denied summary judgment on plaintiff's Court No. II, which claimed misrepresentation as to the odometer reading on a used car sold to her by defendant corporation as the proximate cause of her accident and subsequent injuries. A state agency rule adopted pursuant to 30-14-104 was not inconsistent with the rules and decisions of the FTC and decisions of the Federal Courts, although the rule deals with sales and the main purpose of the federal law is to prevent unlawful restraint of trade. Whether the alleged violation was a cause of plaintiff's damages was a jury issue. Kopischke v. First. Cont. Corp., 187 M 471, 610 P2d 668 (1980).

30-14-142. Penalties.

Compiler's Comments

2003 Amendment: Chapter 322 at beginning of (1) inserted initial clause concerning subsection (2); in (2) in first sentence increased maximum fine from $1,000 to $10,000 and inserted last sentence relating to effect of the fine; and made minor changes in style. Amendment effective April 15, 2003.

1999 Amendment: Chapter 342 in (1) and (2) substituted "fine" for "penalty"; in (2) increased fine amount from $500 to $1,000; in (3) increased fine amount from $2,000 to $5,000; and made minor changes in style. Amendment effective October 1, 1999.

30-14-143. Disposition of civil fines, settlement proceeds, amounts awarded in judgments, costs, and fees.

Compiler's Comments

2021 Amendment: Chapter 256 in (1)(a) near beginning inserted "settlement proceeds not otherwise designated for a specific use pursuant to court order, amounts awarded in judgments"; in (1)(b) inserted first sentence concerning the account balance not exceeding three times the amount of the budget appropriated, inserted second sentence concerning funds obligated to implement the settlement agreement, near beginning of third sentence inserted "settlement proceeds not otherwise designated for a specific use pursuant to court order, amounts awarded in judgment", and near end of third sentence inserted "no later than the first business day in January of the subsequent biennium"; in (2) near beginning inserted "settlement proceeds, amounts awarded in judgments"; and made minor changes in style. Amendment effective October 1, 2021.

2013 Amendment: Chapter 217 in (1)(a) at beginning inserted exception clause and inserted (1)(b) concerning disposition of civil fines recovered pursuant to 30-14-144. Amendment effective October 1, 2013.

Saving Clause: Section 4, Ch. 217, L. 2013, was a saving clause.

2005 Amendment: Chapter 280 deleted former (2) that read: "(2) All civil fines, costs, and fees received or recovered by the attorney general pursuant to this part must be deposited into a state special revenue account to the credit of the attorney general and must be used to defray the expenses of the office of the attorney general in discharging its regulatory powers and duties in relation to this part. Any excess civil fines, costs, or fees must be transferred to the general fund"; and made minor changes in style. Amendment effective July 1, 2005.

Effective Date: Section 4, Ch. 136, L. 2003, provided: "[This act] is effective July 1, 2003."

30-14-144. Additional penalty for unfair or deceptive act committed against vulnerable adult.

Compiler's Comments

2023 Amendment: See 2023 Session Law for amendment made by sec. 1, Ch. 12, L. 2023. Amendment effective October 1, 2023.

Effective Date: This section is effective October 1, 2013.

Saving Clause: Section 4, Ch. 217, L. 2013, was a saving clause.

30-14-158. Prohibition against tiktok — penalty — enforcement — definitions.

Compiler's Comments

Effective Date: Section 5, Ch. 503, L. 2023, provided: "[This act] is effective January 1, 2024."

Preamble: The preamble attached to Ch. 503, L. 2023, provided: "WHEREAS, the People's Republic of China is an adversary of the United States and Montana and has an interest in gathering information about Montanans, Montana companies, and the intellectual property of users to engage in corporate and international espionage; and

WHEREAS, TikTok is a wholly owned subsidiary of ByteDance, a Chinese corporation; and

WHEREAS, the People's Republic of China exercises control and oversight over ByteDance, like other Chinese corporations, and can direct the company to share user information, including real-time physical locations of users; and

WHEREAS, TikTok gathers significant information from its users, accessing data against their will to share with the People's Republic of China; and

WHEREAS, TikTok fails to remove, and may even promote, dangerous content that directs minors to engage in dangerous activities, including but not limited to throwing objects at moving automobiles, taking excessive amounts of medication, lighting a mirror on fire and then attempting to extinguish it using only one's body parts, inducing unconsciousness through oxygen deprivation, cooking chicken in NyQuil, pouring hot wax on a user's face, attempting to break an unsuspecting passerby's skull by tripping him or her into landing face first into a hard surface, placing metal objects in electrical outlets, swerving cars at high rates of speed, smearing human feces on toddlers, licking doorknobs and toilet seats to place oneself at risk of contracting coronavirus, attempting to climb stacks of milkcrates, shooting passersby with air rifles, loosening lug nuts on vehicles, and stealing utilities from public places; and

WHEREAS, TikTok's stealing of information and data from users and its ability to share that data with the Chinese Communist Party unacceptably infringes on Montana's right to privacy; and

WHEREAS, TikTok's continued operation in Montana serves as a valuable tool to the People's Republic of China to conduct corporate and international espionage in Montana and may allow the People's Republic of China to track the real-time locations of public officials, journalists, and other individuals adverse to the Chinese Communist Party's interests; and

WHEREAS, TikTok's allowance and promotion of dangerous challenges threatens the health and safety of Montanans."

Severability: Section 3, Ch. 503, L. 2023, was a severability clause.

30-14-159. Publishing and distribution of material harmful to minors — age verification — requirements — penalties — exceptions — reporting — definitions.

Compiler's Comments

Effective Date: Section 3, Ch. 700, L. 2023, provided: "[This act] is effective January 1, 2024."

Preamble: The preamble attached to Ch. 700, L. 2023, provided: "WHEREAS, pornography is creating a public health crisis and having a corroding influence on minors; and

WHEREAS, due to advances in technology, the universal availability of the internet, and limited age verification requirements, minors are exposed to pornography earlier in age; and

WHEREAS, pornography contributes to the hypersexualization of teens and prepubescent children and may lead to low self-esteem, body image disorders, an increase in problematic sexual activity at younger ages, and increased desire among adolescents to engage in risky sexual behavior; and

WHEREAS, pornography may also impact brain development and functioning, contribute to emotional and medical illnesses, shape deviant sexual arousal, and lead to difficulty in forming or maintaining positive, intimate relationships, as well as promoting problematic or harmful sexual behaviors and addiction; and

WHEREAS, the provisions of this act are intended to provide a civil remedy for damages against commercial entities who distribute material harmful to minors."

30-14-160. Firearms code.

Compiler's Comments

Effective Date: This section is effective October 1, 2023.

Part 2
Unfair Trade Practices Generally

Part Law Review Articles

The Erosion of Equity and the Attack on the FTC's Redress Authority, Vladeck, 82 Mont. L. Rev. 159 (2021).

One Short of a Load: Why an Illinois Brick Repealer Will Increase Private Antitrust Enforcement in Montana, Price, 74 Mont. L. Rev. 399 (2013).

30-14-201. Purpose.

Compiler's Comments

2005 Amendment: Chapter 280 at beginning of last sentence substituted "must be liberally construed" for "shall be literally construed" and at end substituted "accomplished" for "subserved". Amendment effective July 1, 2005.

Case Notes

Regulatory Board Not Considered Person Engaged in Business Subject to Liability Under Montana Unfair Trade Practices Act: The Montana Unfair Trade Practices and Consumer Protection Act of 1973 was created to apply to businesses, not government. Therefore, a state regulatory board is not subject to the Act for alleged unlawful restraint of trade. Wiser v. St., 2006 MT 20, 331 M 28, 129 P3d 133 (2006), following Mont. Vending, Inc. v. Coca-Cola Bottling Co. of Mont., 2003 MT 282, 318 M 1, 78 P3d 499 (2003).

School District Not Considered Person Engaged in Business Subject to Liability Under Montana Unfair Trade Practices Act: The Great Falls school district entered exclusive agreements with Coke and Pepsi to provide soft drinks in school facilities in exchange for $500,000 over a 10-year period. Plaintiff, which had supplied soft drinks to the district for almost 20 years, sued the school district for violation of the Montana Unfair Trade Practices and Consumer Protection Act of 1973. The school district contended that it was not subject to suit under the Act because by definition, it was not a person engaged in business, and the Supreme Court agreed. The plain meaning of person in 30-14-202 does not include a school district. To conclude otherwise would infringe on a school district's statutory power to raise revenue for funding education. A school district is also not a business as defined in the Act because a business is a person, which does not include a school district. Further, in accordance with the purpose set out in this section, the Act was created to apply to competitive businesses, not government, which generally acts as a market regulator and not a competitor. Mont. Vending, Inc. v. Coca-Cola Bottling Co. of Mont., 2003 MT 282, 318 M 1, 78 P3d 499 (2003).

30-14-202. Definitions.

Compiler's Comments

2005 Amendment: Chapter 280 in definition of department substituted "department of justice" for "department of administration" and substituted "2-15-2001" for "2-15-1001". Amendment effective July 1, 2005.

2001 Amendment: Chapter 483 in definition of department substituted reference to department of administration for reference to department of commerce and substituted "2-15-1001" for "2-15-1801"; and made minor changes in style. Amendment effective July 1, 2001.

1981 Amendment: Substituted "department of commerce" for "department of business regulation" in (7).

Case Notes

Regulatory Board Not Considered Person Engaged in Business Subject to Liability Under Montana Unfair Trade Practices Act: The Montana Unfair Trade Practices and Consumer Protection Act of 1973 was created to apply to businesses, not government. Therefore, a state regulatory board is not subject to the Act for alleged unlawful restraint of trade. Wiser v. St., 2006 MT 20, 331 M 28, 129 P3d 133 (2006), following Mont. Vending, Inc. v. Coca-Cola Bottling Co. of Mont., 2003 MT 282, 318 M 1, 78 P3d 499 (2003).

School District Not Considered Person Engaged in Business Subject to Liability Under Montana Unfair Trade Practices Act: The Great Falls school district entered exclusive agreements with Coke and Pepsi to provide soft drinks in school facilities in exchange for $500,000 over a 10-year period. Plaintiff, which had supplied soft drinks to the district for almost 20 years, sued the school district for violation of the Montana Unfair Trade Practices and Consumer Protection Act of 1973. The school district contended that it was not subject to suit under the Act because by definition, it was not a person engaged in business, and the Supreme Court agreed. The plain meaning of person in this section does not include a school district. To conclude otherwise would infringe on a school district's statutory power to raise revenue for funding education. A school district is also not a business as defined in the Act because a business is a person, which does not include a school district. Further, in accordance with the purpose set out in 30-14-201, the Act was created to apply to competitive businesses, not government, which generally acts as a market regulator and not a competitor. Mont. Vending, Inc. v. Coca-Cola Bottling Co. of Mont., 2003 MT 282, 318 M 1, 78 P3d 499 (2003).

30-14-203. Persons responsible.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

1981 Amendment: Substituted "business" for "firm or corporation" in two places.

30-14-204. Proof of intent.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

1981 Amendment: Substituted "or business" for "firm or corporation".

30-14-205. Unlawful restraint of trade.

Case Notes

Insurance Preferred Provider Agreements Upheld — Equal Protection — State Action Required for General Application — Insured and Uninsured Analyzed: In a second appeal to Gazelka v. St. Peter's Hosp., 2015 MT 127, 379 Mont. 142, 347 P.3d 1287, the plaintiff argued that treatment costs incurred at the defendant hospital violated the equal protection clause. The plaintiff also argued that the Montana Preferred Providers Agreements Act (MPPAA) unconstitutionally discriminated against uninsured patients and patients insured by insurers that did not negotiate the most favorable preferred provider agreements. The Supreme Court disagreed with the plaintiff, holding that Montana's equal protection clause contains both a specific guarantee applying to public and private action and a general guarantee. The court held that one's status as an insured or uninsured is not one's race, color, sex, culture, social origin or condition, or political or religious ideas, making the specific guarantee inapplicable. The court then held that for the general guarantee, the plaintiff must demonstrate that state action, not merely private conduct, denied the plaintiff equal protection of the laws. The court then found that the MPPAA did not deny the plaintiff equal protection of the laws because the classes of insured and uninsured were not similarly situated, health insurance is not a social condition for purposes of equal protection, and the MPPAA did not create impermissible classifications based on one's social condition, income, or economic status. Gazelka v. St. Peter's Hosp., 2018 MT 152, 392 Mont. 1, 420 P.3d 528.

Regulatory Board Not Considered Person Engaged in Business Subject to Liability Under Montana Unfair Trade Practices Act: The Montana Unfair Trade Practices and Consumer Protection Act of 1973 was created to apply to businesses, not government. Therefore, a state regulatory board is not subject to the Act for alleged unlawful restraint of trade. Wiser v. St., 2006 MT 20, 331 M 28, 129 P3d 133 (2006), following Mont. Vending, Inc. v. Coca-Cola Bottling Co. of Mont., 2003 MT 282, 318 M 1, 78 P3d 499 (2003).

School District Not Considered Person Engaged in Business Subject to Liability Under Montana Unfair Trade Practices Act: The Great Falls school district entered exclusive agreements with Coke and Pepsi to provide soft drinks in school facilities in exchange for $500,000 over a 10-year period. Plaintiff, which had supplied soft drinks to the district for almost 20 years, sued the school district for violation of the Montana Unfair Trade Practices and Consumer Protection Act of 1973. The school district contended that it was not subject to suit under the Act because by definition, it was not a person engaged in business, and the Supreme Court agreed. The plain meaning of person in 30-14-202 does not include a school district. To conclude otherwise would infringe on a school district's statutory power to raise revenue for funding education. A school district is also not a business as defined in the Act because a business is a person, which does not include a school district. Further, in accordance with the purpose set out in 30-14-201, the Act was created to apply to competitive businesses, not government, which generally acts as a market regulator and not a competitor. Mont. Vending, Inc. v. Coca-Cola Bottling Co. of Mont., 2003 MT 282, 318 M 1, 78 P3d 499 (2003).

Brand Monopoly Over Manufacturer's Own Product Not Violative of Unfair Trade Practices Act: Plaintiffs contended that Video Lottery Consultants, Inc., refused to sell its gambling machines in order to create a monopoly in the sale and use of video lottery machines. However, under the rationale of Sadler v. Rexair, Inc., 612 F. Supp. 491 (D.C. Mont. 1985), a brand monopoly over a manufacturer's own product does not violate the provisions of this section. Smith v. Video Lottery Consultants, Inc., 260 M 54, 858 P2d 11, 50 St. Rep. 939 (1993).

Restraint of Trade Distinguished From Sherman Act — Applicability of Summary Judgment and Injunctive Relief: Although this section is modeled after the federal Sherman Act, 15 U.S.C. 1, the Sherman Act requires two or more persons to be involved in the unlawful trade restraint while the Montana statute appears to be broader, as one person acting alone may violate the provisions of this section. Based upon this statutory difference, coupled with the fact that this section has not been previously interpreted and no underlying factual record was developed in this case, it was premature to dismiss a claim for failure to state a cause of action for which relief could be granted because it could not be said that plaintiffs were not entitled to relief under any set of facts that could be proven in support of their claim. The case was remanded for further discovery, subject to summary dismissal if plaintiffs could not develop a sustainable action. Similarly, if a sustainable action could be developed, injunctive relief may be available under 30-14-222. Smith v. Video Lottery Consultants, Inc., 260 M 54, 858 P2d 11, 50 St. Rep. 939 (1993).

Parallel Pricing as Insufficient Circumstantial Evidence of Restraint of Trade: Where the State brought an action against the defendant retail gasoline dealer, alleging that the defendant acted to restrain trade in the setting of gasoline prices, the federal District Court found that the defendant's actions of price following and parallel pricing were consistent with the defendant's own policies and self-interest, were a rational response to market conditions, were not accompanied by any evidence of other "plus factors" tending to show restraint of trade, and that the evidence of the defendant's pricing methods was therefore insufficient circumstantial evidence to show a violation of either state or federal law. St. v. SuperAmerica, 559 F. Supp. 298, 40 St. Rep. 944 (D.C. Mont. 1983).

Milk Pricing Control — Actions Compelled by Law Not Unfair Trade Practices: A third-party plaintiff brought an action for declaratory and injunctive relief against the operation and enforcement of certain milk pricing statutes, claiming those statutes violated the provisions of 30-14-205, and the third-party defendant moved to dismiss the claim on the grounds that it did not state a claim for relief. The court found that although the statutes challenged by the plaintiff did fix the price of milk, eliminate competition, and create a monopoly, the only reason whereby 30-14-224 could control was if that section expressly or impliedly repealed the Milk Price Control Act. The court found no such repeal had been intended by the Legislature. Hinshaw v. Beatrice Foods, Inc., 37 St. Rep. 1677 (D.C. Mont. 1980) (apparently not reported in Federal Supplement).

30-14-211. Establishing cost survey.

Compiler's Comments

2003 Amendment: Chapter 322 in first sentence of (1) after "trade or business" deleted "establish the cost survey provided for in 30-14-210. When petition for a cost survey has been so presented to the department, the department shall"; and made minor changes in style. Amendment effective April 15, 2003.

30-14-213. Sales excepted.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-14-219. Recovery on illegal contracts forbidden.

Compiler's Comments

2003 Amendment: Chapter 322 after "30-14-205" inserted "through 30-14-214 or 30-14-216"; and made minor changes in style. Amendment effective April 15, 2003.

30-14-220. Enforcement by department.

Compiler's Comments

2005 Amendment: Chapter 280 in (2) near end of first sentence before "department" deleted "director of the"; in (3)(b) after "department" deleted "in its discretion"; in (4) after "necessary" deleted "in its judgment"; in (7) near middle substituted "pay to the department" for "pay to the state"; and made minor changes in style. Amendment effective July 1, 2005.

2003 Amendment: Chapter 322 in (1) substituted "may" for "shall"; in (2) at end substituted "may make its own investigation" for "shall:

(a) make its own investigation;

(b) within 60 days of the finding of probable cause make a written report of its investigation; and

(c) mail a copy of its findings to the person initially giving notice of a violation"; in (3)(a) near middle after "this part" substituted "or" for "and", after "it" substituted "may" for "shall", and substituted "the location of the hearing, and the date of the hearing, which may not be less than 5 days" for "at a place and upon a day not less than 5 days"; in (3)(c) near beginning substituted "at the hearing" for "at the place and time so fixed"; in (7) increased the maximum penalty from $1,000 to $10,000; and made minor changes in style. Amendment effective April 15, 2003.

30-14-221. Investigations.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

1985 Amendment: In second sentence of (3) substituted "department" for "commissioner" in two places.

1983 Amendment: In (3), in first sentence after "forfeiture" substituted language prohibiting the use of compelled testimony, evidence, or information in a criminal prosecution, and allowing the Commissioner to grant immunity from prosecution except for false statements given pursuant to a subpoena for "An individual may not be prosecuted or subjected to a penalty or forfeiture for or on account of a transaction, matter, or thing concerning which he is compelled to testify or produce evidence after having claimed his privilege against self-incrimination. An individual so testifying is not exempt from prosecution and punishment for perjury committed in testifying."

30-14-222. Injunctions — damages — production of evidence.

Compiler's Comments

2005 Amendments — Composite Section: Chapter 130 in (1) in second sentence after "30-14-205" inserted "through"; and made minor changes in style. Amendment effective October 1, 2005.

Chapter 280 in (1) at beginning of first sentence substituted "A person who is or will be injured or the department may bring an action" for "Any person who is or will be injured, the department, or the attorney general may maintain an action" and in second sentence substituted "30-14-205 through 30-14-214" for "30-14-205, 30-14-214"; in (4) near middle substituted "department" for "state"; and made minor changes in style. Amendment effective July 1, 2005.

2003 Amendment: Chapter 322 in (1) in first sentence substituted "Any person who is or will be injured, the department, or the attorney general may maintain an action to enjoin an act that is in violation of 30-14-205 through 30-14-214 or 30-14-216 through 30-14-218" for "Any person, if injured thereby, or the attorney general may maintain an action to enjoin a continuance of an act in violation of 30-14-205 through 30-14-218" and in second sentence inserted "30-14-214, or 30-14-216"; at end of (2)(a) substituted "the greater of three times the amount of actual damages sustained or $1,000" for "three times the amount of actual damages sustained"; inserted (2)(b) relating to a daily penalty; in (3) in second sentence before "prosecution" deleted "misdemeanor" and near end inserted "30-14-214, 30-14-216 through"; inserted (4) relating to attorney fees and costs; and made minor changes in style. Amendment effective April 15, 2003.

Case Notes

Restraint of Trade Distinguished From Sherman Act — Applicability of Summary Judgment and Injunctive Relief: Although 30-14-205 is modeled after the federal Sherman Act, 15 U.S.C. 1, the Sherman Act requires two or more persons to be involved in the unlawful trade restraint while the Montana statute appears to be broader, as one person acting alone may violate the provisions of 30-14-205. Based upon this statutory difference, coupled with the fact that 30-14-205 has not been previously interpreted and no underlying factual record was developed in this case, it was premature to dismiss a claim for failure to state a cause of action for which relief could be granted because it could not be said that plaintiffs were not entitled to relief under any set of facts that could be proven in support of their claim. The case was remanded for further discovery, subject to summary dismissal if plaintiffs could not develop a sustainable action. Similarly, if a sustainable action could be developed, injunctive relief may be available under this section. Smith v. Video Lottery Consultants, Inc., 260 M 54, 858 P2d 11, 50 St. Rep. 939 (1993).

Reversal of Award of Attorney Fees — Applicability of Specific Statutes: Respondents contended that under 27-1-316, 28-3-704, and 30-14-222 they were entitled to attorney fees. The court considered each statute and decided: (1) since the issue of unlawful restraint of trade was reversed, no damages were allowable under 30-14-222; (2) because there was no allowance for attorney fees where the covenantor brings an action for breach of contract against the covenantee, 27-1-316 was inapplicable; and (3) since an agreement with an attorney fee provision was entered into prior to the July 1, 1971, effective date enumerated in 28-3-704 and was found to have been merged in the deeds that contained no such provision, 28-3-704 was also not applicable. The award of attorney fees to respondents was reversed. Haggerty v. Gallatin County, 221 M 109, 717 P2d 550, 43 St. Rep. 674 (1986).

30-14-223. Department's institution of suit.

Compiler's Comments

2005 Amendment: Chapter 130 in two places after "30-14-205" inserted "through"; and made minor changes in style. Amendment effective October 1, 2005.

2003 Amendment: Chapter 322 in first sentence at beginning after "Upon the" deleted "third", inserted "30-14-214, or 30-14-216", and substituted "the department may institute a proceeding in a court" for "the department shall institute proper suits or quo warranto proceedings in a court"; in last sentence inserted "30-14-214, or 30-14-216"; and made minor changes in style. Amendment effective April 15, 2003.

1981 Amendment: Substituted "business" for "corporation" in five places.

30-14-224. Penalties.

Compiler's Comments

2003 Amendment: Chapter 322 in (1) at beginning deleted "Except as otherwise provided in this section", inserted "purposely or knowingly", substituted "30-14-207 through 30-14-214 or 30-14-216 through 30-14-218" for "30-14-206 through 30-14-218", substituted "guilty of an offense for each violation" for "guilty of a misdemeanor for each single violation", substituted "may be fined an amount not more than $10,000" for "shall be fined not less than $100 or more than $1,000", and increased maximum imprisonment term from 6 months to 2 years; at end of (2) substituted "imprisonment for a period of not more than 5 years, and the offender may be subject to a fine in an amount not exceeding $25,000" for "imprisonment in the county jail for a period not less than 24 hours or more than 1 year or by fine not exceeding $25,000, or both"; in (3) at end increased the revocation time from 1 year to 5 years; and made minor changes in style. Amendment effective April 15, 2003.

30-14-225. Prohibited practices — advertising allowed — violations.

Compiler's Comments

2001 Amendment: Chapter 345 in (1) after "engaged in" deleted "automobile repair or"; in (1)(b) after "directing" and in (2) after "engaged in" deleted "automobile repair services or"; in (3) after "33-18-223" deleted "or an automobile repair business", after "work" deleted "or automobile repair services", and after "broker" deleted "or the automobile repair business"; deleted former (4) that read: "(4) Except as provided in 33-18-224, in a communication between an insurer and an insured regarding an insurance claim, the insurer may not:

(a) require, suggest, or encourage the use of the name of a particular automobile repair business or location; or

(b) mention or provide the name of a particular automobile repair business or location"; and made minor changes in style. Amendment effective April 21, 2001.

Severability: Section 7, Ch. 345, L. 2001, was a severability clause.

Retroactive Applicability: Section 9, Ch. 345, L. 2001, provided: "[This act] applies retroactively, within the meaning of 1-2-109, to October 1, 1999."

1999 Amendments — Composite Section: Chapter 174 in (1) in introductory clause after "glass" inserted "or in the business of automobile repair"; in (1)(a) at end inserted "including any incentive to purchase automobile glass or automobile repairs offered to the customer in which the customer, in conjunction with the purchase of automobile glass or automobile repairs, receives cash or other valuable consideration"; and inserted (5) establishing violations. Amendment effective October 1, 1999.

Chapter 526 throughout (1), (2), and (3) inserted references to automobile repair; and inserted (4) prohibiting an insurer from directing or encouraging the use of a particular automobile repair business. Amendment effective October 1, 1999.

Severability: Section 7, Ch. 526, L. 1999, was a severability clause.

1997 Amendment: Chapter 207 in (3), in two places, substituted references to glass broker for "person" and at end deleted "or a set fee paid by the insurance company to the glass repair shop for an amount in excess of the amount paid to the glass repair shop".

Effective Date: Section 7, Ch. 554, L. 1993, provided: "[This act] is effective on passage and approval." Approved April 28, 1993.

30-14-226. Disposition of civil fines, settlement proceeds, amounts awarded in judgments, costs, and fees.

Compiler's Comments

2021 Amendment: Chapter 256 in (1) near beginning inserted "settlement proceeds not otherwise designated for a specific use pursuant to court order, amounts awarded in judgments";

in (2) inserted first sentence concerning the account balance not exceeding three times the amount of the budget appropriated, inserted second sentence concerning funds obligated to implement the settlement agreement, near beginning of third sentence inserted "settlement proceeds not otherwise designated for a specific use pursuant to court order, amounts awarded in judgment", and near end of third sentence inserted "no later than the first business day in January of the subsequent biennium"; and made minor changes in style. Amendment effective October 1, 2021.

2005 Amendment: Chapter 280 deleted former (2) that read: "(2) All civil fines, costs, and fees received or recovered by the attorney general pursuant to this part must be deposited into a state special revenue account to the credit of the attorney general and must be used to defray the expenses of the office of the attorney general in discharging its regulatory powers and duties in relation to this part. Any excess civil fines, costs, or fees must be transferred to the general fund"; and made minor changes in style. Amendment effective July 1, 2005.

Effective Date: Section 4, Ch. 136, L. 2003, provided: "[This act] is effective July 1, 2003."

30-14-227. Transfer or sale of a franchise — continuance of contracts.

Compiler's Comments

Effective Date: This section is effective October 1, 2021.

Applicability: Section 3, Ch. 224, L. 2021, provided: "[This act] applies to franchise agreements entered into or renewed on or after [the effective date of this act]." Effective October 1, 2021.

30-14-228. Acceptance of United States currency — retailers — government subdivision.

Compiler's Comments

Effective Date: This section is effective October 1, 2023.

Part 3
Motion Picture Fair Trade Practices Act

Part Compiler's Comments

Source: Sections 30-14-301 and 30-14-303 through 30-14-308 are based on Title 18, chapter 77, Idaho Code. Section 30-14-302 is similar to section 19.58.010, Revised Codes of Washington.

Severability: Section 9, Ch. 214, L. 1981, was a severability section.

30-14-303. Definitions.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Part 4
Uniform Trade Secrets Act

Part Compiler's Comments

Source: Chapter 104, L. 1985, is based on the Uniform Trade Secrets Act, 14 U.L.A. 541-551, promulgated by the National Conference of Commissioners on Uniform State Laws.

Severability: Section 10, Ch. 104, L. 1985, was a severability section.

Part Case Notes

No Proof of Improper Acquisition, Effort to Maintain Confidentiality, or Damages — No Violation of Montana Uniform Trade Secrets Act: A software developer made no legal copyright, trademark, or patent protection, did not encrypt or make any effort to maintain confidentiality of coding, and did not include proprietary notice or designation in software that he created. An unrebutted expert testified that the functionality and processes of the software were generally known or readily ascertainable, and the software developer did not make a showing that he suffered damages or detriment from his former employer's use of a similar software. The District Court found on summary judgment that the developer's claim under the Montana Uniform Trade Secrets Act failed. On appeal, the Supreme Court affirmed. Assoc. Management Serv., Inc. v. Ruff, 2018 MT 182, 392 Mont. 139, 424 P.3d 571.

No Constitutional Right to Privacy for Nonhuman Entities — Protection of Trade Secrets Under Other Constitutional and Statutory Schemes: Montana's constitutional individual privacy exception to the public's right to know is limited to natural human individuals only and does not apply to nonhuman entities such as corporations. However, nothing in Art. II, sec. 9, Mont. Const., requires disclosure of trade secrets and other confidential proprietary information when that data is protected from disclosure elsewhere in the state or federal constitution or by statute.

Great Falls Tribune v. Mont. Pub. Serv. Comm'n, 2003 MT 359, 319 M 38, 82 P3d 876 (2003), overruling Mtn. States Tel. & Tel. v. Dept. of Public Service Regulation, 194 M 277, 634 P2d 181 (1981), and its progeny to the extent that those decisions relied on the constitutional balancing test of the right to individual privacy against the public's right to examine documents or observe governmental deliberations as a basis of protecting trade secrets and other confidential proprietary information of nonhuman entities.

30-14-402. Definitions.

Commissioners' Notes

One of the broadly stated policies behind trade secret law is "the maintenance of standards of commercial ethics." Kewanee Oil Co. v. Bicron Corp., 416 U.S. 470 (1974). The Restatement of Torts, Section 757, Comment (f), notes: "A complete catalogue of improper means is not possible," but Section 1(1) [30-14-402(1)] includes a partial listing.

Proper means include:

1. Discovery by independent invention;
2. Discovery by "reverse engineering", that is, by starting with the known product and working backward to find the method by which it was developed. The acquisition of the known product must of course, also be by a fair and honest means, such as purchase of the item on the open market for reverse engineering to be lawful;
3. Discovery under a license from the owner of the trade secret;
4. Observation of the item in public use or on public display;
5. Obtaining the trade secret from published literature;

Improper means could include otherwise lawful conduct which is improper under the circumstances; e.g., an airplane overflight used as aerial reconnaissance to determine the competitor's plant layout during construction of the plant. E. I. du Pont de Nemours & Co., Inc. v. Christopher, 431 F.2d 1012 (CA 5, 1970), cert. den. 400 U.S. 1024 (1970). Because the trade secret can be destroyed through public knowledge, the unauthorized disclosure of a trade secret is also a misappropriation.

The type of accident or mistake that can result in a misappropriation under Section 1(2)(ii)(C) [30-14-402(2)(b)(iii)] involves conduct by a person seeking relief that does not constitute a failure of efforts that are reasonable under the circumstances to maintain its secrecy under Section 1(4)(ii) [30-14-402(4)(b)].

The definition of "trade secret" contains a reasonable departure from the Restatement of Torts (First) definition which required that a trade secret be "continuously used in one's business." The broader definition in the proposed Act extends protection to a plaintiff who has not yet had an opportunity or acquired the means to put a trade secret to use. The definition includes information that has commercial value from a negative viewpoint, for example the results of lengthy and expensive research which proves that a certain process will not work could be of great value to a competitor.

Cf. Telex Corp. v. IBM Corp., 510 F.2d 894 (CA 10, 1975) per curiam, cert. dismissed 423 U.S. 802 (1975) (liability imposed for developmental cost savings with respect to product not marketed). Because a trade secret need not be exclusive to confer a competitive advantage, different independent developers can acquire rights in the same trade secret.

The words "method, technique" are intended to include the concept of "know-how."

The language "not being generally known to and not being readily ascertainable by proper means by other persons" does not require that information be generally known to the public for trade secret rights to be lost. If the principal person who can obtain economic benefit from information is aware of it, there is no trade secret. A method of casting metal, for example, may be unknown to the general public but readily known within the foundry industry.

Information is readily ascertainable if it is available in trade journals, reference books, or published materials. Often, the nature of a product lends itself to being readily copied as soon as it is available on the market. On the other hand, if reverse engineering is lengthy and expensive, a person who discovers the trade secret through reverse engineering can have a trade secret in the information obtained from reverse engineering.

Finally, reasonable efforts to maintain secrecy have been held to include advising employees of the existence of a trade secret, limiting access to a trade secret on "need to know basis", and controlling plant access. On the other hand, public disclosure of information through display, trade journal publications, advertising, or other carelessness can preclude protection.

The efforts required to maintain secrecy are those "reasonable under the circumstances." The courts do not require that extreme and unduly expensive procedures be taken to protect trade secrets against flagrant industrial espionage. See E. I. du Pont de Nemours & Co., Inc. v. Christopher, supra. It follows that reasonable use of a trade secret including controlled disclosure to employees and licensees is consistent with the requirement of relative secrecy.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

No Constitutional Right to Privacy for Nonhuman Entities — Protection of Trade Secrets Under Other Constitutional and Statutory Schemes: Montana's constitutional individual privacy exception to the public's right to know is limited to natural human individuals only and does not apply to nonhuman entities such as corporations. However, nothing in Art. II, sec. 9, Mont. Const., requires disclosure of trade secrets and other confidential proprietary information when that data is protected from disclosure elsewhere in the state or federal constitution or by statute. Great Falls Tribune v. Mont. Pub. Serv. Comm'n, 2003 MT 359, 319 M 38, 82 P3d 876 (2003), overruling Mtn. States Tel. & Tel. v. Dept. of Public Service Regulation, 194 M 277, 634 P2d 181 (1981), and its progeny to the extent that those decisions relied on the constitutional balancing test of the right to individual privacy against the public's right to examine documents or observe governmental deliberations as a basis of protecting trade secrets and other confidential proprietary information of nonhuman entities.

Public Service Commission Rules Creating Impermissible Presumption of Confidentiality in Trade Secrets: Several media organizations sought access to power company documents filed with the Public Service Commission. Applying its administrative rules, the Commission evaluated the power company's claims of confidentiality against basic trade secret law, found that the company had met the initial burden of establishing trade secrets, and concluded that because the media had presented no evidence or argument to the contrary, the company information was entitled to constitutional protection as a matter of law. The Supreme Court disagreed. To the extent that the Commission's rules relied on mere company representations that the information contained trade secrets, the Commission unconstitutionally shifted the initial burden of proof to the public to challenge the confidentiality claims, creating a presumption of confidentiality that directly conflicted with the public's right to view public records and the Commission's duty to make its records available to the public. The court held that a nonhuman entity seeking protective measures for alleged confidential materials filed with a governmental regulating agency must support its claim with a supporting affidavit making a prima facie showing that the materials constitute property rights that are protected by due process. Further, the showing must be more than conclusory and specific enough for the Commission, any objecting parties, and reviewing authorities to clearly understand the nature and basis of the confidentiality claim. The agency then must review the materials at the time of filing, in accordance with subsection (4)(b) of this section and supporting case law, and make an independent determination whether the materials are in fact property rights entitled to due process protection. To the extent that Commission rules required less, the court directed revision of Commission rules to comport with this holding. Great Falls Tribune v. Mont. Pub. Serv. Comm'n, 2003 MT 359, 319 M 38, 82 P3d 876 (2003).

Punitive Damages Available: A court may award exemplary damages and attorney fees under Montana's Uniform Trade Secrets Act even if a jury has decided that punitive damages are not available. The Montana Legislature did not incorporate a definition of punitive damages into the Act. Yeti by Molly, Ltd. v. Deckers Outdoor Corp., 259 F3d 1101 (9th Cir. 2001).

30-14-403. Injunctive relief — royalty.

Commissioners' Notes

Injunctions restraining future use and disclosure of misappropriated trade secrets frequently are sought. Although punitive perpetual injunctions have been granted, e.g., Elcor Chemical Corp. v. Agri-Sul, Inc., 494 S.W. 2d 204 (Tex.Civ.App.1973), Section 2(a) [30-14-403(1)] of this Act adopts the position of the trend of authority limiting the duration of injunctive relief to the extent of the temporal advantage over good faith competitors gained by a misappropriator. See, e.g., K-2 Ski Co. v. Head Ski Co., Inc., 506 F.2d 471 (CA9, 1974) (maximum appropriate duration of both temporary and permanent injunctive relief is period of time it would have taken defendant to discover trade secrets lawfully through either independent development or reverse engineering of plaintiff's products).

The general principle of section 2(a) and (b) [30-14-403(1) and (2)] is that an injunction should last for as long as is necessary, but no longer than is necessary, to eliminate the commercial advantage or "lead time" with respect to good faith competitors that a person has obtained through misappropriation. Subject to any additional period of restraint necessary to negate lead time, an injunction accordingly should terminate when a former trade secret becomes either generally known to good faith competitors or generally knowable to them because of the lawful availability of products that can be reverse engineered to reveal a trade secret.

For example, assume that A has a valuable trade secret of which B and C, the other industry members, are originally unaware. If B subsequently misappropriates the trade secret and is enjoined from use, but C later lawfully reverse engineers the trade secret, the injunction restraining B is subject to termination as soon as B's lead time has been dissipated. All of the persons who could derive economic value from use of the information are now aware of it, and there is no longer a trade secret under section 1(4) [30-14-402(4)]. It would be anti-competitive to continue to restrain B after any lead time that B had derived from misappropriation had been removed.

If a misappropriator either has not taken advantage of lead time or good faith competitors already have caught up with a misappropriator at the time that a case is decided, future disclosure and use of a former trade secret by a misappropriator will not damage a trade secret owner and no injunctive restraint of future disclosure and use is appropriate. See, e.g., Northern Petrochemical Co. v. Tomlinson, 484 F.2d 1057 (CA7, 1973) (affirming trial court's denial of preliminary injunction in part because an explosion at its plant prevent an alleged misappropriator from taking advantage of lead time); Kubik, Inc. v. Hull, 185 USPQ 391 (Mich. App.1974) (discoverability of trade secret by lawful reverse engineering made by injunctive relief punitive rather than compensatory).

Section 2(b) [30-14-403(2)] deals with a distinguishable situation in which future use by a misappropriator will damage a trade secret owner but an injunction against future use nevertheless is unreasonable under the particular circumstances of a case. Situations in which this unreasonableness can exist include the existence of an overriding public interest which requires the denial of a prohibitory injunction against future damaging use and a person's reasonable reliance upon acquisition of a misappropriated trade secret in good faith and without reason to know of its prior misappropriation that would be prejudiced by a prohibitory injunction against future damaging use. Republic Aviation Corp. v. Schenk, 152 USPQ 830 (N.Y.Sup. Ct.1967) illustrates the public interest justification for withholding prohibitory injunctive relief. The court considered that enjoining a misappropriator from supplying the U.S. with an aircraft weapons control system would have endangered military personnel in Viet Nam. The prejudice to a good faith third party justification for withholding prohibitory injunctive relief can arise upon a trade secret owner's notification to a good faith third party that the third party has knowledge of a trade secret as a result of misappropriation by another. This notice suffices to make the third party a misappropriator thereafter under section 1(2)(ii)(B)(I) [30-14-402(2)(b)(ii)(A)]. In weighing an aggrieved person's interests and the interests of a third party who has relied in good faith upon his or her ability to utilize information, a court may conclude that restraining future use of the information by the third party is unwarranted. With respect to innocent acquirers of misappropriated trade secrets, section 2(b) [30-14-403(2)] is consistent with the principle of 4 Restatement Torts (First) § 758(b) (1939), but rejects the Restatement's literal conferral of absolute immunity upon all third parties who have paid value in good faith for a trade secret misappropriated by another. The position taken by the Uniform Act is supported by Forest Laboratories, Inc. v. Pillsbury Co., 452 F.2d 621 (CA7, 1971) in which a defendant's purchase of assets of a corporation to which a trade secret had been disclosed in confidence was not considered to confer immunity upon the defendant.

When section 2(b) [30-14-403(2)] applies, a court is given discretion to substitute an injunction conditioning future use upon payment of a reasonable royalty for an injunction prohibiting future use. Like all injunctive relief for misappropriation, a royalty order injunction is appropriate only if a misappropriator has obtained a competitive advantage through misappropriation and only for the duration of that competitive advantage. In some situations, typically those involving good faith acquirers of trade secrets misappropriated by others, a court may conclude that the same considerations that render a prohibitory injunction against future use inappropriate also render a royalty order injunction inappropriate. See, generally, Prince Manufacturing, Inc. v. Automatic Partner, Inc., 198 USPQ 618 (N.J.Super.Ct.1976) (purchaser of misappropriator's assets from receiver after trade secret disclosed to public through sale of product not subject to liability for misappropriation).

Section 2(c) [30-14-403(3)] authorizes mandatory injunctions requiring that a misappropriator return the fruits of misappropriation to an aggrieved person, e.g., the return of stolen blueprints or the surrender of surreptitious photographs or recordings.

Where more than one person is entitled to trade secret protection with respect to the same information, only that one from whom misappropriation occurred is entitled to a remedy.

Compiler's Comments

1995 Amendment: Chapter 269 in (2), at beginning of first sentence, substituted "In exceptional circumstances" for "If the court determines that it would be unreasonable to prohibit future use" and inserted second sentence defining exceptional circumstances; and made minor changes in style.

Applicability: Section 4, Ch. 269, L. 1995, provided: "With respect to a continuing misappropriation that began prior to [the effective date of this act] [October 1, 1995], [this act] does not apply to the continuing misappropriation that occurs after [the effective date of this act] [October 1, 1995]."

30-14-404. Damages.

Commissioners' Notes

Like injunctive relief, a monetary recovery for trade secret misappropriation is appropriate only for the period in which information is entitled to protection as a trade secret, plus the additional period, if any, in which a misappropriator retains an advantage over good faith competitors because of misappropriation. Actual damage to a complainant and unjust benefit to a misappropriator are caused by misappropriation during this time alone. See Conmar Products Corp. v. Universal Slide Fastener Co., 172 F.2d 150 (CA2, 1949) (no remedy for period subsequent to disclosure of trade secret by issued patent); Carboline Co. v. Jarboe, 454 S.W.2d 540 (Mo.1970) (recoverable monetary relief limited to period that it would have taken misappropriator to discover trade secret without misappropriation). A claim for actual damages and net profits can be combined with a claim for injunctive relief, but, if both claims are granted, the injunctive relief ordinarily will preclude a monetary award for a period in which the injunction is effective.

As long as there is no double counting, Section 3(a) [30-14-404(1)] adopts the principle of the recent cases allowing recovery of both a complainant's actual losses and a misappropriator's unjust benefit that are caused by misappropriation. E.g., Tri-Tron International v. Velto, 525 F.2d 432 (CA9, 1975) (complainant's loss and misappropriator's benefit can be combined). Because certain cases may have sanctioned double counting in a combined award of losses and unjust benefit, e. g., Telex Corp. v. IBM Corp., 510 F.2d 894 (CA10, 1975) (per curiam), cert. dismissed, 423 U.S. 802 (1975) (IBM recovered rentals lost due to displacement by misappropriator's products without deduction for expenses saved by displacement; as a result of rough approximations adopted by the trial judge, IBM also may have recovered developmental costs saved by misappropriator through misappropriation with respect to the same customers), the Act adopts an express prohibition upon the counting of the same item as both a loss to a complainant and an unjust benefit to a misappropriator.

Monetary relief can be appropriate whether or not injunctive relief is granted under section 2 [30-14-403]. If a person charged with misappropriation has acquired knowledge of a trade secret in good faith without reason to know of its misappropriation by another, however, the same considerations that can justify denial of all injunctive relief also can justify denial of all monetary relief. See Conmar Products Corp. v. Universal Slide Fastener Co., 172 F.2d 1950 (CA2, 1949) (no relief against new employer of employee subject to contractual obligation not to disclose former employer's trade secrets where new employer innocently had committed $40,000 to develop the trade secrets prior to notice of misappropriation).

If willful and malicious misappropriation is found to exist, section 3(b) [30-14-404(2)] authorizes the court to award a complainant exemplary damages in addition to the actual recovery under section 3(a) [30-14-404(1)] an amount not exceeding twice that recovery. This provision follows federal patent law in leaving discretionary trebling to the judge even though there may be a jury, compare 35 U.S.C. § 284 (1976).

Whenever more than one person is entitled to trade secret protection with respect to the same information, only that one from whom misappropriation occurred is entitled to a remedy.

Compiler's Comments

1995 Amendment: Chapter 269 in first sentence of (1) substituted exception clause for "In addition to or in lieu of injunctive relief", in second sentence, at beginning, substituted clause authorizing damages, including actual loss caused by misappropriation, for "A complainant also may recover for", and inserted third sentence regarding measurement of damages; and made minor changes in style.

Applicability: Section 4, Ch. 269, L. 1995, provided: "With respect to a continuing misappropriation that began prior to [the effective date of this act][October 1, 1995], [this act] does not apply to the continuing misappropriation that occurs after [the effective date of this act] [October 1, 1995]."

Case Notes

No Error in Finding of No Unjust Enrichment: Plaintiff contended that defendant company was unjustly enriched when a promissory note was unilaterally entered into by one of the owners of defendant business without the knowledge or authorization of the other owners. The District Court held that the company was not unjustly enriched, and on appeal the Supreme Court affirmed. The company had no knowledge of the speculative transaction between plaintiff and the owner until shortly before suit was filed, so plaintiff could show no misconduct or fault on the company's part, nor was the owner authorized to engage in entering promissory notes on the company's behalf. Thus, the District Court did not err in holding that the company was not unjustly enriched. Estate of Pruyn v. Axmen Propane, Inc., 2009 MT 448, 354 M 208, 223 P3d 845 (2009). See also Maxted v. Barrett, 198 M 81, 643 P2d 1161 (1982).

Punitive Damages Available: A court may award exemplary damages and attorney fees under Montana's Uniform Trade Secrets Act even if a jury has decided that punitive damages are not available. The Montana Legislature did not incorporate a definition of punitive damages into the Act. Yeti by Molly, Ltd. v. Deckers Outdoor Corp., 259 F3d 1101 (9th Cir. 2001).

30-14-405. Costs and attorney fees.

Commissioners' Notes

Section 4 [30-14-405] allows a court to award reasonable attorney fees to a prevailing party in specified circumstances as a deterrent to specious claims of misappropriation, to specious efforts by a misappropriator to terminate injunctive relief, and to willful and malicious misappropriation. In the latter situation, the court should take into consideration the extent to which a complainant will recover exemplary damages in determining whether additional attorney's fees should be awarded. Again, patent law is followed in allowing the judge to determine whether attorney's fees should be awarded even if there is a jury, compare 35 U.S.C. Section 285 (1976).

Compiler's Comments

Montana Changes: Montana allows an award of reasonable costs.

30-14-406. Preservation of secret.

Commissioners' Notes

If reasonable assurances of maintenance of secrecy could not be given, meritorious trade secret litigation would be chilled. In fashioning safeguards of confidentiality, a court must ensure that a respondent is provided sufficient information to present a defense and a trier of fact sufficient information to resolve the merits. In addition to the illustrative techniques specified in the statute, courts have protected secrecy in these cases by restricting disclosures to a party's counsel and his or her assistants and by appointing a disinterested expert as a special master to hear secret information and report conclusions to the court.

30-14-407. Statute of limitations.

Commissioners' Notes

There presently is a conflict of authority as to whether trade secret misappropriation is a continuing wrong. Compare Monlith Portland Midwest Co. v. Kaiser Aluminum & Chemical Corp., 407 F.2d 288 (CA9, 1969) (no continuing wrong under California law—limitation period upon all recovery begins upon initial misappropriation) with Underwater Storage, Inc. v. U. S. Rubber Co., 371 F.2d 950 (CADC, 1966), cert. den., 386 U.S. 911 (1967) (continuing wrong under general principles—limitation period with respect to a specific act of misappropriation begins at the time that the act of misappropriation occurs).

This Act rejects a continuing wrong approach to the statute of limitations but delays the commencement of the limitation period until an aggrieved person discovers or reasonably should have discovered the existence of misappropriation. If objectively reasonable notice of misappropriation exists, three years is sufficient time to vindicate one's legal rights.

30-14-408. Effect on other law.

Commissioners' Notes

This Act is not a comprehensive remedy. It applies to duties imposed by law in order to protect competitively significant secret information. It does not apply to duties voluntarily assumed through an express or an implied-in-fact contract. The enforceability of covenants not to disclose trade secrets and covenants not to compete that are intended to protect trade secrets, for example, are governed by other law. The Act also does not apply to duties imposed by law that are not dependent upon the existence of competitively significant secret information, like an agent's duty of loyalty to his or her principal.

Compiler's Comments

1995 Amendment: Chapter 269 in (1), at beginning, inserted exception clause and substituted "providing civil remedies" for "pertaining to civil liability"; in (2)(a) substituted "remedies, whether or" for "or other civil liability or relief that is"; in (2)(b), at beginning, substituted "other civil remedies that are not based upon" for "criminal liability for"; and inserted (2)(c) regarding criminal remedies; and made minor changes in style.

Applicability: Section 4, Ch. 269, L. 1995, provided: "With respect to a continuing misappropriation that began prior to [the effective date of this act] [October 1, 1995], [this act] does not apply to the continuing misappropriation that occurs after [the effective date of this act] [October 1, 1995]."

Part 5
Personal Solicitation Sales

Part Case Notes

Single Instance of Telephone or Home Contact Not Considered Personal Solicitation: Bradley contacted Johnson, a motor vehicle dealer, looking for a specific kind of vehicle. Johnson in turn contacted Muffitt, a salesman at another dealership, to inquire whether Muffitt had any vehicles meeting Bradley's wishes. Muffitt contacted Bradley by telephone and told Bradley that Muffitt's dealership had a vehicle that might be of interest. Bradley invited Muffitt to bring the vehicle to Bradley's home, which Muffitt did, and after test-driving the vehicle, Bradley decided to purchase it. After making 2 months' payments, Bradley decided not to keep the vehicle and sought to cancel the contract under 30-14-504 on grounds that the sale was governed by the law on personal solicitation sales and that Bradley thus had the right to cancel the sale within the cooling-off period allowed by that statute. The Supreme Court concluded that this part does not apply to this one-time sale by telephone or in person at the buyer's home because Bradley did not bring forth any evidence that the dealership regularly attempted sales by telephone or in person, other than at its place of business. Bradley v. N. Country Auto & Marine, 2000 MT 81, 299 M 157, 999 P2d 308, 57 St. Rep. 348 (2000).

30-14-501. Purpose.

Compiler's Comments

2003 Amendment: Chapter 322 substituted "persons" for "consumers". Amendment effective April 15, 2003.

30-14-502. Definitions.

Compiler's Comments

2003 Amendment: Chapter 322 in definition of personal solicitation substituted "seller to sell goods or services" for "seller who regularly engages in transactions of the same kind to sell goods or services which are primarily for personal, family, or household purposes"; in (2)(a) inserted "prior to the attempted sale"; inserted (2)(e) relating to certain attempted sales over $5,000; and made minor changes in style. Amendment effective April 15, 2003.

1981 Amendment: Deleted "child" after "minor" in (2)(c).

Case Notes

Single Instance of Telephone or Home Contact Not Considered Personal Solicitation: Bradley contacted Johnson, a motor vehicle dealer, looking for a specific kind of vehicle. Johnson in turn contacted Muffitt, a salesman at another dealership, to inquire whether Muffitt had any vehicles meeting Bradley's wishes. Muffitt contacted Bradley by telephone and told Bradley that Muffitt's dealership had a vehicle that might be of interest. Bradley invited Muffitt to bring the vehicle to Bradley's home, which Muffitt did, and after test-driving the vehicle, Bradley decided to purchase it. After making 2 months' payments, Bradley decided not to keep the vehicle and sought to cancel the contract under 30-14-504 on grounds that the sale was governed by the law on personal solicitation sales and that Bradley thus had the right to cancel the sale within the cooling-off period allowed by that statute. The Supreme Court concluded that Title 30, ch. 14, part 5, does not apply to this one-time sale by telephone or in person at the buyer's home because Bradley did not bring forth any evidence that the dealership regularly attempted sales by telephone or in person, other than at its place of business. Bradley v. N. Country Auto & Marine, 2000 MT 81, 299 M 157, 999 P2d 308, 57 St. Rep. 348 (2000).

30-14-503. Disclosure obligation.

Compiler's Comments

2003 Amendment: Chapter 322 at end of first sentence deleted "and that he wishes to demonstrate or sell the identified goods or services"; deleted former fourth sentence that read: "Nonprofit organizations are exempt from the requirements of this section"; inserted last sentence providing for a civil fine for violation; and made minor changes in style. Amendment effective April 15, 2003.

30-14-504. Buyer's right to cancel — time allowed — notice — return of goods.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Case Notes

Single Instance of Telephone or Home Contact Not Considered Personal Solicitation: Bradley contacted Johnson, a motor vehicle dealer, looking for a specific kind of vehicle. Johnson in turn contacted Muffitt, a salesman at another dealership, to inquire whether Muffitt had any vehicles meeting Bradley's wishes. Muffitt contacted Bradley by telephone and told Bradley that Muffitt's dealership had a vehicle that might be of interest. Bradley invited Muffitt to bring the vehicle to Bradley's home, which Muffitt did, and after test-driving the vehicle, Bradley decided to purchase it. After making 2 months' payments, Bradley decided not to keep the vehicle and sought to cancel the contract under this section on grounds that the sale was governed by the law on personal solicitation sales and that Bradley thus had the right to cancel the sale within the cooling-off period allowed by that statute. The Supreme Court concluded that Title 30, ch. 14, part 5, does not apply to this one-time sale by telephone or in person at the buyer's home because Bradley did not bring forth any evidence that the dealership regularly attempted sales by telephone or in person, other than at its place of business. Bradley v. N. Country Auto & Marine, 2000 MT 81, 299 M 157, 999 P2d 308, 57 St. Rep. 348 (2000).

30-14-505. Notice of right to cancel.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

30-14-506. Repayment to buyer — retention of goods by buyer — court award, costs, and attorney fees.

Compiler's Comments

2003 Amendment: Chapter 322 in (3) near end increased award from $100 to $500; and made minor changes in style. Amendment effective April 15, 2003.

30-14-507. Redelivery of goods.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Part 6

Sale of Imitation Indian Articles

30-14-602. Articles to be designated and segregated.

Compiler's Comments

1991 Amendment: Inserted third sentence requiring that articles be displayed near a sign designating the articles as imitation; and made minor changes in style.

Part 7

Fraudulent Financing of Mining and Oil Companies

30-14-702. Application.

Compiler's Comments

1983 Amendment: In middle of second sentence, changed "investment department" to "securities commissioner".

Part 9
Price Discrimination

Part Compiler's Comments

Source: This part was requested by the Joint Interim Subcommittee on Marketing of Motor Fuels. See 1990 interim committee report.

Saving Clause: Section 8, Ch. 486, L. 1991, was a saving clause.

Severability: Section 9, Ch. 486, L. 1991, was a severability clause.

30-14-901. Discrimination in price.

Compiler's Comments

2005 Amendment: Chapter 130 at end of (5) after "through" inserted "4 and". Amendment effective October 1, 2005.

Part 11
Plain Language in Contracts

Part Compiler's Comments

Delayed Applicability: Section 8, Ch. 615, L. 1985, provided: "This act applies to consumer contracts [as defined in 30-14-1102] entered into after July 1, 1987."

30-14-1104. Scope.

Compiler's Comments

1987 Amendment: In (2)(c) substituted language exempting an insurance policy subject to Title 33 for "consumer transactions subject to the provisions of 33-15-321 through 33-15-329". The amendment applies to policies and contracts, as defined in 30-14-1102, entered into after July 1, 1987.

30-14-1112. Limitations on remedies.

Compiler's Comments

2009 Amendment: Chapter 56 made section gender neutral; and made minor changes in style. Amendment effective October 1, 2009.

Part 12
Wheelchair Warranties

Part Compiler's Comments

Severability: Section 9, Ch. 259, L. 1995, was a severability clause.

Applicability: Section 10, Ch. 259, L. 1995, provided: "[This act] does not apply to a wheelchair as defined by [section 2] [30-14-1202] sold to a consumer as defined by [section 2] [30-14-1202] before October 1, 1995."

Part 13
Service Contracts — Vehicle Theft Protection Products

Part Compiler's Comments

Effective Date: Section 6, Ch. 162, L. 2007, provided: "[This act] is effective on passage and approval." Approved April 6, 2007.

Applicability: Section 7, Ch. 162, L. 2007, provided: "[This act] applies to service contracts issued on or after January 1, 2008."

30-14-1301. Definitions.

Compiler's Comments

2023 Amendment: See 2023 Session Law for amendment made by sec. 1, Ch. 525, L. 2023. Amendment effective October 1, 2023.

30-14-1302. Requirements for conducting business.

Compiler's Comments

2023 Amendment: See 2023 Session Law for amendment made by sec. 2, Ch. 525, L. 2023. Amendment effective October 1, 2023.

30-14-1303. Required disclosures — reimbursement insurance policy.

Compiler's Comments

2023 Amendment: See 2023 Session Law for amendment made by sec. 3, Ch. 525, L. 2023. Amendment effective October 1, 2023.

30-14-1305. Required disclosure — vehicle theft protection product warranties.

Compiler's Comments

Effective Date: This section is effective October 1, 2023.

Part 14
Montana Telemarketing Registration and Fraud Prevention Act

Part Compiler's Comments

Effective Date: Section 17(2), Ch. 342, L. 1999, provided that this part, except for 30-14-1402(3), is effective October 1, 1999.

30-14-1402. Purpose — scope — rulemaking.

Compiler's Comments

Effective Dates: (1) Section 17(1), Ch. 342, L. 1999, provided that [section 2(3)], enacting 30-14-1402(3), is effective on passage and approval. Approved April 19, 1999.

(2) Section 17(2), Ch. 342, L. 1999, provided that [section 2(1) and (2)], enacting 30-14-1402(1) and (2), is effective October 1, 1999.

Administrative Rules

ARM 23.19.501 Telemarketing definitions.

30-14-1403. Definitions.

Compiler's Comments

2005 Amendment: Chapter 280 in definition of department substituted "department of justice" for "department of administration" and substituted "2-15-2001" for "2-15-1001". Amendment effective July 1, 2005.

2001 Amendment: Chapter 483 in definition of department substituted reference to department of administration for reference to department of commerce and substituted "2-15-1001" for "2-15-1801". Amendment effective July 1, 2001.

Administrative Rules

ARM 23.19.501 Definitions.

30-14-1404. Registration of sellers or telemarketers.

Administrative Rules

ARM 23.19.502 Forms and procedures for initial registration and bonding.

ARM 23.19.503 Forms and procedures for registration renewal.

Attorney General's Opinions

Telemarketers Exempt From Registration and Bonding Requirements Subject to Other Statutory Provisions: The 1999 Montana Telemarketing Registration and Fraud Prevention Act provided that certain sellers and marketers are exempt from the registration and bonding requirements of the Act. However, telemarketers who are exempt from the registration and bonding requirements are nevertheless subject to the other provisions of the Act, such as recordkeeping requirements, disclosure and contract requirements, and the regulation of prohibited and abusive acts and practices. 49 A.G. Op. 6 (2001).

30-14-1405. Exemptions from registration and bonding.

Attorney General's Opinions

Telemarketers Exempt From Registration and Bonding Requirements Subject to Other Statutory Provisions: The 1999 Montana Telemarketing Registration and Fraud Prevention Act provided that certain sellers and marketers are exempt from the registration and bonding requirements of the Act. However, telemarketers who are exempt from the registration and bonding requirements are nevertheless subject to the other provisions of the Act, such as recordkeeping requirements, disclosure and contract requirements, and the regulation of prohibited and abusive acts and practices. 49 A.G. Op. 6 (2001).

30-14-1406. Telemarketing fraud consumer awareness program.

Administrative Rules

ARM 23.19.504 Telemarketing fraud consumer awareness program.

30-14-1407. Authority of department and county attorney.

Compiler's Comments

2005 Amendments — Composite Section: Chapter 130 in (2) at end of first sentence and in (3) at end of first sentence substituted "30-14-1406" for "30-14-1405" (amendment in (3) rendered void by Ch. 280 amendment). Amendment effective October 1, 2005.

Chapter 280 in (1) at beginning after "The department" deleted "the attorney general"; in (2) at end of first sentence substituted "30-14-1406" for "30-14-1405"; deleted former (3) that read: "(3) All civil fines, costs, and fees received or recovered by the attorney general pursuant to this section must be deposited into the state special revenue account to the credit of the attorney general and must be used to defray the expenses of the office of the attorney general in discharging its duties in relation to this section and to establish a telemarketing fraud consumer awareness program similar to the program authorized in 30-14-1405. Any excess civil fines, costs, or fees must be deposited in the general fund"; and made minor changes in style. Amendment effective July 1, 2005.

Administrative Rules

ARM 23.19.505 Civil action enforcement procedure.

30-14-1408. Recordkeeping requirements.

Attorney General's Opinions

Telemarketers Exempt From Registration and Bonding Requirements Subject to Other Statutory Provisions: The 1999 Montana Telemarketing Registration and Fraud Prevention Act provided that certain sellers and marketers are exempt from the registration and bonding requirements of the Act. However, telemarketers who are exempt from the registration and bonding requirements are nevertheless subject to the other provisions of the Act, such as recordkeeping requirements, disclosure and contract requirements, and the regulation of prohibited and abusive acts and practices. 49 A.G. Op. 6 (2001).

30-14-1410. Disclosure and contract requirements.

Administrative Rules

ARM 23.19.505 Civil action enforcement procedure.

Attorney General's Opinions

Telemarketers Exempt From Registration and Bonding Requirements Subject to Other Statutory Provisions: The 1999 Montana Telemarketing Registration and Fraud Prevention Act provided that certain sellers and marketers are exempt from the registration and bonding requirements of the Act. However, telemarketers who are exempt from the registration and bonding requirements are nevertheless subject to the other provisions of the Act, such as recordkeeping requirements, disclosure and contract requirements, and the regulation of prohibited and abusive acts and practices. 49 A.G. Op. 6 (2001).

30-14-1411. Prohibited acts and practices.

Administrative Rules

ARM 23.19.505 Civil action enforcement procedure.

Attorney General's Opinions

Telemarketers Exempt From Registration and Bonding Requirements Subject to Other Statutory Provisions: The 1999 Montana Telemarketing Registration and Fraud Prevention Act provided that certain sellers and marketers are exempt from the registration and bonding requirements of the Act. However, telemarketers who are exempt from the registration and bonding requirements are nevertheless subject to the other provisions of the Act, such as recordkeeping requirements, disclosure and contract requirements, and the regulation of prohibited and abusive acts and practices. 49 A.G. Op. 6 (2001).

30-14-1412. Abusive acts and practices.

Compiler's Comments

2005 Amendment: Chapter 280 in (2) at beginning after "department" deleted "or the attorney general". Amendment effective July 1, 2005.

2001 Amendment: Chapter 350 inserted (1)(f) prohibiting intentionally blocking a person using caller identification or *69 from accessing the seller's or telemarketer's phone number, but allowing the providing of a reasonable substitute name and number accurately identifying the entity causing the call to be made and a working telephone number at which that entity's personnel can be contacted; and made minor changes in style. Amendment effective July 1, 2001.

Administrative Rules

ARM 23.19.505 Civil action enforcement procedure.

Attorney General's Opinions

Telemarketers Exempt From Registration and Bonding Requirements Subject to Other Statutory Provisions: The 1999 Montana Telemarketing Registration and Fraud Prevention Act provided that certain sellers and marketers are exempt from the registration and bonding requirements of the Act. However, telemarketers who are exempt from the registration and bonding requirements are nevertheless subject to the other provisions of the Act, such as recordkeeping requirements, disclosure and contract requirements, and the regulation of prohibited and abusive acts and practices. 49 A.G. Op. 6 (2001).

30-14-1413. Civil remedies — venue — burden of proof.

Compiler's Comments

2021 Amendment: Chapter 535 in (4)(b) after "part is the district court" substituted "in" for "of Lewis and Clark County or". Amendment effective October 1, 2021.

2005 Amendment: Chapter 280 in (4)(a) at beginning after "department" deleted "or the attorney general"; and made minor changes in style. Amendment effective July 1, 2005.

Administrative Rules

ARM 23.19.505 Civil action enforcement procedure.

Part 15
Unsolicited Advertisement Facsimile Transmissions

30-14-1501. Definitions — unsolicited advertisement through facsimile transmission prohibited — violation.

Compiler's Comments

Effective Date: This section is effective October 1, 2003.

Part 16
Telephone Solicitation No-Call List

Part Compiler's Comments

Effective Date: Section 8, Ch. 589, L. 2003, provided that this part is effective July 1, 2003.

30-14-1601. Definitions.

Compiler's Comments

2005 Amendment: Chapter 280 in definition of department substituted "department of justice" for "department of administration" and substituted "2-15-2001" for "2-15-1001". Amendment effective July 1, 2005.

30-14-1603. Department to provide for no-call list database — rules — inclusion of national database — database not public record — no cost to subscribers.

Compiler's Comments

2015 Amendment: Chapter 348 in (4) substituted "is confidential information as defined in 2-6-1002 and is protected from disclosure" for "may not be considered a public record pursuant to Title 2, chapter 6". Amendment effective October 1, 2015.

Severability: Section 72, Ch. 348, L. 2015, was a severability clause.

2005 Amendment: Chapter 280 in (1) near beginning of first sentence after "department shall" deleted "establish and" and deleted former second sentence that read: "The department shall have the database in operation no later than January 1, 2004"; in (2) in first sentence at beginning deleted "Not later than January 1, 2004" and near middle after "governing the" deleted "establishment of a"; and made minor changes in style. Amendment effective July 1, 2005.

Administrative Rules

ARM 23.19.506 Definitions.

ARM 23.19.507 State do-not-call database.

Part 17
Impediment of Identity Theft

Part Compiler's Comments

Severability: Section 11, Ch. 518, L. 2005, was a severability clause.

Effective Date: Section 12(1), Ch. 518, L. 2005, provided that this part is effective March 1, 2006.

Source: 30-14-1721 is from California Civil Code 1747.06.
30-14-1722 is from California Civil Code 1799.1b, 1747.9.
30-14-1701 through 30-14-1705 are from California Civil Code 1798.80 through 1798.84 (although last two sections of bill were amended out).

30-14-1701. Purpose.

Compiler's Comments

2007 Amendment: Chapter 276 inserted references to 30-14-1712 and 30-14-1713. Amendment effective October 1, 2007.

30-14-1702. Definitions.

Compiler's Comments

2007 Amendment: Chapter 276 in introductory clause inserted references to 30-14-1712 and 30-14-1713; inserted definitions of electronic mail message, internet, internet services provider, and website; and made minor changes in style. Amendment effective October 1, 2007.

30-14-1704. Computer security breach.

Compiler's Comments

2015 Amendment: Chapter 62 inserted (4)(b)(i)(D), (4)(b)(i)(E), and (4)(b)(i)(F) concerning medical record information, taxpayer identification number, and United States internal revenue service personal identification number; inserted (8) concerning electronic copies for the attorney general's consumer protection office; and made minor changes in style. Amendment effective October 1, 2015.

2007 Amendment: Chapter 180 in (4)(b)(i)(B) at end inserted "or tribal identification card number"; and made minor changes in style. Amendment effective October 1, 2007.

30-14-1712. Fraudulent electronic misrepresentation — penalties — exemption.

Compiler's Comments

Effective Date: This section is effective October 1, 2007.

30-14-1713. Remedies for fraudulent electronic misrepresentation.

Compiler's Comments

Effective Date: This section is effective October 1, 2007.

30-14-1726. Definitions.

Compiler's Comments

2011 Amendment: Chapter 42 in definition of consumer after "individual" inserted language concerning a parent, guardian, or conservator. Amendment effective October 1, 2011.

Severability: Section 12, Ch. 138, L. 2007, was a severability clause.

Effective Date: Section 14, Ch. 138, L. 2007, provided that this section is effective July 1, 2007.

30-14-1727. Placement of security freeze.

Compiler's Comments

2011 Amendment: Chapter 42 in (1)(b) at end deleted "by January 31, 2009"; inserted (2) concerning a credit freeze by a parent, guardian, or conservator; and made minor changes in style. Amendment effective October 1, 2011.

Severability: Section 12, Ch. 138, L. 2007, was a severability clause.

Effective Date: Section 14, Ch. 138, L. 2007, provided that this section is effective July 1, 2007.

30-14-1728. Consumer reporting agency requirements.

Compiler's Comments

Severability: Section 12, Ch. 138, L. 2007, was a severability clause.

Effective Date: Section 14, Ch. 138, L. 2007, provided that this section is effective July 1, 2007.

30-14-1729. Temporary lifting of security freeze — consumer requirements — consumer reporting agency duties — notification.

Compiler's Comments

2021 Amendment: Chapter 447 in (2)(c) after "6 a.m. to 9:30 p.m." deleted "mountain standard time or". Amendment effective on occurrence of contingency.

Severability: Section 12, Ch. 138, L. 2007, was a severability clause.

Effective Date: Section 14, Ch. 138, L. 2007, provided that this section is effective July 1, 2007.

30-14-1730. Consumer reporting agency security freeze removal procedures — notification.

Compiler's Comments

Severability: Section 12, Ch. 138, L. 2007, was a severability clause.

Effective Date: Section 14, Ch. 138, L. 2007, provided that this section is effective July 1, 2007.

30-14-1731. Third-party contacts.

Compiler's Comments

Severability: Section 12, Ch. 138, L. 2007, was a severability clause.

Effective Date: Section 14, Ch. 138, L. 2007, provided that this section is effective July 1, 2007.

30-14-1732. Security freeze removal procedure.

Compiler's Comments

Severability: Section 12, Ch. 138, L. 2007, was a severability clause.

Effective Date: Section 14, Ch. 138, L. 2007, provided that this section is effective July 1, 2007.

30-14-1733. Notice of rights.

Compiler's Comments

Severability: Section 12, Ch. 138, L. 2007, was a severability clause.

Effective Date: Section 14, Ch. 138, L. 2007, provided that this section is effective July 1, 2007.

30-14-1734. Exceptions — exemptions.

Compiler's Comments

Severability: Section 12, Ch. 138, L. 2007, was a severability clause.

Effective Date: Section 14, Ch. 138, L. 2007, provided that this section is effective July 1, 2007.

30-14-1735. Fees.

Compiler's Comments

Severability: Section 12, Ch. 138, L. 2007, was a severability clause.

Effective Date: Section 14, Ch. 138, L. 2007, provided that this section is effective July 1, 2007.

30-14-1736. Violations — penalties.

Compiler's Comments

Severability: Section 12, Ch. 138, L. 2007, was a severability clause.

Effective Date: Section 14, Ch. 138, L. 2007, provided that this section is effective July 1, 2007.

Part 20

Montana Consumer Debt Management Services Act

Part Compiler's Comments

Severability: Section 9, Ch. 272, L. 2005, was a severability clause.

Effective Date: Section 12, Ch. 272, L. 2005, provided: "[This act] is effective on passage and approval." Effective April 19, 2005.

Part Administrative Rules

Title 23, chapter 19, subchapter 10, ARM Consumer debt management.

30-14-2003. Definitions.

Compiler's Comments

Code Commissioner Instruction: In definition of department, pursuant to sec. 30, Ch. 280, L. 2005, the code commissioner substituted "department of justice provided for in 2-15-2001" for "department of administration provided for in 2-15-1001".

30-14-2004. Requirements for licensure — fees — rulemaking authority — refusal to grant license — suspension or revocation of license — rules.

Administrative Rules

ARM 23.19.1001 License fee.
ARM 23.19.1002 Bond requirement.
ARM 23.19.1003 List of accreditation and certification providers.
ARM 23.19.1004 Other requirements for a license.

30-14-2010. Requirements for debt management plans — rulemaking authority.

Administrative Rules

ARM 23.19.1005 Consultation and maintenance fees.

Part 21
Regulation of Debt Settlement Providers

Part Compiler's Comments

Effective Date: This part is effective October 1, 2009.

Part 22
Guaranteed Asset Protection Waiver Act

30-14-2201. Title — scope.

Compiler's Comments

Effective Date: Section 10, Ch. 313, L. 2013, provided: "[This act] is effective on passage and approval." Approved April 26, 2013.

Applicability: Section 11, Ch. 313, L. 2013, provided: "[This act] applies to guaranteed asset protection waivers issued on or after October 1, 2013."

30-14-2202. Definitions.

Compiler's Comments

Effective Date: Section 10, Ch. 313, L. 2013, provided: "[This act] is effective on passage and approval." Approved April 26, 2013.

Applicability: Section 11, Ch. 313, L. 2013, provided: "[This act] applies to guaranteed asset protection waivers issued on or after October 1, 2013."

30-14-2203. Requirements for offering guaranteed asset protection waivers.

Compiler's Comments

Effective Date: Section 10, Ch. 313, L. 2013, provided: "[This act] is effective on passage and approval." Approved April 26, 2013.

Applicability: Section 11, Ch. 313, L. 2013, provided: "[This act] applies to guaranteed asset protection waivers issued on or after October 1, 2013."

30-14-2204. Contractual liability or other insurance policies.

Compiler's Comments

Effective Date: Section 10, Ch. 313, L. 2013, provided: "[This act] is effective on passage and approval." Approved April 26, 2013.

Applicability: Section 11, Ch. 313, L. 2013, provided: "[This act] applies to guaranteed asset protection waivers issued on or after October 1, 2013."

30-14-2205. Disclosures.

Compiler's Comments

Effective Date: Section 10, Ch. 313, L. 2013, provided: "[This act] is effective on passage and approval." Approved April 26, 2013.

Applicability: Section 11, Ch. 313, L. 2013, provided: "[This act] applies to guaranteed asset protection waivers issued on or after October 1, 2013."

30-14-2206. Cancellation.

Compiler's Comments

Effective Date: Section 10, Ch. 313, L. 2013, provided: "[This act] is effective on passage and approval." Approved April 26, 2013.

Applicability: Section 11, Ch. 313, L. 2013, provided: "[This act] applies to guaranteed asset protection waivers issued on or after October 1, 2013."

30-14-2207. Commercial transactions exempted.

Compiler's Comments

Effective Date: Section 10, Ch. 313, L. 2013, provided: "[This act] is effective on passage and approval." Approved April 26, 2013.

Applicability: Section 11, Ch. 313, L. 2013, provided: "[This act] applies to guaranteed asset protection waivers issued on or after October 1, 2013."

Part 25
Motorsports Manufacturer Unfair Trade Practices

Part Compiler's Comments

Effective Date: This part is effective October 1, 2007.

Preamble: The preamble attached to Ch. 240, L. 2009, provided: "WHEREAS, the Legislature finds and declares that the distribution and sale of motorsports vehicles in this state affects the general economy of the state and the public interest, safety, and welfare and that the maintenance of strong and sound motorsports dealerships is essential to provide continuing and necessary reliable services to the consuming public in this state and to provide stable employment to the citizens of this state; and

WHEREAS, the Legislature finds that there can be a substantial disparity in bargaining power between motorsports manufacturers and their motorsports dealers and that in order to promote the public interest and the public welfare and in the exercise of the state's police power, it is necessary to regulate the relationship between motorsports manufacturers and motorsports dealers doing business in this state, not only for the protection of motorsports dealers but also for the benefit of the public in ensuring the continued availability and servicing of motorsports vehicles sold to the public; and

WHEREAS, the Legislature recognizes it is in the best interest of motorsports manufacturers and motorsports dealers to conduct business with each other in a fair, efficient, and competitive manner, and the Legislature has determined that the public interest is best served by motorsports dealers being assured of the ability to manage their business enterprises without unreasonable interference by motorsports manufacturers."

Severability: Section 5, Ch. 240, L. 2009, was a severability clause.

30-14-2501. Definitions.

Compiler's Comments

2009 Amendment: Chapter 240 inserted definitions of confidential or proprietary information, department, fleet, motor sports dealer, and motorsports manufacturer; in definition of actual price near beginning after "paid by" substituted "a motorsports dealer less any pecuniary benefit relating to a motorsports product paid or credited" for "the dealer less any incentive paid", after "by the" inserted "motorsports", after "manufacturer" deleted "whether paid", before "dealer" inserted "motorsports", and at end substituted "product" for "vehicle"; in definition of control at end of (b) after "otherwise" deleted "except as expressly provided under the franchise agreement"; deleted former definition of line-make that read: ""Line-make" means a type of motorsports vehicle produced by a manufacturer"; in definition of motorsports vehicle near end inserted "an off-highway vehicle as defined in 61-1-101"; in definition of operate after "manage a" inserted "motorsports"; in definition of own in first sentence after "interest in a" inserted "motorsports"; and made minor changes in style. Amendment effective April 16, 2009.

Applicability: Section 7, Ch. 240, L. 2009, provided: "[This act] applies to motorsports manufacturers and motorsports dealer transactions that occur on or after [the effective date of this section]." Effective April 16, 2009.

30-14-2502. Unfair trade practices — relationship between motorsports manufacturers and motorsports dealers.

Compiler's Comments

2017 Amendment: Chapter 93 in (1)(o) at beginning deleted "except as provided in 61-4-141"; and made minor changes in style. Amendment effective March 23, 2017.

2009 Amendment: Chapter 240 in both versions throughout section substituted reference to motorsports dealer, motorsports manufacturer, and motorsports vehicle for reference to dealer, manufacturer, and vehicle; in (1) near beginning of introductory clause after "provided for in" inserted reference to 30-14-103 and in two places after "manufacturer" deleted "distributor, factory branch, or factory representative"; in (1)(a)(iv) near middle of second sentence after "in writing" deleted "to the dealer"; in (1)(b)(i) near beginning after "deliver" inserted "to any of its motorsports dealers" and near middle after "order" substituted "any motorsports vehicle" for "to a dealer holding a franchise for a line or make of motorsports vehicles sold or distributed by the manufacturer a new vehicle"; in (1)(b)(iii) at beginning deleted "unreasonably"; in (1)(e) deleted former second sentence that read: "For purposes of this subsection, "confidential or proprietary information" means trade secrets as defined in 30-14-402 and includes business plans, marketing plans or strategies, customer lists, contracts, sales data, revenue, or other financial information";

in (1)(f)(ii) after "value" substituted "other than the purchase price" for "for the items"; inserted (1)(f)(iv) providing that a motorsports manufacturer may not coerce, threaten, intimidate, or require a motorsports dealer to order or accept delivery of a motorsports vehicle with special features unless the items are requested or ordered by the dealer or required by law; deleted former (11) that read: "(11) require a change in capital structure or means of financing for the dealership if the dealer at all times meets the reasonable, written, and uniformly applied capital standards determined by the manufacturer"; in (1)(g) at beginning inserted "require a change or", near middle after "dealer" inserted "at all times", and near end after "capital" substituted "standards" for "requirements"; deleted former (13) through (15) that read: "(13) unreasonably require the dealer to change the location or require any substantial alterations to the place of business;

(14) condition a renewal or extension of the franchise on the dealer's substantial renovation of the existing place of business or on the construction, purchase, acquisition, or re-lease of a new place of business unless written notice is first provided 180 days before the date of renewal or extension and the manufacturer demonstrates the reasonableness of the requested actions. The manufacturer shall agree to supply the dealer with an adequate quantity of motorsports vehicles, parts, and accessories to meet the sales level necessary to support the overhead resulting from substantial construction, acquisition, or lease of a new place of business.

(15) coerce, threaten, intimidate, or require, either directly or indirectly, a dealer to order or accept delivery of a motorsports vehicle with special features, accessories, or equipment not included in the list price of the vehicle as advertised by the manufacturer, except items:

(a) that have been voluntarily requested or ordered by the dealer; and

(b) required by law"; in (1)(h) after "including" substituted "attorney fees and costs incurred by a motorsports dealer" for "lawsuits and court costs"; in (1)(h)(i) at beginning inserted "any lawsuit relating to" and near end after "vehicle" substituted "part, or accessory if there is no allegation" for "without"; in (1)(i) at end substituted "products" for "vehicle"; in (1)(j) at end after "manufacturer" deleted "on grounds that a new motorsports vehicle or a prior year's model is in the dealer's inventory at the time of introduction of new model motorsports vehicles"; in (1)(m) at end before "dealers" substituted "motorsports" for "franchised"; in (1)(o) at beginning inserted exception clause and near end after "dealer's" substituted "dealership" for "franchise"; in (1)(p) after "vehicles" inserted "to customers who reside"; deleted former (26) that read: "(26) use a manufacturer order or allocation formula that is not based on actual local area sales and local area market data"; and made minor changes in style.

Chapter 240 in temporary version inserted (1)(s) prohibiting a manufacturer from refusing to allocate, sell, or deliver motorsports vehicles, charging back or withholding payments or other things of value for which the motorsports dealer is otherwise eligible, and preventing the motorsports dealer from participating in any promotion, program, or contest under certain conditions; and inserted (2) providing that subsection (1) does not apply to a sale to a motorsports dealer for resale to a federal, state, or local governmental agency under certain circumstances. Amendment effective April 16, 2009, and terminates on occurrence of contingency.

Chapter 240 in version effective on occurrence of contingency inserted (1)(t) prohibiting a manufacturer from offering a program under certain conditions; inserted (1)(u) prohibiting a manufacturer from refusing to allocate, sell, or deliver motorsports vehicles, charging back or withholding payments or other things of value for which the motorsports dealer is otherwise eligible, and preventing the motorsports dealer from participating in any promotion, program, or contest under certain conditions; inserted (2) providing that subsection (1) does not apply to a sale to a motorsports dealer for resale to a federal, state, or local governmental agency under certain circumstances or to sales to a dealer pursuant to a manufacturer's promotional or incentive program under certain circumstances. Amendment effective on occurrence of contingency.

Applicability: Section 7, Ch. 240, L. 2009, provided: "[This act] applies to motorsports manufacturers and motorsports dealer transactions that occur on or after [the effective date of this section]." Effective April 16, 2009.

30-14-2503. Injunction — damages.

Compiler's Comments

2009 Amendment: Chapter 240 in (1) at beginning of first sentence after "A" substituted "motorsports dealer" for "person who is injured by a violation of 30-14-2502", in second sentence in two places substituted "motorsports manufacturer" for "defendant", at beginning of third sentence inserted "To obtain an injunction", after "necessary" inserted "for the motorsports dealer" and at end substituted "arising from the violation" for "to the plaintiff"; in (2) near beginning after "relief" substituted "any motorsports dealer who incurs pecuniary loss due to a violation of 30-14-2502 by a motorsports manufacturer is entitled to" for "the plaintiff may", after "recover" deleted "from the defendant", and at end substituted "pecuniary loss together with costs, including attorney fees" for "the amount of actual damages sustained plus attorney fees and costs of suit"; deleted former (3) that read: "(3) The proper place for trial of an action based on a claim of a violation of 30-14-2502 is the district court for Lewis and Clark County or the county in which the alleged violation occurred"; inserted (3) providing that a violation of 30-14-2502 also constitutes a violation of 30-14-103 and allowing the department to bring an action to restrain any unlawful act; and made minor changes in style. Amendment effective April 16, 2009.

Applicability: Section 7, Ch. 240, L. 2009, provided: "[This act] applies to motorsports manufacturers and motorsports dealer transactions that occur on or after [the effective date of this section]." Effective April 16, 2009.

Part 26
Credit Report Submission Prohibitions

Part Compiler's Comments

Erroneous Codification Instruction — Code Commissioner Correction: Section 3, Ch. 315, L. 2017, provided that this part was to be codified as an integral part of Title 30, chapter 14, part 1. The code commissioner has codified this section in Title 30, chapter 14, part 26, to more closely reflect the subject matter.

Effective Date: Section 4, Ch. 315, L. 2017, provided: "[This act] is effective on passage and approval." Approved May 4, 2017.

Retroactive Applicability: Section 5, Ch. 315, L. 2017, provided: "[This act] applies retroactively, within the meaning of 1-2-109, to reports as of [the effective date of this act] of ambulance bills incurred for services provided in the state prior to [the effective date of this act] and paid in part to the extent of an insurance policy or for which a record exists of a complaint made to the insurance commissioner's office prior to [the effective date of this act]." Effective May 4, 2017.

Preamble: The preamble attached to Ch. 315, L. 2017, provided: "WHEREAS, individuals in a medical crisis that requires ambulance services may be faced with unexpectedly high bills with the potential to propel them into bankruptcy even after their insurance, if they have any, has paid on the ambulance bills; and

WHEREAS, individuals are responsible for paying ambulance bills with vendors they have selected themselves but often individuals in highly critical medical emergencies are unable to make the decisions on who is providing their ambulance service yet they still are expected to pay a bill over which they had no control."

Part 27
Electrical Generation Facility Ownership Agreements

Part Compiler's Comments

2021 Codification Instruction: Section 3, Ch. 377, L. 2021, provided that sections 1 and 2 were to be codified in Title 30, chapter 14, part 1. The Code Commissioner has instead codified these sections as a separate new part.

30-14-2701. Definitions.

Compiler's Comments

Effective Date: Section 5, Ch. 377, L. 2021, provided: "[This act] is effective on passage and approval." Approved May 3, 2021.

Retroactive Applicability: Section 6, Ch. 377, L. 2021, provided: "[This act] applies retroactively, within the meaning of 1-2-109, to actions taken by an owner on or after January 1, 2021."

Code Commissioner Correction: To reflect the repeal of 15-24-3001 and the enactment of an identical definition of "electrical generation facility" in 75-20-104 by Ch. 13, L. 2021, the Code Commissioner in (2) substituted "75-20-104" for "15-24-3001".

Preamble: The preamble attached to Ch. 377, L. 2021, provided: "WHEREAS, electrical generation facilities located in Montana have significant implications for the economy, environment, and health and welfare of Montana consumers; and

WHEREAS, closure of electrical generation facilities without the unanimous consent of all co-owners threatens the reliable supply of electricity for Montanans; and

WHEREAS, failure or refusal to fund operations of Montana electrical generation facilities by facility owners without the consent of all owners threatens the safety of workers at the facility, threatens Montana's interest in environmental remediation of the facility, and threatens the reliable supply of electricity for Montana consumers; and

WHEREAS, electrical generation facility owners who fail to fund their share of operating costs without the unanimous consent of all co-owners or seek closure of an electrical generation facility without the unanimous consent of all co-owners of the facility place on Montana local government units and Montana electricity consumers the burdens of disruption in facility operations or closure of the facility; and

WHEREAS, Montana statute prohibits unfair or deceptive acts or practices in the conduct of trade or commerce in accordance with section 30-14-103, MCA, and provides for civil action by the Department of Justice to enforce compliance with statute and for temporary, preliminary, and permanent injunctive relief and civil fine."

Severability: Section 4, Ch. 377, L. 2021, was a severability clause.

30-14-2702. Unfair or deceptive acts or practices — ownership agreement.

Compiler's Comments

Effective Date: Section 5, Ch. 377, L. 2021, provided: "[This act] is effective on passage and approval." Approved May 3, 2021.

Retroactive Applicability: Section 6, Ch. 377, L. 2021, provided: "[This act] applies retroactively, within the meaning of 1-2-109, to actions taken by an owner on or after January 1, 2021."

Preamble: The preamble attached to Ch. 377, L. 2021, provided: "WHEREAS, electrical generation facilities located in Montana have significant implications for the economy, environment, and health and welfare of Montana consumers; and

WHEREAS, closure of electrical generation facilities without the unanimous consent of all co-owners threatens the reliable supply of electricity for Montanans; and

WHEREAS, failure or refusal to fund operations of Montana electrical generation facilities by facility owners without the consent of all owners threatens the safety of workers at the facility, threatens Montana's interest in environmental remediation of the facility, and threatens the reliable supply of electricity for Montana consumers; and

WHEREAS, electrical generation facility owners who fail to fund their share of operating costs without the unanimous consent of all co-owners or seek closure of an electrical generation facility without the unanimous consent of all co-owners of the facility place on Montana local government units and Montana electricity consumers the burdens of disruption in facility operations or closure of the facility; and

WHEREAS, Montana statute prohibits unfair or deceptive acts or practices in the conduct of trade or commerce in accordance with section 30-14-103, MCA, and provides for civil action by the Department of Justice to enforce compliance with statute and for temporary, preliminary, and permanent injunctive relief and civil fine."

Severability: Section 4, Ch. 377, L. 2021, was a severability clause.

Part 28

Consumer Data Privacy Act

Part Compiler's Comments

Effective Date: Section 14, Ch. 681, L. 2023, provided that this part is effective October 1, 2024.

30-14-2817. Enforcement.

Compiler's Comments

Termination: Section 15, Ch. 681, L. 2023, provided: "[Section 12(2)] [30-14-2817(2)] terminates April 1, 2026."

CHAPTER 15
FOREIGN-TRADE ZONES

Part 1
General Provisions

30-15-104. Taxation of corporations operating foreign-trade zones and their goods.

Compiler's Comments

1985 Amendment: Deleted former (1) that read "All goods held in a foreign trade zone are subject to inventory taxation."

CHAPTER 16
SMALL BUSINESS
LICENSING COORDINATION

Chapter Administrative Rules

Title 42, chapter 8, ARM Board of Review — eStop business licenses.

Part 1
General Provisions

30-16-102. Purpose.

Compiler's Comments

1991 Amendment: In (1), at beginning after "eliminate", deleted "retail, wholesale, consumer service, manufacturer, and distributor"; inserted (4) relating to acquisition and maintenance of licenses necessary to conduct business; and made minor changes in style. Amendment effective May 16, 1991.

Saving Clause: Section 5, Ch. 744, L. 1991, was a saving clause.

Severability: Section 6, Ch. 744, L. 1991, was a severability clause.

Administrative Rules

ARM 42.8.106 Electronic submission of documents and electronic signatures.

30-16-103. Definitions.

Compiler's Comments

2003 Amendment: Chapter 405 in definition of license at end of (a) substituted "15-6-225" for "90-4-102". Amendment effective October 1, 2003.

2001 Amendment: Chapter 591 in definition of license at end of (a) inserted "including the production of energy using an alternative renewable energy source as defined in 90-4-102". Amendment effective July 1, 2001.

Severability: Section 28, Ch. 591, L. 2001, was a severability clause.

1999 Amendment: Chapter 54 in (2) substituted "department of revenue" for "department of commerce" and substituted "2-15-1301" for "2-15-1801"; in (3)(b) after "Title 75" inserted "chapters 1 through 3, 5 through 7, 10, 15, 16, and 20"; and made minor changes in style. Amendment effective March 15, 1999.

1997 Amendment: Chapter 366 in definition of Board of Review, after "department", inserted "of revenue"; and in definition of plan, after "system", substituted "and the procedures developed by the board of review that are" for "document, which is" and at end inserted "of revenue".

1997 Statement of Intent: The statement of intent attached to Ch. 366, L. 1997, provided: "A statement of intent is required for this bill because [section 1] [30-16-104] grants rulemaking authority to the board of review established in 30-16-302 for the purpose of implementing a one-stop business licensing pilot project required by the 54th Legislature."

1995 Amendment: Chapter 355 inserted definition of Board of Review; in definition of license, in (b) after "Title 75", deleted "and Title 80"; in definition of person, after "cooperative", inserted "limited liability company"; inserted definition of plan; and made minor changes in style. Amendment effective July 1, 1995.

Severability: Section 6, Ch. 355, L. 1995, was a severability clause.

1991 Amendment: Inserted definitions of Department and person; and made minor changes in style. Amendment effective May 16, 1991.

Saving Clause: Section 5, Ch. 744, L. 1991, was a saving clause.

Severability: Section 6, Ch. 744, L. 1991, was a severability clause.

Administrative Rules

Title 42, chapter 8, ARM Board of Review — eStop business licenses.

30-16-104. Rulemaking.

Compiler's Comments

1997 Statement of Intent: The statement of intent attached to Ch. 366, L. 1997, provided: "A statement of intent is required for this bill because [section 1] [30-16-104] grants rulemaking authority to the board of review established in 30-16-302 for the purpose of implementing a one-stop business licensing pilot project required by the 54th Legislature."

Administrative Rules

ARM 42.8.106 Electronic submission of documents and electronic signatures.

Part 2
Licensing Coordination Center

30-16-201. Designation of small business licensing coordination center — duties of center.

Compiler's Comments

2005 Amendment: Chapter 427 in (6) inserted second sentence requiring that the center immediately inform each business enterprise applying for a license that the business enterprise is required to obtain a business name from the secretary of state before any other state license application may be processed; and made minor changes in style. Amendment effective October 1, 2005.

1999 Amendment: Chapter 51 deleted former (13) that read: "(13) on January 4, 1993, present a report to the legislature containing its analysis and recommendations as required in subsections (1) through (4)"; and made minor changes in style. Amendment effective March 15, 1999.

1991 Amendment: In first sentence substituted "department shall" for "governor shall designate an agency to"; in (7) substituted "business community" for "businessman"; and inserted (13) requiring report to Legislature. Amendment effective May 16, 1991.

Saving Clause: Section 5, Ch. 744, L. 1991, was a saving clause.

Severability: Section 6, Ch. 744, L. 1991, was a severability clause.

Administrative Rules

ARM 42.8.102 eStop business licensing guide.

ARM 42.8.103 Anniversary dates established by department.

ARM 42.8.104 Responsibilities.

ARM 42.8.105 Pro-rating license fees.

30-16-204. Authority to issue licenses.

Compiler's Comments

Saving Clause: Section 5, Ch. 744, L. 1991, was a saving clause.

Severability: Section 6, Ch. 744, L. 1991, was a severability clause.

Effective Date: Section 8, Ch. 744, L. 1991, provided: "[This act] is effective on passage and approval." Approved May 16, 1991.

Part 3
Business Registration and Licensing — Board of Review

30-16-301. Business registration and licensing plan — administration.

Compiler's Comments

2011 Amendment: Chapter 26 in (1) in introductory clause in two places after "30-12-203" deleted "30-13-203, 30-13-206, 30-13-210, 30-13-217"; and made minor changes in style. Amendment effective October 1, 2011.

2005 Amendment: Chapter 47 in (1)(c) at beginning substituted "payment of" for "credit card discounts in relation to" and at end inserted "by credit card, debit card, or other commercially acceptable means as provided in 15-1-231". Amendment effective October 1, 2005.

2003 Amendment: Chapter 474 in (1) in two places inserted references to 50-57-201 through 50-57-206 and 50-57-208; and made minor changes in style. Amendment effective January 1, 2004.

1999 Amendment: Chapter 54 in (2) after "department" deleted "of revenue" and substituted "an employee" for "a deputy director". Amendment effective March 15, 1999.

1997 Amendment: Chapter 366 substituted (1) setting out applicable statutes and license criteria for former (1) through (4) that read: "(1) Before January 1, 1997, the department shall develop a plan:

(a) to establish an information service detailing all state licenses that are required in order to engage in business in Montana and the locations for applying for those licenses; and

(b) for a uniform method by which all state agencies may identify businesses.

(2) The method developed under subsection (1)(b) must include a phased approach to:

(a) complete a requirements analysis and specification document, including an overview systems design;

(b) complete a detailed requirements analysis, including a general systems design;

(c) establish interagency procedures for effectuating the plan;

(d) select those licenses that will be included in the initial implementation of the plan and the date and manner in which the licenses will be integrated into the plan; and

(e) complete a cost-benefit analysis of the final implementation of the plan.

(3) The department shall on January 2, 1997, recommend to the legislature any statutory or budgetary changes for implementing the plan.

(4) Each state agency shall review its licenses and recommend to the legislature on January 2, 1997, those licenses that should be eliminated or consolidated and justify those that should be retained"; in (2), after "department", inserted "of revenue" and after "charge of" inserted "administering"; and made minor changes in style.

1997 Statement of Intent: The statement of intent attached to Ch. 366, L. 1997, provided: "A statement of intent is required for this bill because [section 1] [30-16-104] grants rulemaking authority to the board of review established in 30-16-302 for the purpose of implementing a one-stop business licensing pilot project required by the 54th Legislature."

Saving Clause: Section 5, Ch. 355, L. 1995, provided: "[Section 2] [30-16-301] does not affect rights and duties that matured, penalties that were incurred, or proceedings that were begun before [the effective date of this act]." Effective July 1, 1995.

Severability: Section 6, Ch. 355, L. 1995, was a severability clause.

Effective Date: Section 8, Ch. 355, L. 1995, provided that this section is effective July 1, 1995.

Administrative Rules

ARM 42.8.102 eStop business licensing guide.
ARM 42.8.103 Anniversary dates established by department.
ARM 42.8.104 Responsibilities.
ARM 42.8.105 Pro-rating license fees.

30-16-302. Board of review.

Compiler's Comments

2005 Amendment: Chapter 427 in (1) in third sentence after "human services" deleted "the secretary of state"; and made minor changes in style. Amendment effective October 1, 2005.

2001 Amendment — Coordination: Chapter 323 in (1) in second sentence substituted reference to department of labor and industry for reference to department of commerce and substituted "a member appointed by the president of the senate, and a member appointed by the speaker of the house" for "the president of the senate or a designee, and the speaker of the house or a designee and at end of third sentence inserted "by the governor"; and inserted (5) providing that board is attached to department of revenue for administrative purposes. Amendment effective April 21, 2001.

The amendments to this section made by sec. 1, Ch. 323, L. 2001, were replaced by sec. 2, Ch. 323, L. 2001, a coordination section.

The amendments to this section made by sec. 69, Ch. 483, L. 2001, were replaced by sec. 2, Ch. 323, L. 2001, a coordination section.

1999 Amendment: Chapter 7 in (1) in second sentence after "environmental quality" inserted "livestock", after "secretary of state" deleted "the director of the office of budget and program planning, the commissioner of labor and industry", and inserted third sentence allowing further appointment to the board of review upon request; deleted former (3)(d) that read: "(d) recommend, in questionable cases, whether a particular license falls within the scope of this chapter"; substituted language in (4) allowing the board of review to implement a plan for streamlined registration and licensing to include unspecified licenses for former language that read: "In developing a recommended plan for streamlined registration and licensing procedures, the board of review shall consider the experience gained from the consolidated employer registration process implemented by the department of revenue and the department of labor and industry"; and made minor changes in style. Amendment effective February 11, 1999.

1997 Amendment: Chapter 366 in (1), in second sentence after "department", inserted "of revenue".

1997 Statement of Intent: The statement of intent attached to Ch. 366, L. 1997, provided: "A statement of intent is required for this bill because [section 1] [30-16-104] grants rulemaking authority to the board of review established in 30-16-302 for the purpose of implementing a one-stop business licensing pilot project required by the 54th Legislature."

Severability: Section 6, Ch. 355, L. 1995, was a severability clause.

Effective Date: Section 8, Ch. 355, L. 1995, provided that this section is effective July 1, 1995.

Code Commissioner Change: Pursuant to sec. 1, Ch. 546, L. 1995, the Code Commissioner substituted Department of Public Health and Human Services for Department of Social and Rehabilitation Services.

Pursuant to sec. 2, Ch. 546, L. 1995, the Code Commissioner substituted Department of Public Health and Human Services for Department of Family Services.

Pursuant to sec. 568, Ch. 546, L. 1995, the Code Commissioner substituted Department of Environmental Quality for Department of Health and Environmental Sciences.

Administrative Rules

ARM 42.8.102 eStop business licensing guide.
ARM 42.8.103 Anniversary dates established by department.
ARM 42.8.104 Responsibilities.
ARM 42.8.105 Pro-rating license fees.

Attorney General's Opinions

Legislator Prohibited From Appointment to Board of Review: Membership on the Board of Review established in this section is considered a public office of a civil nature pursuant to the five-part test in State ex rel. Barney v. Hawkins, 79 M 506, 257 P 411 (1927). Therefore, Art. V, sec. 9, Mont. Const., and 5-2-104 prohibit the President of the Senate and the Speaker of the House of Representatives from appointing a legislator as a member of the Board of Review, including appointment as a nonvoting member. Because of the prohibition against the appointment of a legislator to a civil office during the legislator's term of office, the President and Speaker may appoint only a nonlegislator as a member of the Board of Review. 49 A.G. Op. 15 (2002).

30-16-303. Participation of state agencies.

Compiler's Comments

2005 Amendment: Chapter 427 deleted former (1)(b) that read: "(b) the secretary of state"; and made minor changes in style. Amendment effective October 1, 2005.

2003 Amendment: Chapter 190 in (1)(a) after "departments of agriculture" deleted "commerce". Amendment effective April 1, 2003.

2001 Amendment: Chapter 116 at end of (4)(a) inserted "in an amount equal to no more than one-half of the total cost of processing and issuing a license"; inserted (4)(b) allowing the license applicant to be charged for remaining amount of the total cost of processing and issuing a license; and made minor changes in style. Amendment effective March 23, 2001.

1999 Amendment: Chapter 7 inserted (2) and (3) regarding inclusion of unspecified licenses in a plan for streamlined registration and licensing; inserted (4) regarding transfers of funds to defray costs associated with administration of streamlined registration and licensing; and made minor changes in style. Amendment effective February 11, 1999.

Severability: Section 6, Ch. 355, L. 1995, was a severability clause.

Effective Date: Section 8, Ch. 355, L. 1995, provided that this section is effective July 1, 1995.

Code Commissioner Change: Pursuant to sec. 1, Ch. 546, L. 1995, the Code Commissioner substituted Department of Public Health and Human Services for Department of Social and Rehabilitation Services.

Pursuant to sec. 2, Ch. 546, L. 1995, the Code Commissioner substituted Department of Public Health and Human Services for Department of Family Services.

Pursuant to sec. 568, Ch. 546, L. 1995, the Code Commissioner substituted Department of Environmental Quality for Department of Health and Environmental Sciences.

Administrative Rules

ARM 42.8.101 eStop licensing — definitions.
ARM 42.8.102 eStop business licensing guide.

ARM 42.8.103 Anniversary dates established by department.
ARM 42.8.104 Responsibilities.
ARM 42.8.105 Pro-rating license fees.

CHAPTER 17
ELECTRONIC DIRECTORY OF MONTANA PRODUCTS

Part 1
General Provisions

Part Compiler's Comments

Effective Date: This part is effective October 1, 2005.

Part Collateral References

Made in Montana, Montana Department of Commerce, https://madeinmontanausa.com.

30-17-101. Electronic directory of Montana products.

Compiler's Comments

2019 Amendment: Chapter 147 in (2)(a) at end substituted "2-6-1017" for "2-6-1017(1)". Amendment effective April 17, 2019.

2015 Amendment: Chapter 348 in (1)(a) and (2)(a) after "internet" deleted "or world wide web"; and in (2)(a) near end substituted "distribution list" for "mailing list" and substituted "2-6-1017(1)" for "2-6-109(1)". Amendment effective October 1, 2015.

Severability: Section 72, Ch. 348, L. 2015, was a severability clause.

Collateral References

Made in Montana, Montana Department of Commerce, https://madeinmontanausa.com.

CHAPTER 18
ELECTRONIC TRANSACTIONS

Part 1
Uniform Electronic Transactions Act

Part Compiler's Comments

Severability: Section 20, Ch. 52, L. 2001, was a severability clause.

Effective Date: Section 21, Ch. 52, L. 2001, provided: "[This act] is effective July 1, 2001."

Applicability: Section 22, Ch. 52, L. 2001, provided: "[This act] applies to any electronic record or electronic signature created, generated, sent, communicated, received, or stored on or after July 1, 2001."

Part Case Notes

Election Administrator Properly Rejected Electronic Signatures on Petition for Nomination of Independent Candidate — Acceptance of Electronic Signatures Not Required Under Election Laws or Uniform Electronic Transactions Act. Meyer v. Jacobsen, 2022 MT 93, 408 Mont. 369, 510 P.3d 52.

30-18-102. Definitions.

Compiler's Comments

2007 Amendment: Chapter 130 inserted definitions of cryptosystem and state agency; and made minor changes in style. Amendment effective October 1, 2007.

Preamble: The preamble attached to Ch. 130, L. 2007, provided: "WHEREAS, the 56th Montana Legislature adopted the Montana Electronic Transactions With State Agencies and Local Government Units Act in an effort to establish processes by which citizens, businesses, and other entities could effectively, efficiently, and legally transact official business with state and local governments through technology enabled by electronic means; and

WHEREAS, the 57th Montana Legislature adopted the Uniform Electronic Transactions Act in an effort to expand processes by which citizens, businesses, and other entities can effectively, efficiently, and legally transact official business through technology enabled by electronic means; and

WHEREAS, the adoption and implementation of the Uniform Electronic Transactions Act has eliminated the need for the Montana Electronic Transactions With State Agencies and Local Government Units Act."

Administrative Rules

ARM 42.8.106 Electronic submission of documents and electronic signatures.

30-18-103. Scope.

Compiler's Comments

2023 Amendment: See 2023 Session Law for amendment made by sec. 55, Ch. 647, L. 2023. Amendment effective May 19, 2023.

Applicability: Section 62, Ch. 647, L. 2023, provided: "(1) [This act] applies to statewide ballot issues submitted to the secretary of state on or after [the effective date of this act].

(2) [This act] applies to ballot issues submitted to the county election administrator for approval of the form of the petition required by 7-5-132 on or after [the effective date of this act].

(3) [This act] applies to a petition prepared pursuant to 7-7-2224 that is filed with the election administrator under 7-7-2225 on or after [the effective date of this act]." Effective May 19, 2023.

Saving Clause: Section 58, Ch. 647, L. 2023, was a saving clause.

Severability: Section 61, Ch. 647, L. 2023, was a severability clause.

2005 Amendment: Chapter 575 in (2)(b) after "30-1-107" deleted "and 30-1-206". Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

Case Notes

Election Administrator Properly Rejected Electronic Signatures on Petition for Nomination of Independent Candidate — Acceptance of Electronic Signatures Not Required Under Election Laws or Uniform Electronic Transactions Act. Meyer v. Jacobsen, 2022 MT 93, 408 Mont. 369, 510 P.3d 52.

30-18-106. Legal recognition of electronic records, electronic signatures, and electronic contracts.

Case Notes

Premarital Agreement — Allocation of 40% Ownership Interest in Brokerage Service Company Upheld: A wife argued that the District Court erred in allocating a 40% ownership interest in a brokerage service company to her husband. The Supreme Court held that the transfer was enforceable under 30-18-106 even though the wife had provided $280,000, which was transferred to the husband's separate checking account without an acknowledgment before a notary public. The $280,000 was a loan from the wife that was repaid in full. The $20,000 used to purchase the initial interest was a gift since no repayment schedule was ever executed and no consideration was requested. In addition, under 28-3-206, uncertainty is to be resolved against the party who caused the uncertainty to exist. With respect to the loan, the Supreme Court remanded after applying 31-1-106 and holding that the wife's loan of $280,000 was not interest-free. In re Marriage of Weiss, 2010 MT 188, 357 Mont. 320, 239 P.3d 123. In Weiss v. Weiss, 2011 MT 240, 362 Mont. 157, 261 P.3d 1034, the Supreme Court concluded that the District Court correctly determined on remand that the $280,000 loan was paid off in full by the husband and that the District Court's calculation of simple interest on the loan was correct.

30-18-115. Transferable records.

Compiler's Comments

2005 Amendment: Chapter 575 in (4) in first sentence near beginning substituted "30-1-201(2)(v)" for "30-1-201(20)"; and made minor changes in style. Amendment effective October 1, 2005.

Saving Clause: Section 92, Ch. 575, L. 2005, was a saving clause.

Applicability: Section 93, Ch. 575, L. 2005, provided: "[This act] applies to a document of title that is issued or a bailment that arises on or after [the effective date of this act]. [This act] does not apply to a document of title that is issued or a bailment that arises before [the effective date of this act] even if the document of title or bailment would be subject to [this act] if the document of title had been issued or bailment had arisen after [the effective date of this act]. [This act] does not apply to a right of action that has accrued before [the effective date of this act]." Effective October 1, 2005.

30-18-117. Acceptance and distribution of electronic records by governmental agencies.

Compiler's Comments

2013 Amendment: Chapter 123 in (1) and (3) substituted "30-18-111(6)" for "30-18-111(5)". Amendment effective October 1, 2013.

Administrative Rules

ARM 44.2.301 Acceptance of electronic records and electronic signatures.

30-18-118. Interoperability.

Compiler's Comments

2007 Amendment: Chapter 130 in (2) in first sentence at beginning substituted "Any state agency" for "The secretary of state" and at end after "part" deleted "for state government that are consistent with the provisions of Title 2, chapter 20" and in second sentence near middle after "cryptosystem" deleted "as defined in 2-20-103"; and made minor changes in style. Amendment effective October 1, 2007.

Preamble: The preamble attached to Ch. 130, L. 2007, provided: "WHEREAS, the 56th Montana Legislature adopted the Montana Electronic Transactions With State Agencies and Local Government Units Act in an effort to establish processes by which citizens, businesses, and other entities could effectively, efficiently, and legally transact official business with state and local governments through technology enabled by electronic means; and

WHEREAS, the 57th Montana Legislature adopted the Uniform Electronic Transactions Act in an effort to expand processes by which citizens, businesses, and other entities can effectively, efficiently, and legally transact official business through technology enabled by electronic means; and

WHEREAS, the adoption and implementation of the Uniform Electronic Transactions Act has eliminated the need for the Montana Electronic Transactions With State Agencies and Local Government Units Act."

CHAPTER 19
RENTAL AND RENTAL-PURCHASE AGREEMENTS

Part 1
Montana Rental-Purchase Agreement Act

Part Compiler's Comments

Severability: Section 14, Ch. 263, L. 2001, was a severability clause.

Effective Date: Section 15, Ch. 263, L. 2001, provided: "[This act] [30-19-101 through 30-19-104 and 30-19-109 through 30-19-116] is effective on passage and approval." Approved April 19, 2001.

Applicability: Section 16, Ch. 263, L. 2001, provided: "[This act] [30-19-101 through 30-19-104 and 30-19-109 through 30-19-116] applies to rental-purchase agreements that are entered into on or after [the effective date of this act]." Effective April 19, 2001.

CHAPTER 20
FIREARMS AND AMMUNITION MADE IN MONTANA

Part 1
Montana Firearms Freedom Act

Part Compiler's Comments

Applicability: Section 8, Ch. 205, L. 2009, provided: "[This act] applies to firearms, firearms accessories, and ammunition that are manufactured, as defined in [section 3] [30-20-103], and retained in Montana after October 1, 2009."

Effective Date: This part is effective October 1, 2009.

30-20-104. Prohibitions.

Case Notes

Finding That Commerce Clause Extends to Sale and Manufacture of Firearms That Could Be Sold Only in Montana Affirmed: Because Congress could rationally conclude that unlicensed firearms manufactured in Montana could make their way to and substantially affect the interstate market, federal regulation is within Congress's commerce power. Mont. Shooting Sports Ass'n v. Holder, 727 F3d 975 (9th Cir. 2013).

Preemption of MFFA Affirmed: Because the Montana Firearms Freedom Act (MFFA) attempts to circumvent federal law and conflicts with federal law, the MFFA ceases to be operative and is preempted and invalid. Mont. Shooting Sports Ass'n v. Holder, 727 F3d 975 (9th Cir. 2013).

Standing to Sue Affirmed: When a plaintiff has made specific allegations substantiating his plan to manufacture the "Montana Buckaroo" rifle, had experience in running his own shooting range equipment manufacturing business, and would incur economic costs if he were to comply with federal firearm manufacture licensing requirements, the plaintiff alleged injury sufficient to establish standing. Mont. Shooting Sports Ass'n v. Holder, 727 F3d 975 (9th Cir. 2013).

Part 2
Montana Ammunition Availability Act

Part Compiler's Comments

Severability: Section 13, Ch. 440, L. 2015, was a severability clause.

Effective Date: Section 14, Ch. 440, L. 2015, provided: "[This act] is effective on passage and approval." Chapter 440, L. 2015, was enacted into law without the governor's signature on May 6, 2015.

Applicability: Section 15, Ch. 440, L. 2015, provided: "[This act] applies to tax years beginning after December 31, 2015."

30-20-204. Property tax exemption for manufacturing of ammunition components — conditions — real property exemption applies to safety zone.

Compiler's Comments

2019 Amendment: Chapter 3 in (1)(a) substituted "15-10-109" for "15-10-108". Amendment effective October 1, 2019.

Termination: Section 16, Ch. 440, L. 2015, provided that this section terminates December 31, 2024.

Part 3
Financial Industry Nondiscrimination

30-20-301. Financial industry nondiscrimination — definitions.

Compiler's Comments

Effective Date: This section is effective October 1, 2023.

CHAPTER 22
NONFERROUS METAL TRANSACTIONS

Part 1
General Provisions

Part Compiler's Comments

Effective Date: This part is effective October 1, 2009.

30-22-101. Definitions.

Compiler's Comments

2023 Amendment: See 2023 Session Law for amendment made by sec. 3, Ch. 372, L. 2023. Amendment effective May 3, 2023.

2013 Amendment: Chapter 174 in definition of salvage metal dealer inserted "recycling"; and made minor changes in style. Amendment effective October 1, 2013.

Applicability: Section 4, Ch. 174, L. 2013, provided: "[This act] applies to offenses committed on or after [the effective date of this act]." Effective October 1, 2013.

30-22-102. Recordkeeping.

Compiler's Comments

2023 Amendment: See 2023 Session Law for amendment made by sec. 4, Ch. 372, L. 2023. Amendment effective May 3, 2023.

30-22-104. Sale of catalytic converters.

Compiler's Comments

Effective Date: Section 6, Ch. 372, L. 2023, provided: "[This act] is effective on passage and approval." Approved May 3, 2023.

CHAPTER 23
GENETIC INFORMATION PRIVACY

Part 1
Genetic Information Privacy Act

Part Compiler's Comments

Effective Date: This part is effective October 1, 2023.

CHAPTER 22
NONFERROUS METAL TRANSACTIONS

Part 1
General Provisions

Part Compiler's Comments

Effective Date: This part is effective October 1, 2009.

30-22-101. Definitions.

Compiler's Comments

2023 Amendment: See 2023 Session Law for amendment made by sec. 3, Ch. 372, L. 2023. Amendment effective May 3, 2023.

2013 Amendment: Chapter 174 in definition of salvage metal dealer inserted "recycling"; and made minor changes in style. Amendment effective October 1, 2013.

Applicability: Section 4, Ch. 174, L. 2013, provided: "[This act] applies to offenses committed on or after [the effective date of this act]." Effective October 1, 2013.

30-22-102. Recordkeeping.

Compiler's Comments

2023 Amendment: See 2023 Session Law for amendment made by sec. 4, Ch. 372, L. 2023. Amendment effective May 3, 2023.

30-22-104. Sale of catalytic converters.

Compiler's Comments

Effective Date: Section 6, Ch. 372, L. 2023, provided: "[This act] is effective on passage and approval." Approved May 3, 2023.

CHAPTER 23
GENETIC INFORMATION PRIVACY

Part 1
Genetic Information Privacy Act

Part Compiler's Comments

Effective Date: This part is effective October 1, 2023.